The MetroHealth System
(A Component Unit of Cuyahoga County)

Financial Report
December 31, 2012 and 2011

Dave Yost • Auditor of State

Board of Trustees
MetroHealth System
2500 MetroHealth Drive
Cleveland, Ohio 44109-1998

We have reviewed the *Independent Auditor's Report* of the MetroHealth System, Cuyahoga County, prepared by McGladrey LLP, for the audit period January 1, 2012 through December 31, 2012. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The MetroHealth System is responsible for compliance with these laws and regulations.

Dave Yost
Auditor of State

June 5, 2013

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McGladrey

Independent Auditor's Report

To the Board of Trustees of
The MetroHealth System
Cleveland, Ohio

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities and the discretely presented component unit of The MetroHealth System (the System), a component unit of Cuyahoga County, Ohio, as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We did not audit the financial statements of the discretely presented component unit, The MetroHealth Foundation Inc. (the Foundation) which represents 100% of the assets and revenues of the discretely presented component unit. Those statements were audited by other auditors whose reports have been furnished to us, and our opinions, insofar as they relate to the amounts included for the Foundation are based solely on the reports of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the discretely presented component unit of The MetroHealth System as of December 31, 2012 and 2011, and the respective changes in financial position and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3–15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming opinions on the financial statements that collectively comprise the System's basic financial statements. The accompanying schedule of expenditures of federal awards as required by *Office of Management and Budget Circular A-133*, *Audits of States, Local Governments, and Non-Profit Organizations* is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our reports dated April 23, 2013 and April 24, 2012 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

McGladrey LLP

Cleveland, Ohio
April 23, 2013

Management's Discussion and Analysis

This section of The MetroHealth System's (the System) annual financial report presents management's discussion and analysis (MD&A) of the System's financial performance and provides an overall review of the System's financial position and activities as of and for the years ended December 31, 2012 and 2011. This discussion should be read in conjunction with the accompanying financial statements and footnotes. The discussion and analysis is designed to focus on current activities, resulting change, and currently known facts. The financial statements, footnotes, and this discussion and analysis are the responsibility of the System's management.

Overview of the Financial Statements

During 2011, the System elected early implementation of GASB Statement No. 62 – *Codification of Accounting and Financial Reporting Guidance contained in pre-November 1989 FASB and AICPA Pronouncements*. The Statement incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in certain FASB and AICPA pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements. GASB Statement No. 62 also eliminates the election made by the System under GASB Statement No. 20 – *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, to apply the provisions of all relevant pronouncements of the FASB Standards Codification, which did not conflict with or contradict GASB pronouncements.

The System's financial statements are prepared on the accrual basis in accordance with generally accepted accounting principles promulgated by the GASB. The System is structured as a single enterprise fund with revenues recognized when earned, not when received. Expenses are recognized when incurred, not when paid. Capital assets are capitalized and are depreciated (except land and construction in progress) over their useful lives. See the *Notes to Financial Statements* for a summary of the System's significant accounting policies.

Following this MD&A are the basic financial statements of the System together with the notes, which are essential to a complete understanding of the data. The System's basic financial statements are designed to provide readers with a broad overview of the System's finances.

The *Statement of Net Position* presents information on all the System's assets and liabilities, with the net amount reported as net position. Over time, increases and decreases in net position may serve as a useful indicator of the System's financial position.

The *Statement of Revenues, Expenses and Changes in Net Position* presents information showing how the System's net position changed during each year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of timing of related cash flows. Thus, revenues and expenses are reported in the statement for some items that will result in cash flows in future periods.

The *Statement of Cash Flows* relates to the flows of cash and cash equivalents. Consequently, only transactions that affect the System's cash accounts are recorded in this statement. A reconciliation is provided at the bottom of the *Statement of Cash Flows* to assist in the understanding of the difference between cash flows from operating activities and operating income or loss.

The accompanying financial statements of the System include the MetroHealth Medical Center, a short-term acute care and long-term rehabilitation facility; Broadway Medical Offices, Buckeye Health Center and MetroHealth outpatient community health facilities; MetroHealth Centers for Skilled Nursing Care, consisting of the Old Brooklyn Nursing Facility and The Elisabeth Severance Prentiss Center for Skilled Nursing Care; and several urban and suburban health centers.

The Old Brooklyn Nursing Facility (144 beds) was closed effective December 14, 2011. In 2012, the System sold 91 bed licenses for $1,247 and the remaining 53 licenses were sold in early 2013 for $668. The building has been converted for use as a rehabilitation facility.

The System is the public health care system for Cuyahoga County, Ohio (the County). It is organized and operated by its board of county hospital trustees (the Board) pursuant to Chapter 339 of the Ohio Revised Code. Until 2010, members of the Board were jointly appointed by the Board of County Commissioners of the County, and the senior judges of the Probate and Common Pleas Courts of the County. Effective January 2011, the County voters established a new form of government by charter (the Charter). Under the Charter, future members of the Board are appointed by the County Executive together with the senior judges of the Probate and Common Pleas Courts of the County, subject to confirmation by the County Council.

In accordance with GASB Statement No. 14, *The Financial Reporting Entity* and GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units,* the System's financial statements are included, as a discretely presented component unit, in the County's Consolidated Annual Financial Report (CAFR). A copy of the CAFR can be obtained from Mark A. Parks, Jr., Acting Fiscal Officer, County Administration Building, 1219 Ontario Street, Cleveland, Ohio 44113.

In accordance with GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, The MetroHealth Foundation, Inc. (Foundation) is presented as a discretely presented component unit in a separate column in the System's financial statements to emphasize that it is legally separate from the System. The Foundation is a not-for-profit organization supporting the System through fundraising. The Foundation is not included in the following Management's Discussion and Analysis section, but is included in greater detail in the financial statements and footnotes. In addition, MHS Holding LLC and MHS Purchasing LLC are presented as blended entity component units whose financial activity is included with the activities of the System.

Financial and Operating Highlights for 2012

- Outpatient visits increased 3.6% over prior year levels.
- Hospital patient days decreased 0.3% from the prior year.
- Inpatient and outpatient surgical volumes increased 6.2% from 2011 levels.
- Total net position increased by $13.9 million for the year.
- Emergency room visits decreased 1.0% from the prior year to 104,558 annual visits.
- The MetroHealth Rehabilitation Institute was relocated to the former Old Brooklyn Nursing Facility in late 2012, after renovations.

Financial and Operating Highlights for 2011

- Outpatient visits increased 6.9% over prior year levels.
- Hospital patient days increased 0.6% from the prior year.
- Inpatient and outpatient surgical volumes increased 4.5% from 2010 levels.
- Total net position decreased by $2.5 million for the year.
- Emergency room visits increased 6.0% from the prior year to 105,609 annual visits.
- The Old Brooklyn Nursing Facility was closed December 14, 2011.

Financial Analysis of the System at December 31, 2012 and 2011

The System's total assets increased by 0.7% to $780.9 million and total liabilities decreased 1.9% to $442.4 million in 2012. The System's total net position increased $13.9 million in 2012, or 4.3% from the prior year. Table 1 summarizes the System's Statements of Net Position on December 31, in years 2012, 2011 and 2010.

TABLE 1
THE METROHEALTH SYSTEM
STATEMENTS OF NET POSITION
(DOLLARS IN THOUSANDS)

	2012	2011	2010
Assets:			
Current assets	$ 149,695	$ 117,403	$ 143,763
Investments	282,343	306,954	256,084
Restricted assets	69,146	79,110	87,256
Capital assets	265,264	261,662	266,457
Other assets	14,482	10,504	8,876
Total assets	780,930	775,633	762,436
Liabilities:			
Current liabilities	114,583	127,286	111,176
Long-term liabilities	327,785	323,719	324,124
Total liabilities	442,368	451,005	435,300
Net position:			
Net investment in capital assets	64,477	54,306	55,731
Restricted, debt service payments	25,706	31,396	33,917
Unrestricted	248,379	238,926	237,488
Total net position	$ 338,562	$ 324,628	$ 327,136

Current Assets

Fiscal year 2012 ended with an increase in total current assets of $32.3 million or 27.5% compared to 2011. Cash and cash equivalents decreased $0.2 million from normal business activity. Net patient accounts receivable increased $4.1 million or 5.3% from the prior year. Other non-patient receivables increased by $29.0 million to $52.4 million in 2012. A receivable related to the Hospital Care Assurance Program (HCAP) totaling $33.4 million was outstanding at the end of 2012 and was received in the first quarter of 2013. The balance has historically been received by the end of the fourth quarter. Also included in other receivables is $8.4 million due to the System for participation in the State of Ohio's supplemental Medicaid program that provides access to available funding up to 100% of the Medicare upper payment limit for inpatient hospital services (UPL Program). The outstanding UPL balance represents a decrease of $4.1 million or 33.2% from the prior year.

In 2012, medical and non-medical supplies inventories were up 3.9% and prepaid expenses decreased $1.0 million to $2.6 million. The decrease in prepaid expenses is related to large information technology invoices paid prior to 2012 that are nearing the end of their expense amortization schedule. Annual prepaid insurance policies were again processed in January instead of the normal December payment cycle.

Fiscal year 2011 ended with a decrease in total current assets of $26.4 million or 18.3% compared to 2010. Cash and cash equivalents increased $0.8 million from normal business activity. Net patient accounts receivable increased $9.2 million or 13.3% from the prior year. Other non-patient receivables decreased by $34.3 million to $23.4 million in 2011. A HCAP receivable totaling $35.2 million was outstanding at the end of 2010 and was received in the first quarter of 2011. The balance has been historically received by the end of the fourth quarter. Also included in other receivables is a $12.5 million UPL Program receivable. The outstanding UPL balance represents an increase of $1.4 million or 12.7% from the prior year.

In 2011, medical and non-medical supplies inventories were up 1.7% and prepaid expenses decreased $2.2 million to $3.6 million.

Investments

In 2012, total investments decreased $24.6 million or 8.0% from the prior year. Board designated general investments decreased by $32.2 million or 20.4%, Academic fund balances decreased by $0.4 million or 1.3% and the Depreciation Reserve fund increased $8.0 million or 6.7%. The Board designated general investments decrease of $32.2 million is mostly attributed to $33.4 million in HCAP payments normally received in the fourth quarter that were received in the first quarter of 2013. The Depreciation Reserve fund increase results from annual funding requirements of $5.9 million, investment returns of $2.6 million and a mark to market adjustment decrease of $0.5 million.

In 2011, total investments increased $50.9 million or 19.9% from the prior year. General Board designated investments increased by $42.1 million or 36.4%, Academic fund balances decreased by $0.7 million or 2.3% and the Depreciation Reserve fund increased $9.5 million or 8.6%. The Board designated general investments increase of $42.1 million is mostly attributed to a $35.2 million HCAP payment received in the first quarter of 2011 for the 2010 program. The Depreciation Reserve fund increase results from higher annual funding requirements of $5.9 million, investment returns of $3.2 million and a mark to market adjustment increase of $0.3 million.

Restricted Assets

Restricted Assets includes restricted cash and cash equivalents, special purpose investments, and restricted assets under bond indenture agreements. In 2012, restricted assets decreased by $10.0 million to $69.1 million and is related to bond project fund draws of $4.8 million and debt service activity.

In 2011, restricted assets decreased by $8.1 million to $79.1 million and is related to bond project fund draws of $5.8 million and debt service funding activity.

Capital Assets

In 2012, capital expenditures totaled $29.8 million, a $3.1 million increase from 2011. Expenditures on the larger projects include $4.5 million for the Middleburg Heights Family Health Center, $2.9 million for the Imaging Center expansion, $1.6 million for the hospital enterprise software licensing and implementation project, $1.4 million for the replacement of MetroHealth Drive, $1.3 million to renovate the Old Brooklyn post acute facility for usage as a rehabilitation center, $1.1 million for information technology infrastructure, and $0.9 million for roof replacements. The System's 2012 capital expenditures were from operating funds and Series 2009B Project Funds.

In 2011, capital expenditures totaled $26.7 million, a $7.7 million increase from 2010. Expenditures on the larger projects include $2.2 million for Retherm Systems, $2.4 million for IV pump replacements, $1.7 million for radiology oncology facility upgrades and $1.2 million for HVAC equipment upgrades. The System's 2011 capital expenditures were from operating funds and Series 2009B Project Funds.

Other Assets

In 2012, other assets totaled $14.5 million, an increase of $4.0 million from 2011. Included in other assets are the System’s investments in blended component units, deferred bond financing costs, long-term prepaid expenses and long-term other receivables. Growth in other assets is attributed to a $3.4 million increase in the value of the MHS Holdings LLC investment, and the 2012 transfer of the MetroHealth Foundation’s interest in Premier Purchasing Partners, L.P. to the System. The investment (MHS Purchasing LLC), now held by the System, was valued at $0.6 million at the end of 2012. Addition information is found in the notes to the financial statements.

In 2011, other assets totaled $10.5 million, an increase of $1.6 million from the prior year. In 2011, the System formed an entity (MHS Holdings LLC) to acquire and own interests in certain health care businesses. The value of MHS Holdings LLC at the end of 2011 was $6.6 million. Additional information is available in the notes to the financial statements. Long-term prepaid expenses and deferred financing costs decreased by a total of $0.9 million, primarily from scheduled expense amortization.

Current Liabilities

In 2012, total current liabilities decreased $12.7 million or 10.0% from the prior year. Current liabilities categories experiencing large decreases include accrued payroll and related liabilities, contribution payable to the public employees retirement system (PERS), and current installment of long-term liabilities. Accrued payroll and related liabilities decreased $13.1 million and is related to scheduled payroll payment dates (timing of payments). Contribution payable to the PERS category decreased $3.4 million and is attributed to larger January 2012 payments from November and December 2011 activity. Normally there is a one month payment lag. Current installments of long-term liabilities decreased $6.1 million primarily from a bond refunding escrow payment of $5.9 million payable in 2012. Current liabilities categories that experienced large increases include $6.8 million in accounts payable, and $5.4 million in other current liabilities. The higher accounts payable balance is related to higher capital project accruals and normal business activity. Other current liabilities growth is attributed to accrued amounts payable for state franchise fees and HCAP Program assessments. Growth of these two liabilities totaled $6.5 million and is attributed to timing of payments and larger amounts due.

In 2011, total current liabilities increased $16.1 million or 14.5% from the prior year. Current liabilities accounts that experienced large increases include $4.3 million in additional accrued payroll and related liabilities, $3.8 million in the contribution payable to the PERS, $3.3 million in self-insurance liabilities, and a $7.0 million increase in current installments of long-term debt. The higher payroll accrual is related to normal payroll processing cycles. The 2011 PERS liability includes two months instead of the normal one month payment lag. The current installments of long-term debt increase is related to a fourth quarter Bond refunding and issue where higher principal payments are due resulting from the debt restructure. Liability categories that experienced decreases include other current liabilities, $3.6 million, and the accrued interest payable, $1.0 million. The other current liabilities category decrease of $3.6 million is related to an HCAP Program assessment that was outstanding at the end of 2010 that is generally paid prior to each year end.

