

VII. STANDING COMMITTEES

B. Finance, Audit and Facilities Committee

UW Medicine Board Annual Financial Report

This report is for information only.

Attachment

UW Medicine Board Annual Financial Report to the UW Board of Regents,
November, 2012



UW Medicine Board
Annual Financial Report to the UW Board of Regents
November, 2012

EXECUTIVE SUMMARY

UW Medicine performed well financially in FY 2012, exceeding budgeted expectations. Federal healthcare reform advanced, with a landmark ruling by the Supreme Court, and general economic conditions remained challenging.

In line with national trends, UW Medicine's overall hospital volumes remained relatively flat. However, the complexity and severity level of UW Medicine's patient population increased, with strong volumes in high intensity services. While less funding was received from the special, one-time American Recovery and Reinvestment Act (ARRA), other federal funds were obtained for progress UW Medicine made in implementing Meaningful Use (MU) milestones specified in the health reform bill related to the Electronic Medical Record (EMR).

Factors contributing to growth in FY 2012 included the addition of Valley Medical Center as the eighth entity of UW Medicine on July 1, 2011; expansion of the primary care network with two new clinics in Ravenna and Northgate and an expansion of space at the Kent Des Moines clinic. Major construction projects include: Phase I of the Montlake Tower construction at UWMC, which began occupancy in October 2012, expands and replaces the existing Neonatal ICU, provides additional inpatient beds for oncology services and expands diagnostic and interventional imaging; and South Lake Union Phase 3.1 scheduled to be substantially complete in February 2013, which will provide expanded research space.

Total revenue in FY 2012 for UW Medicine was \$3.6 billion, \$2.6 billion from the hospitals, clinics and practice plans and \$1 billion from the School of Medicine. This represented a 17 percent increase compared to FY 2011. Net income for the UW Medicine hospitals, clinics and practice plans was \$49.9 million, yielding a 1.9% margin. The consolidated balance sheet for UW Medicine remained stable. Cash increased by over \$80 million during the year.

The SOM absorbed additional reductions in Washington State funding in FY2012. Revenue from research declined as a result of the ramp-down of American Recovery and Reinvestment Act (ARRA) awards. However, overall revenues for the School of Medicine (SOM) increased 1 percent in FY 2012 compared with the prior year from self-sustaining program revenue, institutional support and transfers from practice plans. Reserves increased primarily as a result of endowment principal additions and unspent Research Cost Recovery funds.

Working with Chartis LLC, UW Medicine continues to make progress in assessing Accountable Care Organization (ACO) strategies to position the system for the changes required for national health reform. UW Medicine strategic expansion, coupled with our high-quality patient care and cost reduction efforts, are crucial as payment reforms are implemented.

Financial Highlights for FY 2012

UW Medical Center (UWMC)

UWMC experienced strong operating revenues of \$881 million in high-intensity services such as cardiology, neonatal intensive care, solid organ transplantation and oncology. Net income was \$40.5 million, including \$6.5 million in Electronic Health Record (EHR) incentive payments. Construction of the Montlake Tower continued during the year, and the new 50-bed neonatal intensive care unit is expected to open in late fall 2012, followed by the 30 bed oncology unit.

Harborview Medical Center (HMC)

Harborview had higher-intensity inpatient case mix, strong outpatient volumes in the Emergency Department and Specialty Clinics, and continued to be successful in executing process improvement initiatives in the areas of Revenue Cycle Improvements, Supply Chain Management and Transformation of Care. Total operating revenues were \$766 million with net income of \$7.9 million, including \$9.0 million in EHR incentive payments.

Northwest Hospital (NWH)

UW Medicine continued the integration of the strategic plan at the NWH campus. Key initiatives implemented included the relocation of the UWMC midwife deliveries, UWMC orthopedic joint surgical cases, and the UWMC Multiple Sclerosis Center to the Northwest Hospital campus. Construction of the SCCA's Proton beam facility was substantially completed on the campus, with patient care scheduled to begin in early 2013. Total operating revenues increased by \$24 million to \$300 million in FY 2012. Significant performance improvement activities occurred at NWH during the year. A net loss of \$(2.7) million was reported for the year which is an improvement of \$(5.7) million over the prior year. The loss included \$0.3 million in EHR incentive payments.