Long-Term Liabilities

In 2012, total long-term liabilities, less current installments, increased $4.0 million or 1.3% from the prior year. Long term self-insurance liabilities increased by $6.0 million or 18.9% and the accrued vacation and sick leave liability increased by $3.2 million or 9.7% from the prior year. The increase in self-insurance liabilities is related to higher expected malpractice and workers' compensation claims per the independent actuarial reports. Long-term debt decreased by $5.0 million.

In 2011, total long-term liabilities, less current installments, decreased $0.4 million or 0.1% from the prior year. Long-term debt decreased by $16.0 million or 6.3%, estimated amounts due to third-party payors declined by $1.7 million or 30.3%, and the accrued vacation and sick leave liability decreased by $1.3 million or 3.8% from the prior year. The derivative instruments – rate swaps increased by $11.9 million, and the self-insurance liabilities increased by $6.6 million or 26.2% from the prior year.

The large decrease in long-term debt is related to a revised debt service payment schedule resulting from the System's fourth quarter Series 2011 Refunding Bond issue where higher principal payments are due in 2012 thus classified in current liabilities. Additional information regarding the System's long-term debt can be found in Note 5 of the Financial Statements. Growth in other long-term liabilities of $11.9 million resulted from unfavorable market adjustments on the System's two interest SWAP agreements that are linked to its long-term debt. The increase in self-insurance liabilities is related to higher expected malpractice and workers' compensation claims per the independent actuarial reports.

TABLE 2
THE METROHEALTH SYSTEM
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
(DOLLARS IN THOUSANDS)

	Years ended December 31, 2012	2011	2010
Revenues:			
Operating revenues			
Net patient service revenue	$ 683,263	$ 665,917	$ 643,024
Other revenue	58,970	60,039	57,686
	742,233	725,956	700,710
Non-operating revenues			
County appropriation	36,029	36,031	39,907
Investment income	4,803	5,611	6,202
Unrealized (loss) income on investments	(934)	(11,664)	(2,948)
Other revenue	4,620	5,972	5,830
Grants and donations	3,289	3,995	4,087
Grants for capital acquisitions	51	680	700
	47,858	40,625	53,778
Total revenues	790,091	766,581	754,488
Expenses:			
Operating expenses			
Salaries and wages	426,900	419,376	399,399
Employee benefits	96,554	98,201	90,107
Purchased services	41,172	43,515	48,107
Medical supplies	50,607	47,625	39,265
Pharmaceuticals	31,559	32,859	31,033
Plant operations	27,468	27,615	25,934
Non-medical supplies	14,096	14,877	14,401
Other expenses	21,423	17,362	16,481
Insurance	18,606	18,510	13,239
Depreciation and amortization	31,402	31,528	32,098
	759,787	751,468	710,064
Non-operating expenses			
Grant expenses and support	3,522	3,890	4,551
Interest expense	12,848	13,731	13,240
	16,370	17,621	17,791
Total expenses	776,157	769,089	727,855
Increase (decrease) in net position	13,934	(2,508)	26,633
Total net position--beginning of the year	324,628	327,136	300,503
Total net position--end of the year	$ 338,562	$ 324,628	$ 327,136

The System's total operating and non-operating revenues in 2012 were $790.1 million while operating and non-operating expenses totaled $776.2 million. This resulted in a net position increase of $13.9 million for the year. This compares to the 2011 net position decrease of $2.5 million from total revenues of $766.6 million and total expenses of $769.1 million.

Operating Revenues

2012 Activity

In 2012, operating revenues increased $16.3 million or 2.3% from the prior year. Net patient service revenue increased $17.3 million or 2.7% and other operating revenues decreased $1.0 million or 1.8% from 2011 levels. The net patient revenue increase between 2011 and 2012 is attributed to higher outpatient volume growth, strategic pricing and a $4.0 million settlement from the Centers for Medicare & Medicaid Services (CMS) for an error in the Rural Budget Neutrality adjustment factor used in 1998.

The System's patient volumes were mixed when compared to 2011 levels. Hospital patient days decreased 0.3%, discharges were up 3.1%, inpatient surgeries increased 5.6% and deliveries increased 1.0%. Outpatient visits were up 3.6% from 2011 results. Emergency room visits decreased 1.0% and outpatient surgical volumes increased 6.6% from the prior year.

Gross patient revenues increased $61.2 million or 3.0% from the prior year but were mostly offset with higher contractual and denial adjustments of $25.6 million and additional uncompensated care of $30.7 million. The System’s level of uncompensated care continues to reflect the System’s status as a safety net facility in Cuyahoga County. Hospital Care Assurance (HCAP) and Upper Payment Limit (UPL) program revenues, also components of net patient revenue, increased by $6.5 million or 12.1% from 2011 levels. HCAP and UPL programs are discussed in further detail in the System’s financial statement’s notes. Prior year settlement adjustments, also affecting net patient revenue, totaled $10.0 million, an increase of $6.0 million from the prior year.

2011 Activity

In 2011, operating revenues increased $25.2 million or 3.6% from the prior year. Net patient service revenue increased $22.9 million or 3.6% and other operating revenues increased $2.4 million or 4.1% from 2010 levels. The net patient revenue increase between 2010 and 2011 is mostly attributed to volume growth, strategic pricing and optimized charge capture.

The System's patient volumes were generally higher when compared to 2010 levels. Hospital patient days increased 0.6%, discharges were down 0.6%, inpatient surgeries increased 4.5% and deliveries declined 1.9%. Outpatient visits were up 6.9% from 2010 results. Emergency room visits increased 6.0% and outpatient surgical volumes increased 4.5% from the prior year.

Gross patient revenues increased $169.8 million or 9.2% from the prior year but were mostly offset with higher contractual and denial adjustments of $93.0 million and additional uncompensated care of $41.8 million. Hospital Care Assurance (HCAP) and Upper Payment Limit (UPL) program revenues, also components of net patient revenue, decreased by $2.4 million or 4.3% from 2010 levels. Prior year settlement adjustments, also affecting net patient revenue, totaled $4.0 million, a decrease of $9.6 million from the prior year.

Non-Operating Revenues

2012 Activity
In 2012, non-operating revenues totaled $47.9 million, an increase of $7.2 million or 17.8% from the prior year. Non-operating revenues include county appropriation revenue of $36.0 million, investment income of $4.8 million, unrealized investment losses of $0.9 million, other non-operating revenue of $4.6 million, and grants and donations of $3.3 million.

Investment income was lower by $0.8 million from the prior year as a result of continued, historically low interest rates. Unrealized losses on investments decreased by $10.7 million from the prior year which relates to stable market value changes in 2012 on the System's two interest rate SWAP agreements, after a large unfavorable swing in 2011. Other non-operating revenues and grant revenues were both down $1.4 million and $1.3 million, respectively from 2011 levels.

2011 Activity
In 2011, non-operating revenues totaled $40.6 million, a decrease of $13.2 million or 24.5% from the prior year. Non-operating revenues include county appropriation revenue of $36.0 million, investment income of $5.6 million, unrealized investment losses of $11.7 million, other non-operating revenue of $6.0 million, and grants and donations of $4.7 million.

County appropriation revenue decreased 9.7% from $39.9 million in 2010. Investment income was lower by $0.6 million from the prior year due to interest rates remaining historically low. Unrealized investment losses increased by $8.7 million, which relates to the market value changes of the System's two interest rate SWAP agreements. Grant revenues and other non-operating revenues were up slightly from 2010.

Operating Expenses

The following table summarizes the System's operating expenses in the last three years. The System's total operating expenses increased in 2012 by $8.3 million or 1.1% from 2011 and increased in 2011 by $41.4 million or 5.8% from 2010.

TABLE 3
THE METROHEALTH SYSTEM
OPERATING EXPENSES
(DOLLARS IN THOUSANDS)

	2012	2011	2010
Operating expenses:			
Salaries and wages	$ 426,900	$ 419,376	$ 399,399
Employee benefits	96,554	98,201	90,107
Purchased services	41,172	43,515	48,107
Medical supplies	50,607	47,625	39,265
Pharmaceuticals	31,559	32,859	31,033
Plant operations	27,468	27,615	25,934
Non-medical supplies	14,096	14,877	14,401
Other expenses	21,423	17,362	16,481
Insurance	18,606	18,510	13,239
Depreciation and amortization	31,402	31,528	32,098
Total operating expenses	$ 759,787	$ 751,468	$ 710,064

2012 Activity

In 2012, salaries and wages were $426.9 million, an increase of $7.5 million or 1.8% from the prior year. The small increase between years is attributed to a 3.0% general wage increase, offset by reductions in FTE's.

Employee benefits expense in 2012 was $96.6 million, a decrease of $1.6 million or 1.7% from 2011. Health care benefits decreased $0.7 million, unemployment compensation decreased $1.2 million and tuition and education expenses increased by $0.2 million.

Purchased services expenses were $41.2 million in 2012, a decrease of $2.3 million, or 5.4% from 2011. Consulting services declined by $3.3 million or 46.2% from the prior year. Legal fees were also lower, down by $0.7 million, or 69.5% from the prior year. Information technology service contracts, other service contracts and software licensing expenses were higher by $1.3 million or 9.0% from the prior year.

Medical supplies expenses were $50.6 million in 2012, an increase of $3.0 million or 6.3% from the prior year. Pharmaceutical expenses were $31.6 million, a decrease of $1.3 million or 4.0% from 2011.

Plant operations expenses were $27.5 million, a decrease of $0.1 million or 0.5% from 2011. Utility costs declined by $1.3 million from the prior year but were offset by higher helicopter support costs of $0.5 million, higher telecommunication costs of $0.4 million and higher leased space costs of $0.5 million.

Non-medical supplies totaled $14.1 million, a decrease of $0.8 million or 5.2%. Department supplies were down $0.4 million from the prior year.

Other expenses were $21.4 million, an increase of $4.1 million or 23.4% from 2011. The 2012 state franchise fee assessment of $10.2 million was $2.8 million higher than in 2011 and was the largest single contributor of the increase. Advertising and miscellaneous expenses both increased by $0.2 million.

Insurance expenses were $18.6 million, an increase of $0.1 million from the prior year. Depreciation and amortization expenses were $31.4 million, a decrease of $0.1 million from the prior year.

<u>2011 Activity</u>
In 2011, salaries and wages were $419.4 million, an increase of $20.0 million or 5.0% from the prior year. The increase is primarily attributed to restructuring of physician productivity-based incentive programs, and strategic physician hires and FTE growth.

Employee benefits expense in 2011 was $98.2 million, an increase of $8.1 million or 9.0% from 2010. Health care benefits increased $4.6 million, unemployment compensation increased $0.8 million and workers' compensation expenses decreased $0.5 million. System contributions to the Ohio Public Employee Retirement System (OPERS) increased $2.4 million on higher salaries and wages.

Purchased services expenses were $43.5 million in 2011, decreasing $4.6 million, or 9.5% from 2010. Consulting services declined by $9.1 million or 55.7% after a robust expense year in 2010. Department purchased services increased $2.8 million, or 18.6% from the prior year. Information technology service contracts, other service contracts and software licensing expenses were higher by $1.6 million or 12.9% from 2010.

Medical supplies expenses were $47.6 million in 2011, an increase of $8.4 million or 21.3% from the prior year. Pharmaceutical expenses were $32.9 million, an increase of $1.8 million or 5.9% from 2010.

Plant operations expenses were $27.6 million, an increase of $1.7 million or 6.5% from 2010 levels. The increase is related to a one-time asbestos abatement credit of $2.3 million taken in 2010 (not available in 2011), and lower electrical utility costs of $1.1 million.

Non-medical supplies totaled $14.9 million, an increase of $0.5 million or 3.3% from 2010. Facilities maintenance supplies and nutrition services food purchases were each higher by $0.2 million in 2011.

Other expenses were $17.4 million, an increase of $0.9 million or 5.3%. The 2011 state franchise fee assessment of $7.4 million was $1.5 million higher than in 2010. Property taxes decreased by $0.6 million in 2011. 2010 property taxes were unusually high from a one-time adjustment.

Insurance expenses were $18.5 million, an increase of $5.3 million or 39.8% from the prior year. The increase is mostly related to higher expected malpractice claims per the 2011 independent actuarial report. Depreciation and amortization expenses were $31.5 million, a decrease of $0.6 million, or 1.8% from the prior year.

Non-Operating Expenses

Non-operating expenses, which include specific purpose fund expenses (grant expenses) and interest expense, decreased $1.3 million or 7.1% from 2011 levels. Non-operating expenses were $16.4 million and $17.6 million in 2012 and 2011, respectively.

Interest expense in 2012 decreased by $0.8 million or 6.4% from 2011 and is related to saving from the 2011 debt restructure (Series 2011 Bonds), partially offset by higher swap interest costs of $0.5 million, and smaller capitalized interest credits. Interest expense in 2011 increased $0.5 million or 3.7% from 2010 and was related to lower capitalized interest from reduced capital spending.

Specific purpose fund expenses totaled $3.5 million, $3.9 million and $4.6 million in 2012, 2011 and 2010, respectively.

Economic Factors and Next Year's Budget

Several factors and uncertainties that are contained in the budget are:

- The System received approval February 5, 2013 from federal officials to launch MetroHealth Care Plus, a Medicaid waiver program that will provide a medical home and health coverage for up to 30,000 uninsured residents of Cuyahoga County. The MetroHealth Care Plus Program is the first in Ohio to provide healthcare coverage to more of the uninsured.

- The System has budgeted to receive an appropriation of approximately $36.0 million from the County in 2013. This funding level approximates the 2012 and 2011 appropriations but is a 10% reduction from amounts received in years 2008 through 2010.

- The System will continue to explore revenue enhancements, cost reductions and productivity improvements.

- Capital funds needed for replacement of depreciated equipment and facilities, and vital service-line growth and expansion, will require the use of the remaining Series 2009B project funds and unrestricted investments. In addition, efforts to obtain appropriate philanthropy to offset operational and capital needs will continue in 2013.

- The SFY 2012/2013 State budget carries forward the existing 2010/2011 Hospital Franchise Fee (HFF) and Upper Payment Limit (UPL) programs into the new biennium and further expands the supplemental payment program funded by the HFF for 2012 and 2013 to include Enhanced Medicaid Managed Care Organization (EMMCO) payments. The Governor's proposed SFY 2014/2015 State budget reauthorizes the hospital franchise fee program.

- In 2012, the System earned $31.1 million in gross inpatient and outpatient UPL dollars which includes approximately $6.8 million for EMMCO. The 2013 inpatient and outpatient UPL programs are expected to remain consistent with the 2012 program as it relates to the methodologies used to determine the distribution of funds. The UPL and EMMCO programs are funded by the state franchise fee program which the Governor has reauthorized in his proposed SFY 2014/2015 State budget.

- Net Hospital Care Assurance Program (HCAP) dollars recorded by the System in 2012 were $29.9 million, which included an additional, one-time amount of $2.3 million related to the closure of a hospital in Cuyahoga County. In 2013, no major changes are anticipated or planned related to HCAP Program funding or fund distribution methodologies; therefore the System's 2013 net distribution should approximate the 2012 amount, excluding the $2.3 million one-time transaction. The Governor's proposed SFY 2014/2015 State budget reauthorizes the HCAP program until October 2015.

The MetroHealth System
(A Component Unit of Cuyahoga County)

Statements of Net Position
December 31, 2012 and 2011
(Dollars in Thousands)

	The MetroHealth System		Component Unit The MetroHealth Foundation, Inc.	
Assets	**2012**	**2011**	**2012**	**2011**
Current Assets:				
Cash and cash equivalents	$ 3,065	$ 3,298	$ 161	$ -
Accounts receivable	98,499	93,008	1,551	1,539
Allowance for uncollectible accounts	(16,547)	(15,173)	(136)	(122)
	81,952	77,835	1,415	1,417
Other receivables	52,377	23,379	140	58
Supplies	9,662	9,297	-	-
Prepaid expenses	2,639	3,594	-	-
Total current assets	149,695	117,403	1,716	1,475
Noncurrent Assets:				
Investments:				
General	125,448	157,668	3,627	3,870
Academic funds	29,060	29,448	-	-
Depreciation reserve fund	127,835	119,838	-	-
	282,343	306,954	3,627	3,870
Restricted Assets:				
Cash and cash equivalents	85	88	2,689	3,778
Special purpose investments	5,556	5,556	26,559	23,315
Under bond indenture agreements	63,505	73,466	-	-
	69,146	79,110	29,248	27,093
Capital Assets:				
Land and construction in progress	21,361	16,401	-	-
Land improvements	11,649	11,619	-	-
Buildings and fixed equipment	544,631	536,007	-	-
Equipment	317,537	299,919	26	-
	895,178	863,946	26	-
Accumulated depreciation	(629,914)	(602,284)	(5)	-
	265,264	261,662	21	-
Other assets	14,482	10,504	-	-
Total assets	$ 780,930	$ 775,633	$ 34,612	$ 32,438

See Notes to Financial Statements.

The MetroHealth System
(A Component Unit of Cuyahoga County)

Statements of Net Position (Continued)
December 31, 2012 and 2011
(Dollars in Thousands)

	The MetroHealth System		Component Unit The MetroHealth Foundation, Inc.	
Liabilities	**2012**	**2011**	**2012**	**2011**
Current Liabilities:				
Accounts payable	$ 35,834	$ 29,062	$ 1,508	$ 2,054
Accrued payroll and related liabilities	21,426	34,493	-	-
Contribution payable to the Public Employees Retirement System	5,130	8,504	-	-
Accrued interest payable	3,617	3,315	-	-
Self-insurance liabilities	13,620	15,255	-	-
Estimated amounts due to third-party payors	4,206	5,029	-	-
Accrued vacation and sick leave	7,229	7,419	-	-
Current installments of long-term debt	9,675	15,772	-	-
Other current liabilities	13,846	8,437	427	550
Total current liabilities	114,583	127,286	1,935	2,604
Long-Term Liabilities, less current installments:				
Self-insurance liabilities	38,043	32,000	-	-
Estimated amounts due to third-party payors	4,097	3,839	-	-
Accrued vacation and sick leave	36,215	33,019	-	-
Derivative instruments - rate swaps	14,964	15,353	-	-
Long-term debt	234,466	239,508	-	-
Total long-term liabilities	327,785	323,719	-	-
Total liabilities	442,368	451,005	1,935	2,604
Net Position				
Net investment in capital assets	64,477	54,306	-	-
Restricted, debt service payments	25,706	31,396	-	-
Restricted, program activities	-	-	19,266	17,121
Restricted, nonspendable			9,756	8,998
Unrestricted	248,379	238,926	3,655	3,715
Total net position	$ 338,562	$ 324,628	$ 32,677	$ 29,834

See Notes to Financial Statements.

The MetroHealth System
(A Component Unit of Cuyahoga County)

Statements of Revenues, Expenses, and Changes in Net Position
Years Ended December 31, 2012 and 2011
(Dollars in Thousands)

	The MetroHealth System		Component Unit The MetroHealth Foundation, Inc.	
	2012	**2011**	**2012**	**2011**
Operating Revenues				
Net patient service revenue	$ 683,263	$ 665,917	$ -	$ -
Other revenue	58,970	60,039	-	-
Total operating revenues	742,233	725,956	-	-
Operating Expenses				
Salaries and wages	426,900	419,376	-	-
Employee benefits	96,554	98,201	-	-
Purchased services	41,172	43,515	-	-
Medical supplies	50,607	47,625	-	-
Pharmaceuticals	31,559	32,859	-	-
Plant operations	27,468	27,615	-	-
Non-medical supplies	14,096	14,877	-	-
Other expenses	21,423	17,362	-	-
Insurance	18,606	18,510	-	-
Total operating expenses before depreciation and amortization	728,385	719,940	-	-
Operating income before depreciation and amortization	13,848	6,016	-	-
Depreciation and amortization	31,402	31,528	-	-
Operating loss	(17,554)	(25,512)	-	-
Non-Operating Revenues (Expenses)				
County appropriation	36,029	36,031	-	-
Net investment income (loss)	3,869	(6,053)	4,025	234
Other non-operating revenue	4,620	5,972	-	-
Noncapital grants and donations	3,289	3,995	5,872	9,243
Grant expenses and support	(3,522)	(3,890)	(7,054)	(8,422)
Interest expense	(12,848)	(13,731)	-	-
Total non-operating revenues (expenses)	31,437	22,324	2,843	1,055
Income (loss) before capital contributions	13,883	(3,188)	2,843	1,055
Grants for capital acquisitions	51	680	-	-
Change in net position	13,934	(2,508)	2,843	1,055
Total net position - beginning of year	324,628	327,136	29,834	28,779
Total net position - end of year	$ 338,562	$ 324,628	$ 32,677	$ 29,834

See Notes to Financial Statements.

The MetroHealth System
(A Component Unit of Cuyahoga County)

Statements of Cash Flows
Years Ended December 31, 2012 and 2011
(Dollars in Thousands)

	2012	2011
Cash Flows from Operating Activities		
Patient service revenue	$ 652,791	$ 685,181
Other operating cash receipts	54,966	57,334
Payments to suppliers	(194,935)	(189,204)
Payments for compensation and benefits	(536,469)	(508,721)
Net cash flows (used in) provided by operating activities	(23,647)	44,590
Cash Flows from Noncapital Financing Activities		
County appropriation	36,029	36,031
Restricted grants, donations and other	6,781	7,817
Specific purpose funds expenses	(3,527)	(3,931)
Net cash flows provided by noncapital financing activities	39,283	39,917
Cash Flows from Capital and Related Financing Activities		
Grants for capital acquisition	51	680
Acquisitions and construction	(29,821)	(26,704)
Proceeds from sale of assets and insurance	1,307	894
Proceeds from long-term debt	24,710	67,455
Retirement of long-term debt	(24,710)	(67,956)
Principal payments on long-term debt	(16,021)	(8,535)
Interest payments on long-term debt	(11,595)	(14,225)
Build America Bond receipts	2,158	2,158
Payments of financing fees on long-term debt	(155)	(621)
Net cash flows used in capital and related financing activities	(54,076)	(46,854)
Cash Flows from Investing Activities		
Payments for investment purchases and reinvestments	(860,624)	(872,660)
Proceeds from investment sales and maturities	893,872	830,199
Interest received	4,956	5,624
Net cash flows provided by (used in) investing activities	38,204	(36,837)
Net (decrease) increase in cash and cash equivalents	(236)	816
Cash and cash equivalents		
Beginning	3,386	2,570
Ending	$ 3,150	$ 3,386

(Continued)

The MetroHealth System
(A Component Unit of Cuyahoga County)

Statements of Cash Flows (Continued)
Years Ended December 31, 2012 and 2011
(Dollars in Thousands)

	2012	2011
Reconciliation of Operating Loss to Net Cash Flows (Used in) Provided By Operating Activities:		
Operating loss	$ (17,554)	$ (25,512)
Adjustments to reconcile operating loss to net cash (used in) provided by operating activities		
Depreciation and amortization	31,402	31,528
Provision for bad debts	89,965	84,269
Changes in assets and liabilities:		
Increase in patient accounts receivable	(94,080)	(93,427)
(Increase) decrease in other assets	(33,100)	34,318
Increase in self-insurance liabilities	4,408	9,935
(Decrease) increase in accounts payable and other liabilities	(8,142)	6,437
Increase (decrease) in long-term liabilities	3,454	(2,958)
Net cash flows (used in) provided by operating activities	$ (23,647)	$ 44,590

Noncash Investing, Capital and Financing Activities:

The System held investments at December 31, 2012 and 2011, with a fair value of $351,404 and $385,976, respectively. During 2012 and 2011, the net change in the fair value of these investments was a decrease of $34,572 and an increase of $269, respectively.

The System held interest rate swap obligations at December 31, 2012 and 2011, with a fair value of $14,964 and $15,353, respectively. During 2012 and 2011, the net change in the fair value of these swap obligations was a decrease of $389 and an increase of $11,932, respectively.

During 2012, the System acquired $4,178 in capital assets by entering into capital leases.

See Notes to Financial Statements.

Note 1. Summary of Significant Accounting Policies

Reporting entity: The accompanying financial statements of the MetroHealth System (System) include the MetroHealth Medical Center, a short-term acute care and long-term rehabilitation facility; Broadway Medical Offices, Buckeye Health Center and MetroHealth outpatient community health facilities; MetroHealth Centers for Skilled Nursing Care, consisting of the Old Brooklyn Nursing Facility and the Elisabeth Severance Prentiss Center for Skilled Nursing Care; and several urban and suburban primary care health sites.

The Old Brooklyn Nursing Facility (144 beds) was closed effective December 14, 2011. In 2012, the System sold 91 bed licenses for $1,247 and the remaining 53 licenses were sold in early 2013 for $668. The building has been converted for use as a rehabilitation facility.

The System is the public health care system for Cuyahoga County, Ohio (the County). It is organized and operated by its board of county hospital trustees (the Board) pursuant to Chapter 339 of the Ohio Revised Code. Until 2010, members of the Board were jointly appointed by the Board of County Commissioners of the County, and the senior judges of the Probate and Common Pleas Courts of the County. Effective January 2011, the County voters established a new form of government by charter (the Charter). Under the Charter, future members of the Board are appointed by the County Executive together with the senior judges of the Probate and Common Pleas Courts of the County, subject to confirmation by the County Council. In order to support the general operations of the System, the County of Cuyahoga, Ohio approved an appropriation of $36,029 and $36,031 for 2012 and 2011, respectively. The County has all approved an appropriation of approximately $36,000 for 2013. The System is exempt from federal income taxes as a governmental entity.

In accordance with GASB Statement No. 14, *The Financial Reporting Entity*, the System's financial statements are included, as a discretely presented component unit, in the County's Comprehensive Annual Financial Report (CAFR). A copy of the CAFR can be obtained from Mark A. Parks, Jr., Acting Fiscal Officer, County Administration Building, 1219 Ontario Street, Cleveland, Ohio 44113.

Furthermore, in accordance with GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, The MetroHealth Foundation, Inc. (Foundation) is included as a discretely presented component unit in a separate column in the System's financial statements to emphasize that it is legally separate from the System. The Foundation is a not-for-profit organization supporting the System. The Foundation acts primarily as a fundraising organization to supplement the resources that are available to the System in support of its programs. Although the System does not control the timing or the amount of receipts from the Foundation, the majority of resources, or income thereon, which the Foundation holds and invests, is restricted to support the activities of the System. Because these restricted resources held by the Foundation can only be used by, or for the benefit of the System, it is considered a component unit of the System. Complete financial statements of the Foundation can be obtained by writing to The MetroHealth Foundation, 2500 MetroHealth Drive, Cleveland, Ohio 44109. In addition, MHS Holdings LLC and MHS Purchasing LLC are presented as blended component units whose financial activity is included within the activities of the System. The System owns 99% of MHS Holdings LLC and is the sole member of MHS Purchasing LLC. Although these entities are legally separate from the System, they are reported as if they were part of the System because their sole purpose is to acquire and own investment interests for the System.

Note 1. Summary of Significant Accounting Policies (Continued)

Basis of accounting: The System reports only "business-type" activities, which requires the following financial statements and management discussion and analysis:

- Management's Discussion and Analysis
- Basic Financial Statements including a Statement of Net Position, Statement of Revenues, Expenses and Changes in Net Position, and Statement of Cash Flows, for the System as a whole
- Notes to Financial Statements

The System is accounted for as a proprietary fund (enterprise fund) using the flow of economic resources measurement focus and the accrual basis of accounting. With this measurement focus, all assets and all liabilities associated with the System's operations are included in the Statement of Net Position. Revenue is recognized in the period in which it is earned and expenses are recognized in the period in which incurred.

The System's fiscal year is the calendar year. Pursuant to Ohio law, the System submits a budget to the County for approval by November 1 of each year. The fundamental purpose of the budget is to plan for an expected level of operations and to provide management with a tool to control deviation from such a plan. The budget is prepared on an accrual basis.

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

Statement of Revenues, Expenses and Changes in Net Position: The System recognizes as operating revenues those transactions that are major or central to the provision of health care services. Operating revenues include those revenues received for direct patient care, grants received from organizations as reimbursement for patient care, and other incidental revenue associated with patient care. Operating expenses include those costs associated with providing patient care including costs of professional care, operating the hospital facilities, administrative expenses, and depreciation and amortization. Nonoperating revenues include County appropriations, investment income and special purpose grants and donations, primarily research. Nonoperating expenses include interest expense and expenses from special purpose funds for research related activities.

Net patient service revenue: 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, estimated allowances for uncollectible accounts and uncompensated care allowances. 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. Net patient service revenue is reported net of contractual and retroactive adjustments of $1,099,993 and $1,080,373 and provisions for uncollectible accounts of $89,965 and $84,269 in 2012 and 2011, respectively.

Note 1. Summary of Significant Accounting Policies (Continued)

The System has agreements with third-party payors that provide for payment at amounts different from established charge rates. A summary of the basis of payment by major third-party payors follows:

Medicare and Medicaid: Inpatient acute care services rendered to Medicare and Medicaid program beneficiaries and Medicare capital costs are paid at prospectively determined rates-per-discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. As an academic medical center, medical education payments in addition to disproportionate share entitlements are received from Medicare and Medicaid. Medicare utilizes a prospective payment system for inpatient rehabilitation services and psychiatric services. Effective October 1, 2010, the System no longer participates in the Medicare Periodic Interim Payment (PIP) system.

Medicare outpatient claims are reimbursed under the Ambulatory Payment Classification based prospective payment system. The payments are based on patient assessment data classifying patients into one of the Medicare Ambulatory Payment Classifications. Inpatient rehabilitation and psychiatric and services are reimbursed at a prospectively determined per diem rate. Certain outpatient services related to Medicare beneficiaries and capital costs for Medicaid beneficiaries are reimbursed based on a cost-based methodology subject to certain limitations. The System is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare and Medicaid fiscal intermediaries. The System's classification of patients under the Medicare and Medicaid programs and the appropriateness of their admission are subject to an independent review. Differences between the estimated amounts accrued at interim and final settlements are reported in the Statement of Revenues, Expenses and Changes in Net Position in the year of settlement. The System recorded favorable adjustments of $9,975 and $3,991 in 2012 and 2011, respectively, due to prior year retroactive adjustments to amounts previously estimated and changes in estimates. The 2012 amount recorded for retroactive adjustments includes a change in estimate of $4,000 related to a nationwide settlement with the Centers for Medicare & Medicaid Services (CMS) resulting from an error in the Rural Budget Neutrality adjustment factor used in 1998.