Valley Medical Center (VMC)

VMC experienced growth in both its inpatient hospital and clinic activities. UW Medicine continued the integration of the strategic plan on the VMC campus with the work of the Operational Integration Oversight Committee. Highlights included providing expanded clinical coverage for neurological surgery and thoracic surgery consultation and expanding the training site for the UW emergency medicine residency program to VMC. Additional integration was completed in areas of quality & safety, compliance, pharmacy, marketing and a variety of other services. During most of 2012, the organization focused on the replacement of clinical and financial information systems and began implementation of Epic, which should be fully implemented in November 2012 in primary care, specialty care, and urgent care clinics and the inpatient hospital. Operating costs supporting the systems implementation were approximately \$10 million. Total operating revenues were \$428 million with a net loss of \$(5.6) million, which included \$1.3 million in EHR incentive payments.

UW Neighborhood Clinics (UWNC)

UWNC's operating funding support in FY 2012 was \$16.2M. This was \$520k in excess of expectations. Financial performance was impacted by inclement weather and higher than expected start-up costs for new clinics. The expansion of the Kent-Des Moines clinic was completed and the Ravenna and Northgate clinics opened in FY12. UWNC's required subsidy for primary care is consistent with national benchmarks and experiences at other comparable practices in academic medical centers and private settings. The secondary and tertiary care referrals generated by UWNC result in significant revenue for UW Medicine hospitals.

University of Washington Physicians (UWP)

FY 2012 operating revenues were \$253.0 million, an increase of \$22.0 million over FY 2011. Patient care revenue increased \$11.9M over FY11 and was primarily associated with a four percent increase in volumes (as measured in relative value units). UWP reserves decreased \$24.0M, primarily due to a combination of increased support for physician compensation and lower investment earnings in FY12.

Airlift Northwest (ALNW)

Flight volumes at ALNW were on budget for the year. Fuel costs were higher than planned; however, management successfully reduced other expenses to end the year on budget, reporting an operating income of \$2.1 million on total operating revenues of \$39 million for FY 2012. ALNW successfully expanded service to the Yakima area by day-basing a turbocommander aircraft in the region.

UW School of Medicine (SOM)

Due to ongoing economic issues the State of Washington, financial support for the SOM was reduced by 5 percent, resulting in a \$3.1 million reduction in FY 2012. In addition, revenue generated from research activities declined \$27 million (4 percent) from FY 2011 as a result of the ramp-down of American Recovery and Reinvestment Act (ARRA) awards. These reductions were offset by increases in self-sustaining revenue, institutional support, and transfers from practice plans. Overall, revenue of \$ 1.0 billion for the SOM remained relatively flat from FY 2011 to FY 2012, with a slight increase of 1 percent.

Private Support and Gifts

Total private support for UW Medicine for FY 2012 was \$117.0 million, comprising 37 percent of the University's total private support for the year. Private grants decreased in FY 2012, from \$95.7 million in FY 2011 to \$87.8 million in FY 2012. Gifts decreased from \$32.3 million in FY 2011 to \$29.3 million in FY 2012. The decrease in private grants and gifts partially reflects the impact of the economic recession on funding from private foundations.