Net revenue from the Medicare and Medicaid programs accounted for approximately 27% and 27%, respectively, of the System's net patient service revenue for the year ended December 31, 2012, and 27% and 29%, respectively, of the System's net patient service revenue for the year ended December 31, 2011. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. As a result, there is at least a reasonable possibility that recorded estimates could change by a material amount in the near term. Management believes that adequate provision has been made in the financial statements for any adjustments that may result from final settlements.

Other payors: The System has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes prospectively-determined rates-per-discharge, discounts from established charges, and prospectively-determined per diem rates.

Note 1. Summary of Significant Accounting Policies (Continued)

Upper payment limit: In September 2001, the State of Ohio Supplemental Upper Payment Limit program for Public Hospitals (UPL) was approved by the CMS. This program provides access to available federal funding up to 100% of the Medicare upper payment limits for inpatient hospital services rendered by Ohio Public Hospitals to Ohio Medicaid consumers. The State of Ohio FY 2010/2011 budget also included an expansion of the UPL program to outpatient services for the first time. The System received $2,367 and $2,367 in outpatient UPL payments in 2012 and 2011, respectively. At December 31, 2012 and 2011, $8,351 and $12,496, respectively, was due to the System and recorded in the Statements of Net Position in other receivables. The amount recorded in net patient service revenue for UPL by the System was $31,334 and $27,130 in 2012 and 2011, respectively. The State of Ohio discontinued the Program's required contributing match for participants as of June 30, 2009. Effective July 1, 2009, the State began assessing a franchise fee to hospitals to fund healthcare programs, including the UPL program. The System incurred a franchise fee expense of $10,161 and $7,363 in 2012 and 2011, respectively, and recorded the amounts as operating expenses in the other expenses category in the Statements of Revenues, Expenses, and Changes in Net Position. The System's franchise fee liability payable to the State of Ohio at December 31, 2012 and 2011 was $5,403 and $2,379, respectively, and is recorded on the Statements of Net Position in other current liabilities.

Disproportionate share: As a public health care provider, the System renders services to residents of the County and others regardless of ability to pay. The System is classified as a disproportionate share provider by the Medicare and Medicaid programs due to the volume of low-income patients it serves. Accordingly, the System receives additional payments from these programs as a result of this status totaling $45,656 and $42,203 for 2012 and 2011, respectively. These amounts are included in net patient service revenue and include Hospital Care Assurance (HCAP) receipts of $33,399 and $30,224 in 2012 and 2011, respectively, reduced by HCAP assessments paid by the System of $3,486 and $3,320 in 2012 and 2011, respectively. At December 31, 2012 and 2011, the System had a receivable of $33,424 and $0, respectively and a payable amount of $3,486 and $0, respectively. The receivable and payable are included in other receivable and other current liability, respectively, in the Statements of Net Position. The System also provides major trauma services to the region. The ability to continue these levels of service and programs is contingent upon the various continued funding sources.

Charity care: Throughout the admission, billing, and collection processes, certain patients are identified by the System as qualifying for charity care. The System provides care to these patients without charge or at amounts less than its established rates. The charges foregone for charity care provided by the System, totaling $267,840 and $242,823, which represents 12.9% and 12.0% of gross charges in 2012 and 2011, respectively, are not reported as revenue. The System accepts certain indigent Ohio residents and all residents from the County regardless of their ability to pay.

Note 1. Summary of Significant Accounting Policies (Continued)

Medicare and Medicaid Electronic Health Records (EHR) Incentive Programs: The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid Incentive Programs beginning in Federal fiscal year 2011 for eligible acute care hospitals that are meaningful users of certified EHR technology, as defined by the Federal Register. The System has implemented certified EHR technology that has enabled it to demonstrate its meaningful use and to qualify for the incentive programs. The initial incentive payments received for both the Medicare and Medicaid EHR incentive programs are estimates based upon data from prior year's cost reports. The final settlements will be determined after the submission of the current annual cost reports and subsequent audits by the fiscal intermediary. The EHR Incentive Programs are expected to continue through September 30, 2014, and the incentive payments will be calculated annually. After that date, hospitals that are not meaningful users or certified users of EHR technology will be subjected to a potential decrease in their Medicare and Medicaid payments. The System accounts for EHR Incentive funds using the grant accounting model. EHR Incentive funds are included in other revenue in the accompanying Statements of Revenues, Expenses and Changes in Net Position and related receivables are included in other receivables in the accompanying Statements of Net Position.

The System successfully registered for the hospital Ohio Medicaid EHR Incentive Program and completed the attestation process in July, 2011. As of December 31, 2012 and 2011, the System has recorded $2,622 and $3,496, respectively for Medicaid EHR incentive. At December 31, 2012 and 2011, the related receivables are $0.

The System successfully registered for the hospital Medicare EHR Incentive Program in July, 2011. The System completed the attestation process on September 6, 2012 after demonstrating the ninety days of continuous use as a meaningful user. During the year ended December 31, 2012, the System recorded Medicare EHR revenue of $2,170, and had a related receivable of $0.

The System successfully registered the hospital physicians, on an individual basis, for the Ohio Medicaid and Medicare EHR Incentive Program and completed the attestation process at various points during 2011 and 2012. As of December 31, 2012 and 2011, the System has recorded $3,672 and $7,331, respectively for Medicaid EHR incentive. During the year ended December 31, 2012, the System recorded Medicare EHR revenue and receivable of $518. At December 31, 2012, the related receivables for Medicaid EHR and Medicare EHR are $332 and $518, respectively. There was no related receivable for the year ended December 31, 2011.

Grants: The System receives financial assistance from federal and state agencies in the United States in the form of grants. The expenditure of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and are subject to audit by the grantor agencies.

Other such audits could be undertaken by federal and state granting agencies and result in the disallowance of claims and expenditures; however, in the opinion of management, any such disallowed claims or expenditures will not have a material effect on the overall financial position of the System.

Cash and cash equivalents: The System considers only the cash in its commercial checking accounts as cash and cash equivalents. Funds in the System's savings / money market accounts are considered Investments. Cash and cash equivalents are stated at cost which is equivalent to fair value.

Note 1. Summary of Significant Accounting Policies (Continued)

Supplies: Medical supplies are stated at the lower of cost or market value on a first-in first-out basis. Pharmaceutical supplies are stated at the lower of cost or market value on a first-in first-out basis.

Investments: The System records its investments at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Unrealized gains and losses on investments are included in net investment income in the Statements of Revenues, Expenses and Changes in Net Position.

The System pools certain of its investments for investment purposes. Investment income for these pooled investments is allocated to the proper investment classification based on each investment's fair value to the total fair value of all pooled investments.

The net realized (loss) gain on investments of ($469) and ($172) in 2012 and 2011, respectively, is the difference between the proceeds received and the amortized cost of investments sold and is included in net investment income (loss) in the Statements of Revenues, Expenses and Changes in Net Position.

Restricted assets: Restricted assets are cash and cash equivalents and investments whose use is limited by legal requirements. Investments under bond indenture agreements represent amounts required by debt instruments to pay bond principal and interest and approved projects. Restricted cash and cash equivalents and special purpose investments represent monies received from donors or grantors to be used for specific purposes, primarily research. The System has elected to use restricted assets before unrestricted assets when an expense is incurred for a purpose for which both resources are available.

Fundraising revenues: Gifts, grants, and program income result from fundraising activities of the Foundation. Though donations are solicited for the Foundation, donors occasionally make their gifts directly to the System.

Contributions: The Foundation recognizes contributions as revenue in the period in which the pledge (promise to give) is received. The Foundation recognizes donated services as contributions if the services (a) create or enhance non-financial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by the Foundation.

Annuity payment obligations: The Foundation has entered into gift annuity agreements which include provisions requiring the Foundation to pay periodic fixed payments to beneficiaries during their lifetimes. Charitable gift annuities differ from other charitable giving options in that the annuity is a general obligation of the Foundation. Accordingly, if the assets of the gift are exhausted as a result of required payments to beneficiaries, unrestricted assets of the Foundation will be utilized to fund future payments.

Income taxes: The Foundation is an Ohio nonprofit corporation and was granted tax-exempt status under Section 501(c)(3) of the Internal Revenue Code and is exempt from income tax on related income pursuant to Section 501(a) of the Code. The Foundation is required to pay taxes on unrelated business income earned by the Foundation.

(Dollars in Thousands)

Note 1. Summary of Significant Accounting Policies (Continued)

Capital assets: Capital assets are stated at cost and contributed capital assets are stated at their fair value at the date of contribution. Expenditures for equipment must exceed $1 per unit and expenditures for renovations must exceed $10 in order for them to be capitalized. Expenditures that substantially increase the useful lives of existing assets are capitalized. Routine maintenance and repairs are expensed as incurred. Depreciation and amortization of assets recorded under capital lease (straight-line method) are provided in amounts sufficient to amortize the cost of the related assets over their estimated useful lives. The following are the most commonly used estimated useful lives:

Buildings	25-40 years
Building improvements	5-20 years
Equipment	3-15 years
Land improvements	5-15 years
Vehicles	4 years

The asset and accumulated depreciation are removed from the related accounts when the asset is disposed. Any income or loss resulting from this disposal is recorded in the Statements of Revenues, Expenses and Changes in Net Position.

Net position: The System classifies its net position into three categories as follows:

Net investment in capital assets – consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds and other debt that are attributable to the acquisition, construction or improvement of those assets.

Restricted – result when constraints placed on the use of the net position are either externally imposed by creditors, grantors, contributors and the like, or imposed by law through constitutional provisions or enabling legislation.

Unrestricted – consists of the remaining net position that does not meet the previously listed criteria.

Bond discounts and bond issuance costs: Deferred financing costs represent debt issuance expenditures on long-term debt obligations and are amortized over the period the bonds are outstanding on a straight-line basis. The amortization for deferred bond financing costs was $163 in 2012 and $169 in 2011. Amortization expense related to bond discounts was $17 in 2012 and $104 in 2011. These amounts are included in interest expense in the Statements of Revenues, Expenses and Changes in Net Position. Accounting guidance requires amounts to be amortized utilizing the effective interest method. The difference between the two amortization methods is immaterial to the financial statements.

Cost of borrowing: Interest costs incurred on debt during the construction or acquisition of assets are capitalized as a component of the cost of acquiring those assets. Capitalized interest of $170 and $515 was recorded in construction in progress as opposed to interest expense for 2012 and 2011, respectively. Construction in progress is transferred to capital assets when assets are substantially completed and amortization of capitalized interest is accounted for in the same manner as other components of asset cost and included in depreciation expense.

Note 1. Summary of Significant Accounting Policies (Continued)

The System has entered into various interest-rate swap agreements. The interest-rate swap agreements are carried at fair value in the Statement of Net Position. These derivative instruments are not effective hedging instruments; therefore, gains and losses are recognized in the Statements of Revenues, Expenses and Changes in Net Position during the period of change as adjustments to investment income on the related debt (see Note 6).

Concentrations of credit risk: Financial instruments that potentially subject the System to concentrations of credit risk consist principally of cash and cash equivalents, patient accounts receivable, and investments.

The System places its cash and cash equivalents with high credit quality financial institutions. The System's investments include money market funds, U.S. Treasury bills and notes, U.S. agency obligations, commercial paper, and corporate bonds.

Concentration of credit risk relating to patient accounts receivable is limited to some extent by the diversity and number of the System's patients and payors. Patient accounts receivable consist of amounts due from government programs, commercial insurance companies, private pay patients, and other group insurance programs. Excluding governmental programs, no payor source represents more than 10.0% of the System's patient accounts receivable. The System maintains an allowance for losses based on the expected collectability of patient accounts receivable.

Reclassifications: Certain reclassifications of 2011 amounts have been made to conform to the 2012 presentation. Among other reclassifications, retail pharmacy revenue is now reported in other operating revenue rather than net patient service revenue in the Statements of Revenues, Expenses and Changes in Net Position; amounts invoiced to recover salaries and benefits from outside entities are presented in other operating revenue instead of reductions to salaries and wages and employee benefits in the Statements of Revenues, Expenses, and Changes in Net Position; additional operating expense reporting categories were created and expense category descriptions were revised with amounts realigned in the Statements of Revenues, Expenses, and Changes in Net Position.

Note 2. Changes in Accounting Principles and Recent Accounting Pronouncements

GASB has issued the following statements that have been recently implemented by the System:

Statement No. 63 – *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* was established to improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. It alleviates uncertainty about reporting those financial statement elements by providing guidance where none previously existed. This Statement also incorporates deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. The System implemented this Statement for the year ended December 31, 2012.

Note 2. Changes in Accounting Principles and Recent Accounting Pronouncements (Continued)

Statement No. 64 – *Derivative Instruments: Application of Hedge Accounting Termination Provisions, Amendment of GASB 53,* was established to enhance comparability and improve financial reporting by clarifying the circumstances in which hedge accounting should continue when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The System implemented this Statement for the year ended December 31, 2012.

There was no significant impact to the financial statements as a result of the application of these standards.

GASB has recently issued the following statements not yet implemented by the System:

Statement No. 61 – *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34,* modifies certain requirements for inclusion of component units in the financial reporting entity. For organizations that previously were required to be included as component units by meeting the fiscal dependency criterion, a financial benefit or burden relationship also would need to be present. Further, for organizations that do not meet the financial accountability criteria for inclusion as component units but that, nevertheless, should be included because the primary government's management determines that it would be misleading to exclude them, this Statement clarifies the manner in which that determination should be made and the types of relationships that generally should be considered in making the determination. The System is required to implement the provisions of this Statement for the year ending December 31, 2013.

Statement No. 65 – *Items Previously Reported as Assets and Liabilities,* establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. This Statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term "deferred" in financial statement presentations. The System is required to implement the provisions of this Statement for the year ending December 31, 2013.

(Dollars in Thousands)

Note 2. Changes in Accounting Principles and Recent Accounting Pronouncements (Continued)

Statement No. 66 – *Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62*, is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, GASB Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in pre-November 30, 1989 FASB and AICPA Pronouncements*. This Statement amends GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, by removing the provision that limits fund-based reporting of an entity's risk financing activities to the general fund and the internal service fund type. This Statement also amends GASB Statement 62 by modifying the specific guidance on accounting for (1) operating lease payments that vary from a straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. The System is required to implement the provisions of this Statement for the year ending December 31, 2013.

Statement No. 68 – *Accounting and Financial Reporting for Pensions,* requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. This Statement also enhances accountability and transparency through revised and new note disclosures and required supplementary information (RSI). The System is required to implement the provisions of this Statement for the year ending December 31, 2015.

Note 3. Deposits and Investments

Deposits

All monies are deposited with the System's banks or trust companies designated by the Board of Trustees. Funds not needed for immediate expenditure may be deposited in interest bearing or non-interest bearing accounts.

Custodial Credit Risk: Custodial credit risk is the risk that, in the event of bank failure, the System's deposits might not be recovered. The FDIC increased insurance through December 31, 2013 for funds held in interest bearing accounts from $100 to $250 per depositor per category of legal ownership. The System's investment policy does not address custodial credit risk. The System's bank deposits at December 31, 2012 and 2011, totaled $ 19,672 and $53,979, respectively, and were subject to the following categories of custodial credit risk:

	2012	2011
Uncollateralized	$ 19,373	$ 53,682
Collateralized with securities held by the pledging institution's trust department, but not in the System's name	49	47
Total amount subject to custodial risk	19,422	53,729
Amount insured	250	250
Total bank balances	$ 19,672	$ 53,979

Note 3. Deposits and Investments (Continued)

Investments

The System: The System’s investment policy authorizes the System to invest in the following investments:

- Securities and obligations of the U.S. Treasury and other federal agencies or instrumentalities.
- Time certificates of deposit or savings accounts and deposit accounts.
- Municipal and state bonds.
- No-load money market mutual funds investing in items listed above.
- Commercial paper that constitutes unsecured short-term debt on an entity defined in Division (D) of Section 1705.01 of the Ohio Revised Code and matures no later than 270 days from purchase date, the aggregate value of the commercial paper does not exceed 10% of the aggregate value of the outstanding paper of the entity, the paper is rated by a least two nationally recognized standard rating services (NRSRS) and is rated in the highest classification and the entity has assets exceeding $500,000, and total combined investments in commercial paper and bankers acceptances does not exceed 25% of the System’s average aggregate investment portfolio.
- Bankers Acceptances that mature no later than 180 days from purchase, the obligations are eligible for purchase by the Federal Reserve System, the issuer has a minimum “AA” long-term debt rating by a majority of NRSRS agencies, the single obligation will not exceed 5% of the System’s total average portfolio, and the total combined investments in bankers acceptances and commercial paper does not exceed 25% of the System’s average aggregate investment portfolio.
- Notes issued by corporations incorporated in the United States and operating in the United States, the notes are rated in the second highest or higher category by at least two NRSRS at the time of purchase, mature in two years or less from the date of purchase and cannot exceed 15% of the System’s total average portfolio.
- No load money market mutual funds rated in the highest category at the time of purchase by at least one NRSRS and consisting exclusively of obligations in the U.S. Treasury and other federal agencies or instrumentalities and commercial paper listed above.

Derivative instruments: In previous periods, the System entered into two separate and distinct interest rate swap agreements ("Swaps") with two counter-parties. The Swaps have notional amounts, maturity schedules, and other features that match the System's two series of underlying variable rate bonds. The Swaps obligate the System to make fixed rate payments to the counter-parties, and obligate the counter-parties to make variable-rate payments to the System. The Swaps are accounted for as "investments" in the System's financial statements pursuant to GASB 53. However, the Swaps were intended, and in fact function, as risk management instruments for current obligations of the System. Consequently, the System does not consider them to be subject to the requirements of the System's investment policy.

(Dollars in Thousands)

Note 3. Deposits and Investments (Continued)

As of December 31, 2012 and 2011, the fair values of the System's investments and their ratings by Standard & Poor's were as follows:

		Investment Maturities	
	2012	Less than 1 year	1-5 years
U.S. Government Agencies			
AAA	$ 270,865	$ 50,722	$ 220,143
Federal National Mortgage Association and Federal Home Loan Mortgage Corporation (Federal Pools)			
AAA	65	-	65
Commercial Paper			
A1	53,744	53,744	-
Money Market			
AAA	10,134	10,134	-
Total investments	$ 334,808	$ 114,600	$ 220,208

Deposits totaling $16,596 are included in investments on the Statement of Net Position at December 31, 2012.

		Investment Maturities	
	2011	Less than 1 year	1-5 years
U.S. Government Agencies			
AAA	$ 237,323	$ 40,277	$ 197,046
Federal National Mortgage Association and Federal Home Loan Mortgage Corporation (Federal Pools)			
AAA	62	1	61
Commercial Paper			
A1	58,177	58,177	-
Money Market			
AAA	18,347	18,347	-
Corporate Bonds			
AAA	21,341	21,341	-
Total investments	$ 335,250	$ 138,143	$ 197,107

Deposits totaling $50,727 were included in investments on the Statement of Net Position at December 31, 2011.

(Dollars in Thousands)

Note 3. Deposits and Investments (Continued)

The System's carrying amounts of the deposits and investments at December 31, 2012 and 2011 are as follows:

	2012	2011
Deposits	$ 19,746	$ 54,112
Investments	334,808	335,250
Total deposits and investments	$ 354,554	$ 389,362

The difference between bank balances and financial statement carrying amounts represent outstanding checks payable and normal reconciling items.

Interest Rate Risk: The System's investment policies limit investment portfolios to maturities of five years or less. All of the System's investments at December 31, 2012 and 2011, have effective maturity dates of less than five years.

Credit Risk: The collateralized mortgage obligations and federal mortgage pools are investments that were made according to policy at the time. In the wake of the financial crisis, the nature of these investments changed and no longer conforms to policy. However, these investments are currently illiquid and cannot be exited at this time.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the System will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The System's investment policy does not address custodial credit risk.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributable to the magnitude of investments in any single issuer. The System holds 5.0% of its portfolio in Bank of Tokyo commercial paper.

(Dollars in Thousands)

Note 3. Deposits and Investments (Continued)

The Foundation: As of December 31, 2012 and 2011, the fair values of the Foundation's investments were as follows:

	2012	2011
Exchange traded funds	$ 3,048	$ 1,918
Money market funds	1,476	1,152
Mutual funds	23,074	21,435
Common stock	25	26
Limited Partnership Interest	2,563	1,698
Premier Purchasing Partners, L.P.	-	956
Total investments	$ 30,186	$ 27,185

Investment income for the years ended December 31, 2012 and 2011 consisted of the following:

	2012	2011
Interest and dividends	$ 746	$ 565
Net realized gains	375	814
Net change in unrealized (losses) gains	2,970	(1,080)
Less investment management fees	(66)	(65)
	$ 4,025	$ 234

The Foundation's investments had cumulative unrealized gains of $1,921 and $604 and cumulative unrealized losses of $281 and $1,727 at December 31, 2012 and 2011, respectively.

(Dollars in Thousands)

Note 4. Capital Assets

The following summarizes changes in the capital assets of the System for the years ended December 31, 2012 and 2011:

2012	Beginning Balance	Additions	Reductions/ Transfers	Ending Balance
Capital assets not being depreciated:				
Land	$ 9,314	$ -	$ -	$ 9,314
Construction in progress	7,087	33,027	(28,067)	12,047
Total nondepreciated capital assets	16,401	33,027	(28,067)	21,361
Depreciable capital assets:				
Land improvements	11,619	30		11,649
Buildings and fixed equipment	536,007	9,286	(662)	544,631
Equipment	299,919	22,765	(5,147)	317,537
Total depreciable capital assets	847,545	32,081	(5,809)	873,817
Less accumulated depreciation:				
Land improvements	(7,342)	(423)		(7,765)
Buildings and fixed equipment	(360,608)	(15,964)	239	(376,333)
Equipment	(234,334)	(15,015)	3,533	(245,816)
Total accumulated depreciation	(602,284)	(31,402)	3,772	(629,914)
Total depreciable capital assets - net	245,261	679	(2,037)	243,903
Total capital assets - net	$ 261,662	$ 33,706	$ (30,104)	$ 265,264

(Dollars in Thousands)

Note 4. Capital Assets (Continued)

2011	Beginning Balance	Additions	Reductions/ Transfers	Ending Balance
Capital assets not being depreciated:				
Land	$ 9,314	$ -	$ -	$ 9,314
Construction in progress	4,386	27,658	(24,957)	7,087
Total nondepreciated capital assets	13,700	27,658	(24,957)	16,401
Depreciable capital assets:				
Land improvements	11,574	45		11,619
Buildings and fixed equipment	530,980	5,066	(39)	536,007
Equipment	291,186	19,854	(11,121)	299,919
Total depreciable capital assets	833,740	24,965	(11,160)	847,545
Less accumulated depreciation:				
Land improvements	(6,921)	(421)		(7,342)
Buildings and fixed equipment	(344,110)	(16,508)	10	(360,608)
Equipment	(229,952)	(14,599)	10,217	(234,334)
Total accumulated depreciation	(580,983)	(31,528)	10,227	(602,284)
Total depreciable capital assets - net	252,757	(6,563)	(933)	245,261
Total capital assets - net	$ 266,457	$ 21,095	$ (25,890)	$ 261,662

Total depreciation and amortization expense related to capital assets for 2012 and 2011 was $31,402 and $31,528, respectively.

(Dollars in Thousands)

Note 5. Long-Term Debt

Information regarding the System's long-term debt activity and balances as of and for the year ended December 31, 2012 is as follows:

	2012				
	Beginning Balance	Additions	Payments/ Reductions	Ending Balance	Due Within One Year
Hospital Improvement and Refunding Revenue Bonds Series, 1997, bear interest at rates ranging from 4.6% to 5.6% and mature in varying amounts through 2027. Partially refunded in 2011 with Hospital Refunding Revenue Bonds, Series 2011.	$ 17,600	$ -	$ -	$ 17,600	$ -
Hospital Refunding Revenue Bonds, Series 1997A, bear interest at rates ranging from 4.1% to 5.5%. Partially and advance refunded in 2011 with Hospital Refunding Revenue Bonds, Series 2011.	5,730	-	(5,730)	-	-
Hospital Improvement Revenue Bonds, Series 2003, bear variable interest rates and mature in varying amounts through 2033. Refunded with Hospital Refunding Bonds, Series 2012.	25,460	-	(25,460)	-	-
Hospital Improvement and Revenue Bonds, Series 2005, bear variable interest rates and mature in varying amounts through 2035.	72,505	-	(390)	72,115	410
Hospital Facilities Revenue Bonds, Series 2009B, bear interest at 8.2% and mature in varying amounts through 2040.	75,000	-	-	75,000	-
Hospital Refunding Revenue Bonds, Series 2011, bear interest at 3.2% and mature in varying amounts through 2019.	67,455	-	(8,635)	58,820	7,630
Hospital Refunding Revenue Bonds, Series 2012, bear variable interest rates and mature in varying amounts through 2033.	-	24,710	-	24,710	785
Equipment obligation, GE Leasing, as defined in the respective lease agreement, bears interest at 6.0% and matures through 2014.	23	-	(10)	13	10
Equipment obligation, IBM Leasing, as defined in the respective lease agreement, bears interest at 2.7% and matures through 2014.	606	-	(252)	354	283
Equipment obligation, RBS Asset Finance, as defined in the respective lease agreement, bears interest at 3.0% and matures through 2019.	-	417	(41)	376	56
Equipment obligation, RBS Asset Finance, as defined in the respective lease agreement, bears interest at 3.1% and matures through 2019.	-	2,102	(135)	1,967	277

(Dollars in Thousands)

Note 5. Long-Term Debt (Continued)

	2012				
	Beginning Balance	Additions	Payments/ Reductions	Ending Balance	Due Within One Year
Equipment obligation, RBS Asset Finance, as defined in the respective lease agreement, bears interest at 2.9% and matures through 2019.	$ -	$ 1,659	$ (72)	$ 1,587	$ 219
Loan obligation, Cuyahoga County Sanitary Engineering, as defined in the respective loan agreement, matures through 2018.	40	-	(6)	34	5
	264,419	28,888	(40,731)	252,576	9,675
Unamortized discount and loss on refunding	(9,139)	(256)	960	(8,435)	-
Long-term debt	$ 255,280	$ 28,632	$ (39,771)	$ 244,141	$ 9,675

Information regarding the System's long-term debt activity and balances as of and for the year ended December 31, 2011 is as follows:

	2011				
	Beginning Balance	Additions	Payments/ Reductions	Ending Balance	Due Within One Year
Hospital Improvement and Refunding Revenue Bonds Series, 1997, bear interest at rates ranging from 4.6% to 5.6% and mature in varying amounts through 2027. Partially refunded in 2011 with Hospital Refunding Revenue Bonds, Series 2011.	$ 30,155	$ -	$ (12,555)	$ 17,600	$ -
Hospital Refunding Revenue Bonds, Series 1997A, bear interest at rates ranging from 4.1% to 5.5%. Partially and advance refunded in 2011 with Hospital Refunding Revenue Bonds, Series 2011.	60,605	-	(54,875)	5,730	5,730
Hospital Improvement Revenue Bonds, Series 2003, bear variable interest rates and mature in varying amounts through 2033.	26,185	-	(725)	25,460	750
Hospital Improvement and Revenue Bonds, Series 2005, bear variable interest rates and mature in varying amounts through 2035.	72,880	-	(375)	72,505	390
Hospital Facilities Revenue Bonds, Series 2009A, bear interest at 3.9%, refunded with Hospital Refunding Revenue Bonds, Series 2011.	7,683	-	(7,683)	-	-
Hospital Facilities Revenue Bonds, Series 2009B, bear interest at 8.2% and mature in varying amounts through 2040.	75,000	-	-	75,000	-
Hospital Refunding Revenue Bonds, Series 2011, bear interest at 3.2% and mature in varying amounts through 2019.	-	67,455	-	67,455	8,635

(Dollars in Thousands)

Note 5. Long-Term Debt (Continued)

	2011				
	Beginning Balance	Additions	Payments/ Reductions	Ending Balance	Due Within One Year
Equipment obligation, GE Leasing, as defined in the respective lease agreement, bears interest at 6.0% and matures through 2014.	$ 29	$ -	$ (6)	$ 23	$ 10
Equipment obligation, IBM Leasing, as defined in the respective lease agreement, bears interest at 2.7% and matures through 2014.	874	-	(268)	606	252
Loan obligation, Cuyahoga County Sanitary Engineering, as defined in the respective loan agreement, matures through 2018.	44		(4)	40	5
	273,455	67,455	(76,491)	264,419	15,772
Unamortized discount and loss on refunding	(9,211)	(816)	888	(9,139)	-
Long-term debt	$ 264,244	$ 66,639	$ (75,603)	$ 255,280	$ 15,772

Effective February 1, 1997, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $70,000 of Hospital Improvement and Refunding Revenue Bonds Series 1997 (The MetroHealth System Project) (Series 1997). The proceeds of the Series 1997 Bonds were used to refund $20,900 of Series 1989 Bonds; to finance the construction of various improvements and additions to The MetroHealth Medical Center; and to pay costs of issuance of the Series 1997 Bonds. On November 22, 2011, the entire principal amounts of the Series 1997 Bonds maturing in years 2012 through 2019 were refunded with proceeds from the County's Series 2011 Hospital Refunding Revenue Bonds. The refundings totaled $11,440.

Effective November 1, 1997, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $77,525 of Hospital Refunding Revenue Bonds, Series 1997A (The MetroHealth System Project) (Series 1997A). On February 15, 1998, the proceeds of the Series 1997A Bonds were used to refund the entire $73,725 remaining outstanding balance of the Series 1989 Bonds. The 1997 refundings resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $9,753. The unamortized difference, $0 and $7 at December 31, 2012 and 2011, respectively, is reported in the accompanying financial statements as a reduction from long-term debt and is included as additional interest expense through the year 2012. On November 22, 2011, all outstanding Series 1997A principal amounts maturing on and after February 15, 2012 were refunded or advance refunded using proceeds from the County's Series 2011 Hospital Refunding Revenue Bonds. The Bond refundings totaled $55,170 of which $49,440 was immediately refunded and $5,730 was advance refunded for February 2012.

Note 5. Long-Term Debt (Continued)

Effective March 13, 2003, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $30,545 of Hospital Improvement Variable Rate Demand Revenue Bonds, Series 2003 (The MetroHealth System Project) (Series 2003 Bonds). The proceeds of the Series 2003 Bonds were used to pay costs of constructing and equipping the Critical Care Pavilion and an administrative building. The bonds bear interest at a variable rate (not to exceed 10.0%) determined weekly as established by the Remarketing Agent based on current market values for similar bond offerings and are due at various dates until 2033. The interest rate at December 31, 2011, was 0.07%. On December 20, 2012, all outstanding Series 2003 Bonds were refunded using proceeds from the County's Series 2012 Hospital Refunding Revenue Bonds issuance. The Bond refundings totaled $24,710.

In connection with the issuance of the Series 2003 Bonds, the System entered into a Reimbursement Agreement with a bank. Under the terms of the Reimbursement Agreement, the System entered into an Irrevocable Letter of Credit issued by a local bank that expired on March 22, 2010. Effective March 1, 2010, the System entered into a new letter of credit reimbursement agreement ("2003 Letter of Credit") that was due to expire on March 16, 2013.

Commencing June 16, 2010, the System was required to pay the bank a letter of credit fee payable in quarterly installments at variable rates ranging from 95 basis points to 175 basis points depending on the debt rating in effect as of the date the rating report is released. In addition, the System paid to the bank a closing fee of 20 basis points and to the remarketing agent an advisory fee of 7.5 basis points. As of December 31, 2011, the letter of credit fee was 95 basis points. There were no amounts outstanding on the letters of credit as of December 31, 2011.

This letter of credit was extinguished in conjunction with the refunding of the Series 2003 Bonds and issue of the Series 2012 Bonds on December 20, 2012.

Effective July 1, 2005, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $74,535 of Hospital Improvement and Refunding Variable Rate Demand Revenue Bonds, Series 2005 (The MetroHealth System Project) (Series 2005 Bonds). Proceeds from the 2005 Series Bonds were used to advance refund $56,995 of the outstanding Series 1999 Bonds, to pay costs of constructing, renovating, furnishing, equipping, and improving the Old Brooklyn Campus long-term care and skilled nursing facility; and to pay certain costs of issuance of the Series 2005 Bonds. The bonds bear interest at a variable rate (not to exceed 10.0%) determined weekly as established by the Remarketing Agent based on current market values for similar bond offerings and are due at various dates until 2035. The interest rates at December 31, 2012 and 2011 were 0.11% and 0.07%, respectively.

In connection with the issuance of the Series 2005 Bonds, the System entered into a Reimbursement Agreement with a bank. Under the terms of the Reimbursement Agreement, the System entered into an Irrevocable Letter of Credit issued by a local bank that was due to expire on July 16, 2010. Effective June 1, 2010, the System entered into a new letter of credit reimbursement agreement ("2005 Letter of Credit") that was due to expire on July 16, 2013 with PNC Bank (as Administrative Agent) and JPMorgan Chase Bank (collectively referred to as the "Banks"), and PNC Capital Markets as Lead Arranger and Book Runner. Effective December 20, 2012 this agreement was extended and JPMorgan Chase Bank was effectively replaced by Fifth Third Bank. This extension is scheduled to expire on December 16, 2015.

Note 5. Long-Term Debt (Continued)

In the event there is a remarketing drawing on the letter of credit and the tendered bonds have not been remarketed by the 367th day from the Remarketing Drawing, the System has the option to convert the obligation to a term loan in the amount of the unpaid portion of the remarketing drawing. The term loan is payable in twelve equal quarterly installments accruing interest at the base rate plus 2%. The base rate is defined as the highest of the Prime Rate, the sum of the Federal Funds Open rate plus .50%, the sum of the daily Libor Rate plus 1%, or 5% per annum. In the event of default, the term loan will be due immediately upon demand by the Banks.

Commencing with the extension dated December 20, 2012, the System is required to pay the Banks a letter of credit fee payable in quarterly installments at variable rates ranging from 70 basis points to 140 basis points depending on the debt rating in effect as of the date the rating report is released. In addition, the System paid to the Lead Arranger an arrangement fee of 7.5 basis points (and an additional $10 administration fee to the Agent Bank). As of December 31, 2012 and 2011, the letter of credit fee was 95 and 95 basis points, respectively. There were no amounts outstanding on the letters of credit as of December 31, 2012 and 2011.

The 2005 Letter of Credit is subject to various financial covenants for debt service coverage, long-term debt to capitalization, cash to debt and days cash on hand.

The July 28, 2005, bond refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $5,179. The unamortized difference ($3,544 and $3,764 at December 31, 2012 and 2011, respectively), reported in the accompanying financial statements, as a reduction from long-term debt, is being amortized as an increase to interest expense through the year 2029.

Effective December 1, 2009, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $8,466 of Hospital Facilities Revenue Bonds, Series 2009A. The proceeds of the Series 2009A Bonds were used to purchase the Valentine parking garage on the System's main campus. The Bonds carried an interest rate of 3.9% and were to mature through 2014. On November 22, 2011, all outstanding Series 2009A Bonds totaling $7,076 were refunded from proceeds of the County's Series 2011 Hospital Refunding Revenue Bonds.

Effective January 28, 2010, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $75,000 of Hospital Revenue Bonds, Taxable Series 2009B, (The MetroHealth System), (Build America Bonds – Direct Payment). Proceeds from the Series 2009B will be used to pay for costs of hospital facilities, including three medical helicopters, the acquisition, construction and equipping of additional multi-specialty ambulatory centers in strategic locations, and additional scheduled equipment purchases and facilities renovations; funding the Bond Reserve Fund for the Series 2009B Bonds; and certain bond issuance costs. The Bonds bear interest at a fixed rate of 8.223% per annum and mature at various dates through 2040. As a qualified Build America Bond Issue, per terms of the federal government's American Recovery and Reinvestment Act of 2009, the System will apply to receive direct payments semiannually from the Secretary of the United States Treasury in the amount of 35% of the corresponding bond interest paid. Payments received from the Treasury are recorded in other non-operating revenue.

Note 5. Long-Term Debt (Continued)

Effective November 8, 2011, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $67,455 of Hospital Refunding Revenue Bonds, Series 2011, (The MetroHealth System), (Taxable Bonds). Proceeds from the Series 2011 Bonds were used to currently refund the entire principal amount of the Series 1997 Bonds maturing on February 15, 2012 through February 15, 2019; currently refund the outstanding principal amount of the Series 1997A Bonds maturing on and after February 15, 2013; advance refund the principal amount of the Series 1997A Bonds maturing February 15, 2012; currently refund all the outstanding Series 2009A Bonds; and pay certain costs of issuance of the Series 2011 Bonds. The Bonds bear interest at a fixed rate of 3.16% per annum and mature at various dates through 2019.

The November 8, 2011 bond refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $5,187. The unamortized difference ($4,382 and $5,098 at December 31, 2012 and 2011, respectively), reported in the accompanying financial statements as a reduction from long-term debt, is being amortized as an increase to interest expense through the year 2019. The System advance refunded the 1997, 1997A and 2009 Series Bonds to reduce its total debt service payment over the next eight years by $13,646 and to obtain an economic gain of $1,377.

Effective December 20, 2012, Cuyahoga County, acting by and through the Board of Trustees of The MetroHealth System, issued $24,710 of Hospital Refunding Revenue Bonds, Series 2012, (The MetroHealth System), (Series 2012 Bonds). Proceeds from the Series 2012 Bonds were used to refund the entire principal amount of the Series 2003 Bonds maturing on March 1, 2013 through March 1, 2033. The debt service payments required for the Series 2012 do not differ from the debt service payments that were required under the Series 2003 Bonds. The Bonds bear variable rate interest and mature at various dates through 2033. The interest rate at December 31, 2012 was 1.08%.

The December 20, 2012 bond refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $256. The unamortized difference ($255 at December 31, 2012) is reported in the accompanying financial statements as a reduction from long-term debt, and is being amortized as an increase to interest expense through the year 2033.

The Series 1997, 1997A, 1999, 2003, 2005, 2009A, 2009B, 2011 and 2012 Bonds were issued pursuant to a master trust bond indenture agreement between the County, acting by and through the System's Board of Trustees, and the bond trustee. The Series 1997, 1997A, 1999, 2003, 2005, 2009B, 2011 and 2012 Bonds are special obligations issued by the County payable solely from the revenue derived from the operation of the System and other monies available to the System's Board of Trustees. Accordingly, the bond proceeds and indebtedness have been recorded as assets and liabilities of the System.

The terms of the master trust bond indenture agreement provide for the establishment of a depreciation reserve fund and maintenance of certain special funds, which are maintained under the control of the bond trustee, and are used for payment of principal and interest on the bonds when due.

(Dollars in Thousands)

Note 5. Long-Term Debt (Continued)

The revenue bonds and lease obligation payment requirements for fiscal years subsequent to December 31, 2012, are as follows:

	Total Lease and Loan Obligations			Total Hospital Revenue Bonds		
	Principal	**Interest**	**Total**	**Principal**	**Interest**	**Total**
2013	$ 850	$ 118	$ 968	$ 8,825	$ 11,852	$ 20,677
2014	648	95	743	9,115	11,574	20,689
2015	592	77	669	9,415	11,276	20,691
2016	610	59	669	9,725	10,968	20,693
2017	628	41	669	10,055	10,649	20,704
2018–2022	1,003	25	1,028	43,945	48,399	92,344
2023–2027	-	-	-	45,280	40,647	85,927
2028–2032	-	-	-	38,190	32,257	70,447
2033–2037	-	-	-	42,495	21,113	63,608
2038–2041	-	-	-	31,200	3,939	35,139
	$ 4,331	$ 415	$ 4,746	248,245	$ 202,674	$ 450,919
Unamortized discount				(253)		
Unamortized difference between reacquisition price and the net carrying amount of old debt				(8,182)		
Total hospital revenue bonds — net				$ 239,810		

The cost value of Hospital Revenue Bonds was $247,992 and $263,480 at December 31, 2012 and 2011, respectively.

There are no amounts remaining to be paid to bond holders related to defeased debt at December 31, 2012.

(Dollars in Thousands)

Note 6. Derivative Instruments

The System's objectives of its derivative instruments include managing the risk of increased debt service resulting from rising market interest rates, the risk of decreased surplus returns resulting from falling interest rates, and the management of the risk of an increase in the fair value of outstanding fixed rate obligations resulting from declining market interest rates. Consistent with its interest rate risk management objectives, the System entered into various interest rate swap agreements with a total outstanding notional amount of $96,825 and $97,965 at December 31, 2012 and 2011, respectively.

The System's swap agreements do not meet the criteria for hedging and are reported as investment derivative instruments. The fair value of the swap agreements based on current settlement prices at December 31, 2012 and 2011, was ($14,964) and ($15,353), respectively. The amounts due to the counterparties are included within the liability section of the Statements of Net Position. The fair value increase of $389 in 2012 and the fair value decrease of $11,932 in 2011 are included in net investment income (loss) in the Statements of Revenues, Expenses and Changes in Net Position. As a result of the agreements, net settlements increased the System's interest expense by $2,606 and $2,121 in 2012 and 2011, respectively.

The following table describes the terms of the System's two interest rate swap agreements:

12/31/2012 Notional Amount	12/31/2011 Notional Amount	Effective Date	Termination Date	Early Termination Option	The System Pays	Counterparty Pays
$ 72,115	$ 72,505	July 28, 2005	February 1, 2035	the System	Fixed 3.3%	64.2% of ISDA 5 Yr. Swap Rate
$ 24,710	$ 25,460	March 13, 2003	March 1, 2033	the System	Fixed 3.5%	68.9% of ISDA 5 Yr. Swap Rate

On July 28, 2005, the System entered into a swap agreement with an initial amortizing notional amount of $74,535. The notional amount is based on the Series 2005 Bond principal repayment schedule that ends in 2035. Per the terms of an amended agreement effective June 1, 2006, the System pays a fixed rate of 3.3% and the counterparty pays 64.2% of the International Swaps and Derivatives Association, Inc. (ISDA) USD five-year swap rate. The original agreement previously required the counterparty to pay 70% of the 3-month USD LIBOR. In 2012, ISDA five-year interest rates ranged between 0.7% and 1.4%. The net amount is exchanged monthly between the two parties. The System has an early termination option.

On March 13, 2003, the System entered into a swap agreement with an amortizing notional amount of $30,545. The amortizing notional amount is based on the Series 2003 Bond principal repayment schedule ending on March 1, 2033. On December 20, 2012 the Series 2003 Bonds were advance refunded with proceeds from the issuance of the Series 2012 Bonds, which maintain an identical repayment schedule. Per terms of an amended agreement effective June 1, 2006, the System pays a fixed rate of 3.5% and the counterparty pays 68.9% of the ISDA USD five-year swap rate. The original agreement previously required the counterparty to pay 75% of the 3-month USD LIBOR rate. Net settlement amounts are exchanged monthly. The System has an early termination option.

Interest Rate Risk: The System is exposed to interest rate risk on its interest rate swaps. On the pay-fixed receive variable swaps, as the ISDA Swap index decreases, the System's net payment on the swaps increase.

(Dollars in Thousands)

Note 7. Other Long-Term Liabilities

Amounts Due to Third-Party Payors: The System has agreements with third-party payors that provide for payment of amounts different from established rates. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and are adjusted in future periods, as final settlements are determined. See Note 1, net patient service revenue, for additional information. As of December 31, 2012 and 2011, the liability for amounts due to third-party payors was $8,303 and $8,868, respectively.

Accrued Vacation and Sick Leave: System employees earn vacation and sick leave at varying rates depending on job classification and years of service. Employees can accumulate up to three years of their earned vacation leave. All accumulated, unused vacation time is paid upon separation if the employee has at least one year of service with the System. There is no limit on the amount of sick time earned. Upon retirement, employees with a minimum of 10 years of service have sick leave balances paid out at 50% of eligible hours at their current rate of pay. The maximum payout is 800 hours. As of December 31, 2012 and 2011, the liability for accrued vacation and sick leave was $43,444 and $40,438, respectively.

Other Long-Term Liabilities: Other long-term liabilities consist of the following at December 31, 2012 and 2011:

2012	Beginning Balance	Additions	Deletions	Ending Balance	Due Within One Year
Amounts due to third-party payors	$ 8,868	$ 1,915	$ (2,480)	$ 8,303	$ 4,206
Accrued vacation and sick leave	40,438	45,078	(42,072)	43,444	7,229
Derivative instruments - rate swaps	15,353	-	(389)	14,964	-
	$ 64,659	$ 46,993	$ (44,941)	$ 66,711	$ 11,435

2011	Beginning Balance	Additions	Deletions	Ending Balance	Due Within One Year
Amounts due to third-party payors	$ 10,769	$ 1,439	$ (3,340)	$ 8,868	$ 5,029
Accrued vacation and sick leave	39,900	42,300	(41,762)	40,438	7,419
Derivative instruments - rate swaps	3,421	11,932	-	15,353	-
	$ 54,090	$ 55,671	$ (45,102)	$ 64,659	$ 12,448

Risk Management: The System is exposed to various risks of loss related to torts; theft of or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The System is self-insured for employee health insurance, workers compensation and medical malpractice but maintains commercial insurance policies for property and casualty, automobile, aircraft (helicopter and fixed wing) as well as excess coverage for medical malpractice claims and employee health insurance. Settled claims for workers compensation and medical malpractice have not exceeded insurance coverage in any of the past three years.

(Dollars in Thousands)

Note 7. Other Long-Term Liabilities (Continued)

During the normal course of its operations, the System has become a defendant in various legal actions. In the opinion of legal counsel and the System administration, the disposition of the pending cases will not have a material adverse effect of the financial condition or operations of the System. However, depending on the amount and timing of such resolution, an unfavorable resolution of some or all of these matters could materially affect the System's future results of operations or cash flows in a particular year.

The System is self-insured for employee health, medical malpractice and worker's compensation claims. For the professional and patient care liability and worker's compensation, professional actuarial insurance consultants have been retained to determine funding requirements. Amounts funded for professional and patient care have been placed in an irrevocable self-insurance trust account, which is being administered by a trustee. For the employee health claims, a historical analysis has been performed of incurred but not reported claims to determine the liability at December 31, 2012 and 2011.

Losses from asserted claims and from unasserted claims identified under the System's incident reporting systems are accrued based on estimates that incorporate the System's past experience, as well as other considerations including the nature of each claim or incident and relevant trend factors. The liability for estimated self-insured claims includes estimates of the ultimate costs for both reported claims and incurred but not reported claims, for 2012, 2011 and 2010 as follows:

2012	Beginning Balance	Claims Incurred	Claims Paid	Ending Balance	Due Within One Year
Worker's compensation	$ 8,876	$ 2,719	$ (2,300)	$ 9,295	$ 2,874
Self-insurance	38,379	16,377	(12,388)	42,368	10,746
Employee health	1,536	17,959	(17,661)	1,834	1,834
	$ 48,791	$ 37,055	$ (32,349)	$ 53,497	$ 15,454

2011	Beginning Balance	Claims Incurred	Claims Paid	Ending Balance	Due Within One Year
Worker's compensation	$ 8,724	$ 2,823	$ (2,671)	$ 8,876	$ 3,055
Self-insurance	28,596	15,488	(5,705)	38,379	12,200
Employee health	1,517	17,484	(17,465)	1,536	1,536
	$ 38,837	$ 35,795	$ (25,841)	$ 48,791	$ 16,791

2010	Beginning Balance	Claims Incurred	Claims Paid	Ending Balance	Due Within One Year
Worker's compensation	$ 8,473	$ 3,285	$ (3,034)	$ 8,724	$ 3,348
Self-insurance	30,003	10,310	(11,717)	28,596	8,606
Employee health	1,513	15,837	(15,833)	1,517	1,517
	$ 39,989	$ 29,432	$ (30,584)	$ 38,837	$ 13,471

The current portion of employee health liabilities is included in other current liabilities.

(Dollars in Thousands)

Note 7. Other Long-Term Liabilities (Continued)

The liabilities recorded for worker's compensation and self-insurance at December 31, 2012 are discounted liabilities. The discount rate used was 1.5 percent. The undiscounted liabilities are approximately $735 and $2,127 higher for worker's compensation and self-insurance, respectively.

The liabilities recorded for worker's compensation and self-insurance at December 31, 2011 are discounted liabilities. The discount rate used was 1.5 percent. The undiscounted liabilities are approximately $600 and $2,100 higher for worker's compensation and self-insurance, respectively.

Note 8. Operating Leases

The System has entered into operating lease agreements for medical and office space, which expire through 2020. Contract terms range between one and fifteen years and contain rent escalation clauses and renewal options for additional periods ranging from one to five years.

Minimum rental commitments under operating leases extending beyond one year at December 31, 2012, are as follows:

2013	$	2,180
2014		1,439
2015		1,125
2016		1,062
2017		740
2018-2020		1,250
Total	$	7,796

Rent expense totaled $2,428 in 2012 and $2,104 in 2011.

Note 9. Benefit Plans

Pension: Employee retirement benefits are available for substantially all employees under three separate retirement plans administered by the Ohio Public Employees Retirement System (OPERS). The plans are the Traditional Pension Plan — a cost-sharing, multiple-employer defined benefit pension plan; the Member-Directed Plan — a defined contribution pension plan in which the members invests both member and employee contributions (employer contributions vest over five years at 20% per year). Under the Member-Directed Plan, members accumulate retirement assets equal to the value of member and (vested) employee contributions plus any investment earnings; and the Combined Plan — a cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan. OPERS provides retirement, disability, survivor, and post retirement healthcare benefits, to the Traditional and Combined Plan members however, healthcare benefits are not statutorily guaranteed. Participants in the Member-Directed Plan do not qualify for ancillary benefits. Chapter 145 of the Ohio Revised Code assigns the authority to establish and amend benefits to the OPERS Board of Trustees. The Ohio Public Employees Retirement System issues a stand-alone financial report and may be obtained by writing to OPERS, 277 East Town Street, Columbus, Ohio 43215-4642, or by calling 614-222-5601 or 800-222-7377.

Note 9. Benefit Plans (Continued)

The Ohio Revised Code provides statutory authority for employee and employer contributions. For the years ended December 31, 2012, 2011, and 2010, the employee contribution rate was 10.0% of covered payroll and the System was required to contribute 14.0% of covered payroll. For 2012, member and employer contribution rates were consistent across all three plans. Employee contributions to OPERS for the years ended December 31, 2012, 2011, 2010 and 2009 were $38,717, $37,487, $35,705 and $34,572, respectively, equal to the required contributions for each year. The System's contributions to OPERS for the years ended December 31, 2012, 2011, 2010, and 2009, were $54,202, $52,482, $49,988 and $48,406, respectively, equal to the required contributions for each year.

Post Retirement Benefits: OPERS maintains a cost-sharing multiple employer defined benefit post-employment healthcare plan, which includes a medical plan, prescription drug program, and Medicare Part B premium reimbursement, to qualifying members of both the Traditional Pension and Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits including post employment healthcare coverage.

In order to qualify for post employment healthcare coverage, age-and-service retirees under the Traditional Pension and Combined Plans must have 10 or more years of qualifying Ohio service credit. Healthcare coverage of disability benefit recipients and qualified survivor benefit recipients is available. The healthcare coverage provided by OPERS meets the definition of an Other Post Employment Benefit (OPEB) as described in GASB Statement No. 45.

The Ohio Revised Code permits, but does not mandate, OPERS to provide OPEB benefits to its eligible members and beneficiaries. Authority to establish and amend benefits is provided in Chapter 145 of the Ohio Revised Code.

The Ohio Revised Code provided the statutory authority requiring public employers to fund post retirement health care through their contributions to OPERS. A portion of each employer's contribution to OPERS is set aside for the funding of post retirement healthcare benefits.

The employer contribution rates are expressed as a percentage of the covered payroll of active members. In 2012, the employer contribution was 14.0% of covered payroll. The Ohio Revised Code currently limits the employer contribution to a rate not to exceed 14.0% of covered payroll. Active members do not make contributions to the OPEB plan.

OPERS' Post Employment HealthCare plan was established under, and is administrated in accordance with, Internal Revenue Code 401(h). Each year, the OPERS Retirement Board determines the portion of the employer contribution rate that will be set aside for funding of post employment health care benefits. The portion of employer contributions allocated to healthcare for members in the Traditional Plan was 4.0% during calendar year 2012. The portion of employer contributions allocated to health care in the Combined Plan was 6.05% during calendar year 2012. Effective January 1, 2013, the portion of employer contributions allocated to healthcare was lowered to 1.0% for both plans, as recommended by the OPERS Actuary. The OPERS Retirement Board is also authorized to establish rules for the payment of a portion of the health care benefits provided by the retiree or their surviving beneficiaries. Payment amounts vary depending on the number of covered dependents and the coverage selected. The System's contributions for 2012, 2011, 2010, and 2009 used to fund post retirement healthcare benefits were $15,485, $14,994, $18,149 and $20,313, respectively, which are included in the System's contractually required contribution of $54,202, $52,482, $49,988 and $48,406 for the years ended December 31, 2012, 2011, 2010, and 2009, respectively.

(Dollars in Thousands)

Note 9. Benefit Plans (Continued)

On September 9, 2004, the OPERS Retirement Board adopted the Health Care Preservation Plan (HCPP), effective on January 1, 2007. Effective as of January 1, 2006, 2007, and 2008, member and employer contribution rates increased, allowing additional funds to be allocated to the healthcare plan.

Note 10. Restricted, Expendable and Nonexpendable Net Position

The System has a restricted expendable net position that is restricted by the master trust bond indenture and donors to specific purposes. The net position is designated for the following purposes at December 31:

	2012	2011
Debt service payment and reserve funds	$ 20,150	$ 25,542
Time restrictions	5,556	5,854
Total	$ 25,706	$ 31,396

The Foundation has a restricted expendable net position that is restricted by the donors or grantors to a specific time or purpose. The net position is designated for the following purposes at December 31:

	2012	2011
Programmatic activities of The MetroHealth System	$ 18,945	$ 16,933
Time restrictions	321	188
Total	$ 19,266	$ 17,121

The Foundation has restricted, nonexpendable net positions in the amounts of $9,756 and $8,998 at December 31, 2012 and 2011, that are restricted in perpetuity, the income from which is expendable to support the programmatic activities of The MetroHealth System.

Note 11. Related Organizations

The System is the primary beneficiary of The MetroHealth Foundation, Inc. (Foundation). The Foundation is a separate not-for-profit entity organized for the purpose of supporting the System in the areas of research, community health and continuing professional education. In accordance with GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, the System has reported the Foundation as a discretely presented component unit in the System's 2012 and 2011 financial statements. The System received support from the Foundation in the amount of $3,067 and $3,933 in 2012 and 2011, respectively, which is recorded as grant revenue on the System's Statements of Revenues, Expenses and Changes in Net Position. The outstanding receivable from the Foundation was $1,200 and $1,581 at December 31, 2012 and 2011, respectively, which is included in other receivables on the System's Statements of Net Position. The System provided the Foundation in-kind support totaling $1,321 and $1,367 in 2012 and 2011, respectively. This support covered the direct expenses of the Development Department and indirect expenses for the use of space and support departments such as information services and environmental services.

Note 11. Related Organizations (Continued)

The System had established restricted funds to differentiate resources, the use of which is restricted by donors or grantors, from resources of general funds on which donors place no restrictions or that arise as a result of the operations of the System. A review of these restricted funds is performed annually to determine that funds, related to completed clinical trials and certain donated money, should be transferred to the Foundation. There were no transfers in 2012 and 2011.

Note 12. Investment in Blended Component Unit

MHS Holdings LLC (LLC) was formed to acquire and own interests in certain health care businesses. The System is the 99% member of the LLC. During 2011, the System's 40% equity interest in CCF/MHS Renal Care Company, LTD., a joint venture with The Cleveland Clinic Foundation, which provides renal care (dialysis), was transferred to the LLC. Because the LLC is considered to be a blended component unit of the System, its financial activity is reflected within the financial activity of the System on these financial statements. At December 31, 2012 and 2011, the LLC had balances of $10,065 and $6,633, respectively that are included in other assets in the System's Statements of Net Position, which essentially represents the LLC's interest in CCF/MHS Renal Care Company LTD. In 2012 and 2011, the LLC recorded other income of $3,432 and $5,113, respectively, that are included in the System's Statements of Revenue, Expenses and Changes in Net Position. The LLC holds no other assets, liabilities, equity, revenue or expenses at December 31, 2012 and 2011. In addition, prior to the establishment of the LLC, the System received $2,548 in distributions from CCF/MHS Renal Care Company, LTD in 2011. No distributions were received during 2012.

MHS Purchasing LLC (MHS) was formed during 2012 to own an interest in Premier Purchasing Partners, L.P. (Premier). Premier is a group purchasing organization that provides the group greater bargaining power for cost of materials. Because MHS is considered to be a blended component unit of the System, its financial activity is reflected within the financial activity of the System on these financial statements. Prior to 2012, this ownership interest was held by the Foundation. At December 31, 2012, MHS had a balance of $643 that is included in other assets in the System's Statements of Net Position, which essentially represents MHS's interest in Premier. In 2012, MHS recorded other income of $643 that is included in the System's Statements of Revenue, Expenses and Changes in Net Position related to the activity of MHS and the transfer of the investment from the Foundation. MHS holds no other assets, liabilities, equity, revenue or expenses at December 31, 2012.

Note 13. Conditional Promises to Give

The Foundation: The Foundation received a conditional pledge of $10,000 commencing in 2005 payable over the next 10 years at $1,000 per year. The outstanding balance of $2,415 and $3,415 at December 31, 2012 and 2011, respectively, is not included in these financial statements in accordance with the Accounting Standards Codifications (ASC) 958, *Not for Profit Entities* due to the fact that the conditions of the grant have not been met.

Note 14. Commitments and Contingencies

CMS Recovery Audit Contractor Program: Congress passed the Medicare Modernization Act in 2003, which among other things established a three-year demonstration of the Medicare Recovery Audit Contractor (RAC) program. The RAC's identified and corrected a significant amount of improper overpayments to providers. In 2006, Congress passed the Tax Relief and Health Care Act of 2006 which authorized the expansion of the RAC program to all 50 states by 2010. The Centers for Medicare and Medicaid Services (CMS) is in the process of rolling out this program nationally.

Construction Commitments: As of December 31, 2012, the System had contractual commitments for the construction of various projects totaling approximately $33,762. Projects with large contractual commitments include $15,887 for the Middleburg Heights Family Health Center, $6,675 for hospital enterprise software licensing and implementation, $2,422 for the Imaging Center expansion, $760 for elevator modernization, and $522 for obstetric fetal monitor equipment. These projects are being funded with operating funds and bond project funds.

Regulatory environment including fraud and abuse matters: The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government activity continues with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the System is in compliance with fraud and abuse, as well as other applicable government laws and regulations. While no regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or asserted at this time.

Patient Protection and Affordable Care Reconciliation Act: On March 23, 2010, the most sweeping health care legislation since the advent of Medicare was signed into law. The law promises to expand insurance coverage to an additional 32 million Americans, reduce the growth of Medicare expenditures, dramatically reform insurance markets, and continue the trend toward value-based payment. The Reconciliation Act amends various provisions of the Patient Protection and Affordable Care Reconciliation Act and adds some new provisions that were not included originally. Several legal challenges have been made against the legislation since it was enacted, and uncertainty exists as to the ultimate impact of the legislation on the health care delivery system. On June 28, 2012, The United States Supreme Court upheld the constitutionality of components of the Affordable Care Act, allowing the historic overhaul of the health care system to continue. Potential impacts of health care reform include uncertainty and volatility in Medicare and Medicaid reimbursement, fundamental changes in payment systems, increased regulation, and significant required investments in health care information technology.

The MetroHealth System
(A Component of Cuyahoga County)

OMB Circular A-133 Requirements

The MetroHealth System
(A Component Unit of Cuyahoga County)

Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

Federal Grantor/Pass-Through Grantor	Program Title	Federal CFDA Number	Grant Number		Federal Expenditures
U.S. Department of Agriculture:					
Pass-Through Program from:					
Ohio Department of Health	Special Supplement Nutrition Program for Women, Infants and Children	10.557	1830011WA0512; 1830011WA0613	$	4,730,295
	TOTAL --- U.S. Department of Agriculture			**$**	**4,730,295**
U.S. Department of Education:					
Pass-Through Program from:					
Ohio Department of Health	Special Education - Grants for Infants and Families -HMG Hospital Based Regional Child Find	84.181	1830011HB0512; 1830011HB0613	$	30,002
Ohio Rehabilitation Services Commission	Rehabilitation Services - Vocational Rehabilitation Grants to States - VRP3	84.126	n/a		210,405
	TOTAL --- U.S. Department of Education			**$**	**240,407**
U.S. Department of Health & Human Services:					
Pass-Through Program from:					
Cuyahoga County Board of Health	Maternal and Child Health Services Block Grants to the States - CFHS Cleveland Regional Perinatal Network; Child & Family Health Services	93.994	01810011MC0512; 01810011MC0613	$	84,867
Western Reserve Area Agency on Aging	Centers for Medicare & Medicaid Services (CMS) Research, Demonstrations, and Evaluations - Access Your Benefits Program	93.779	1YOCMS030365/01; 1YOCMS030365		24,412
Western Reserve Area Agency on Aging	Medicare Enrollment Assistance Program - Access Your Benefits Program	93.071	09AAOHMIPP		36,910
Cuyahoga County	Acquired Immunodeficiency Syndrome (AIDS) Activity - Tuberculosis Prevention & Control	93.118	01810022TB0212; 01810022TB0313		166,011
Cuyahoga County Board of Health	HIV Emergency Relief Project Grants - Ryan White Title I	93.914	CE1100241-01		1,345,837
Ohio Department of Health	*HIV Care Formula Grants* - Ryan White Part B/Title II	93.917	01830012RW0111; 01830012RW0212		119,723
	HIV Care Formula Grants - Ryan White Emergency Assistance Funding - Title II	93.917	n/a		10,827
	Centers for Disease Control and Prevention - Investigations and Technical Assistance - Coverdell Registry for Heart Disease & Stroke Prevention	93.283	01830012HD0108		167,453
Center for Health Affairs	National Bioterrorism Hospital Preparedness Program - HRSA Emergency Preparedness/ASPR Grant	93.889	01860052RP0512; 01860052RP0613		90,381
	TOTAL --- U.S. Department of Health & Human Services			**$**	**2,046,421**
U.S. Department of Homeland Security:					
Pass-Through Program from:					
Cuyahoga County Department of Public Safety	Port Security Grant Program	97.056	AG1100021-01		27,822
	TOTAL --- U.S. Department of Homeland Security			**$**	**27,822**
Research and Development Cluster					
U.S. Department of Education:					
Direct Programs:	National Institute on Disability and Rehabilitation Research - NORSCIS - Collaborative Project	84.133	H133N060017	$	21,450
	Subtotal - U.S. Department of Education - Direct			**$**	**21,450**
	Subtotal - Research & Development Cluster - Direct			**$**	**21,450**
U.S. Department of Defense:					
Pass-Through Program from:					
National Trauma Institute / Department of Defense U.S. Army Medical Research	Military Medical Research & Development - Splenic Injury Prospective Outcomes Trial	12.420	W81XWH-11-1-0841	$	21,502
Neuros Medical / Department of Defense U.S. Army Medical Research	Peripheral Nerve Stimulation Block Technology	12.unknown	W81XWH-10-1-0829		30,462
	Subtotal - U.S. Department of Defense - Pass Through			**$**	**51,964**

(Continued)

The MetroHealth System
(A Component Unit of Cuyahoga County)

Schedule of Expenditures of Federal Awards (Continued)
Year Ended December 31, 2012

Federal Grantor/Pass-Through Grantor	Program Title	Federal CFDA Number	Grant Number		Federal Expenditures
U.S. Department of Health & Human Services:					
Pass-Through Program from:					
Cleveland Clinic Foundation	Cancer Treatment Research - GOG Trials Gynecologic Oncology Group	93.395	CA027469	$	27,824
Duke Clinical Research Institute	Cancer Treatment Research - American College of Surgeons Oncology Group	93.395	CA76001		7,849
Frontier Science	Cancer Treatment Research - Eastern Cooperative Oncology Group	93.395	CA21115		31,482
Frontier Science	Cancer Control - Eastern Cooperative Oncology Group	93.399	CA37403		31,483
Duke Clinical Research / NIAMS	Trans-NIH Recovery Act Research Support - Childhood Arthritis and Research Alliance Network ***** RECOVERY*****	93.701	SPS165191		7,277
Duke Clinical Research / NIH-NHLBI	Trans-NIH Recovery Act Research Support - Prospective Multicenter Imaging Study Evaluation of Chest Pain ***** RECOVERY*****	93.701	DUKE 173530		10,650
Emmes Corporation / NIH-NINDS	Trans-NIH Recovery Act Research Support - Platelet-Oriented Inhibition in New TIA (POINT) ***** RECOVERY*****	93.701	NS062835		8,207
University of Rochester / NIH-NHLBI	Cardiovascular Diseases Research - Risk Stratification in Madit II Type Patients	93.837	R01HL077478		2,262
Brigham & Williams / NIH-NHLBI	Cardiovascular Diseases Research - Pre-Determine Biologic Markers & MRI SCD Cohort Study	93.837	620-5346000-600022475		5,912
University of Rochester / NIH-NHLBI	Cardiovascular Diseases Research - Ranolazine ICD Trial (RAID)	93.837	415639-G, U01 HL966		11,016
Duke Clinical Research/NIH-NHLBI	Cardiovascular Diseases Research - Xanthine Oxidase Inhibition for Hyperuricemic HF Patients	93.837	177494, U10HL08904		945
Duke Clinical Research/NIH-NHLBI	Cardiovascular Diseases Research - Predetermine Biologic Markers and MRI SCD Cohort Study	93.837	177494, HL084904		1,554
Wake Forest Baptist Medical Center / NIH-NHLBI	Cardiovascular Diseases Research - Neuro Outcomes in Diabetics with Heart Surgery	93.837	5R01HL089115-07		8,557
Duke Clinical Research / NIH-NHLBI	Blood Diseases and Resources Research - Bridging Anticoagulation In Patients Who Require Temporary Interruption of Warfarin Therapy	93.839	U01HL087229		33,944
University of Minnesota / NIH-NIAMS	Arthritis, Musculoskeletal and Skin Diseases Research - Faith Hip Fracture	93.846	N00188516		7,550
John Hopkins University Bloomberg / NIH-NIDDK	Diabetes, Digestive, and Kidney Diseases Extramural Research - Gastroparesis Consortium Continuation Data Coordinating Center	93.847	5U01DK074008-07		9,517
University of British Columbia/ NIH-NINDS	Extramural Research Programs in the Neurosciences and Neurological Disorders - SPS-3 Prevention of Small Subcortical Strokes	93.853	NS038529		48,114
Yale / NIH-NINDS	Extramural Research Programs in the Neurosciences and Neurological Disorders - Insulin Resistance Intervention After Stroke Trial	93.853	(A06113) NS044876-02		21,043
University of Virginia / NIH-NR; NIH-NIGMS	Biomedical Research and Research Training - Multicenter Study of Duration of Antibiotics	93.859	GC11617-139126; GC11617-13912601		17,329
UAB at Birmingham/NIH-NIAID	Clinical Trials for Antiviral Therapies	93.unknown	N01-A1-30025		280
Harvard Pilgrim Healthcare / CDC	Vaccine Adverse Events Reporting System	93.unknown	2011-N-13526		133,070
University of Alabama	Clinical Trials for Antiviral Therapies	93.unknown	000189671-242		1,193
New England Research Inst. / NIH-NHLBI	Treatment of Preserved Cardiac Function Heart Failure	93.unknown	N01HC-45207		113
	Subtotal - U.S. Department of Health & Human Services - Pass-through			**$**	**427,171**
	Subtotal - Research & Development Cluster - Pass Through			**$**	**479,135**
	TOTAL - Research & Development Cluster			**$**	**500,585**
	TOTAL EXPENDITURES OF FEDERAL AWARDS			**$**	**7,545,530**

See Note to Schedule of Expenditures of Federal Awards.

Note to Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

Note 1. Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of The MetroHealth System (the System) and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

For the purposes of this schedule, federal awards include direct federal awards and pass-through funds received from nonfederal organizations made under federally sponsored programs conducted by those organizations.

All programs are classified under the federal department that sponsors the program. Pass-through programs are also presented by the entity through which the System received the federal award. Catalog of Federal Domestic Assistance (CFDA) numbers are presented when such numbers are available.

McGladrey

Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

To the Board of Trustees of
The MetroHealth System
Cleveland, Ohio

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities and the discretely presented component unit of The MetroHealth System (the System) as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the System's basic financial statements, and have issued our report thereon dated April 23, 2013. Our report includes a reference to other auditors who audited the financial statements of The MetroHealth Foundation, Inc. (the Foundation), as described in our report on the System's financial statements. This report does not include the results of the other auditor's testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements, will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a deficiency in internal control, described in the accompanying schedule of findings and questioned costs as finding 2012-01 that we consider to be a significant deficiency.

Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards* (Continued)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The MetroHealth System's Response to Findings

The System's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned cost. The System's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

McGladrey LLP

Cleveland, Ohio
April 23, 2013

McGladrey

Independent Auditor's Report on Compliance For Each Major Federal Program and Report on Internal Control Over Compliance Required by OMB Circular A-133

To the Board of Trustees of
The MetroHealth System
Cleveland, Ohio

Report on Compliance for Each Major Federal Program

We have audited The MetroHealth System's (the System) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the System's major federal program for the year ended December 31, 2012. The System's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the System's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the System's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of The MetroHealth System's compliance.

Opinion on Each Major Federal Program

In our opinion, The MetroHealth System complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of the System is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the System's internal control over compliance with the types of requirements that could have a direct and material effect on its major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for its major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

McGladrey LLP

Cleveland, Ohio
April 23, 2013

The MetroHealth System
(A Component Unit of Cuyahoga County)

Schedule of Findings and Questioned Costs
For the Year Ended December 31, 2012

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unqualified Opinion			
Internal control over financial reporting:				
• Material weakness(es) identified?		Yes	X	No
• Significant deficiency(ies) identified?	X	Yes		None reported
Noncompliance material to financial statements noted?		Yes	X	No

Federal Awards

Internal control over major programs:				
• Material weakness(es) identified?		Yes	X	No
• Significant deficiency(ies) identified?		Yes	X	None reported
Type of auditor's report issued on compliance for major programs:	Unqualified Opinion			
Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of Circular A-133?		Yes	X	No

Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children

Dollar threshold used to distinguish between Type A and Type B programs:			$ 300,000	
Auditee qualified as a low risk auditee?	X	Yes		No

Section II - Financial Statement Findings

Finding Number:	2012-01
Finding Description:	Information Technology
Criteria:	A strong internal control environment should include processes that are designed to provide reasonable assurance about the achievement of an entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
Condition:	The System does not have a process in place to periodically review logical access for billing financial applications. Lawson access was reviewed as part of the conversion of the security model but a regular review for all financial statement applications has not been implemented. Development of the System's disaster recovery plan and facilities has not been completed and tested for adequacy and sufficiency or reviewed periodically for continued viability. These conditions were also noted in the prior year. See summary schedule of prior year findings and questioned costs, finding numbers 2011-01 and 2010-01.
Context:	These conditions were identified during our review of the Information Technology General Controls and operational practices and procedures as they relate to the financial statement audit of the System.
Effect:	Inappropriate logical access could cause security over data to be compromised and/or a disruption in operations. An inadequate disaster recovery plan puts the System's resources at risk for data loss and financial services disruptions in the event of a disaster.
Cause:	The findings, while generally understood, were not able to be prioritized for immediate resolution but were planned for future disposition when additional time and resources became available.
Recommendation:	During 2011, we acknowledge that the System did review the propriety of user access for the Lawson application. We recommend that management continue to develop an ongoing comprehensive user access review process that includes annual verification of appropriate access to financial applications. We also recommend performing an IT risk assessment and based on the result of the risk assessment, establishing an ongoing IT audit program to better understand and manage the risk to the System. We were able to observe that the System did enhance the current disaster recovery server room. However, we recommend the System develop a detailed disaster recovery plan and install a larger recovery data center with sufficient capacity to recover all organizational functions including all critical financial processing and regularly exercise the plan and facilities for adequacy and viability.

Section II - Financial Statement Findings (Continued)

Views of responsible officials and planned corrective actions:

Logical Access Controls: The MetroHealth System has implemented access control based upon control rights assigned by Active Directory and the application Access Control systems in accordance with the Electronic Identification, Authentication and Access Control Policy (VI-12). There is an established security request process whereby all access requests are required to be reviewed and approved by the appropriate management prior to implementation. The Information Services Change Management policy is a department specific not an enterprise policy.

All system security access is administered through identified individuals and is based upon the capabilities of individual applications. Information Services is currently preparing to conduct an access review. Additional financial applications will have access reviews throughout the year in 2013. The review process document has been developed and is in use. The System recently added a security engineer whose duties include access audit coordination. The System is actively planning to implement the latest access control upgrades for key applications, such as EPIC and Lawson and is working with vendors of other systems to ensure that systems are compliant with all appropriate regulations, policies and processes.

The access request process has been implemented and verified by MH Internal Audit. EPIC has also been upgraded and the Lawson security portal upgrade is complete.

Disaster Recovery: MetroHealth has a Disaster recovery plan document that includes recovery procedures for the Epic, Lab and Radiology systems as well as our interface engine. The System has tested the Epic and Radiology recovery plans successfully and have the GE Lab system plan scheduled to be tested December 9th. In addition Information Services has contracted with Elyria Memorial Hospital to provide a space sharing arrangement for Disaster Recovery(DR) purposes. The Elyria site is being prepared for The MetroHealth System Disaster Recovery occupancy later this month. Information Services has ordered the communication circuits and have secured the hardware to build out recovery capability for several additional critical systems. These critical systems are targeted for deployment of recovery capability in the first quarter of 2013. Additional deployment of system recovery capability is scheduled later in 2013.

Section III - Findings and Questioned Costs for Federal Awards

None

Summary Schedule of Prior Year Findings and Questioned Costs
For the Year Ended December 31, 2012

Section II – Financial Statement Findings

Finding Number: 2011-01 and 2010-01

Finding Description: Information Technology

Summary of Prior Year Finding:

The System does not have a process in place to periodically review logical access for all applications. The System's disaster recovery plan and the facilities have not been assessed for adequacy and sufficiency or reviewed periodically for continued viability.

Status

Repeat finding – refer to 2012-01.

Section III - Findings and Questioned Costs for Federal Awards

None

METRO HEALTH SYSTEM

CUYAHOGA COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
JUNE 18, 2013