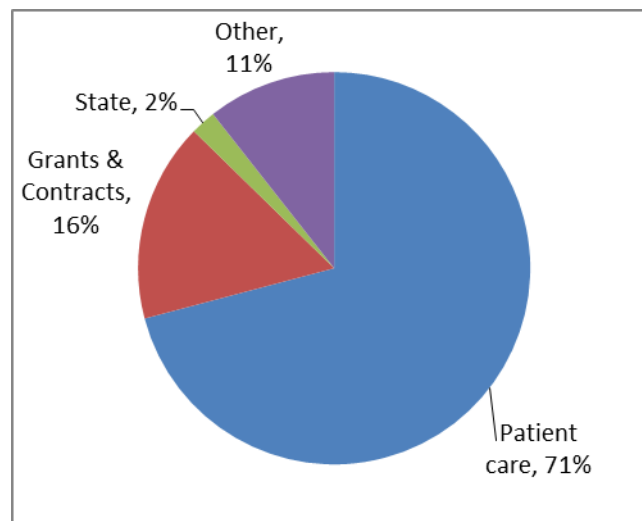
Transfers and Support

Approximately \$618 million of total revenues were transferred between various UW Medicine entities and affiliates to support teaching, research and patient care activities. In FY 2012, the major transfer components included: \$283 million from the physician practice plans (UWP and CUMG) to support School of Medicine faculty salaries, clinical department operations, and central SOM expenditures; \$160 million from UWMC, HMC, and Seattle Children's Hospital to SOM clinical departments to provide faculty salary and program support; \$47 million from UWMC and HMC to the SOM clinical departments to support graduate medical education; \$26 million in purchases of SOM developmental lab services by the medical centers; \$25 million from the medical centers, practice plans and SOM to support the central administrative and service functions of UW Medicine; \$8 million in UWMC and HMC purchases of services from the Consolidated Laundry; and \$5 million in research facilities support from SOM to HMC. There was a total of \$64 million in purchases of supplies and services between UWMC, Fred Hutchinson Cancer Research Center, and the Seattle Cancer Care Alliance related to the operation of inpatient and outpatient oncology services at the SCCA and UWMC.

KEY STATISTICS & RESULTS

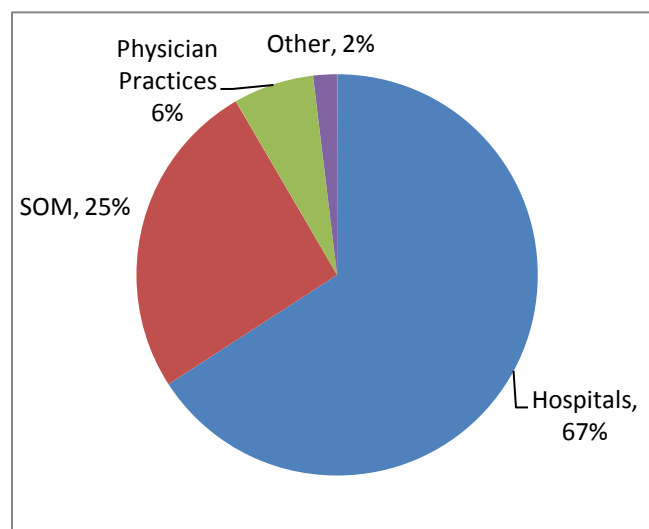
In FY 2012, UW Medicine revenues were \$3.6 billion. This represents an increase of approximately 17 percent compared with FY 2011, in large part due to the addition of Valley Medical Center. Without Valley Medicine Center the growth rate would have been 3 percent. The following charts summarize the sources of revenue for UW Medicine. Over the last five years, total UW Medicine revenue has increased at an average rate of 11 percent per year. These increases have occurred in the context of a competitive local healthcare market, significant reductions in state-funded programs and increased competition for peer reviewed research grant funding.

Fiscal Year 2012 – Revenue by Source Total Revenue \$3.6 billion



(Other includes support from Wyoming, Alaska, Montana, and Idaho, and revenue from endowments and gifts).

Fiscal Year 2012 – Revenue by Entity Category Total Revenue \$3.6 billion



(“Other” includes Airlift Northwest and the Consolidated Laundry.)

UW Medicine revenues come primarily from patient care revenue (71%) and research grants and contracts (16%). The following sections highlight the performance in each of these areas.

PATIENT CARE

The following table summarizes operating revenue received by the UW Medicine hospitals, clinics and practice plans in FY 2011 and FY 2012. This table does not include research grants or other funds (total of \$1.0 billion) received by the School of Medicine and does not include revenue from the Seattle Cancer Care Alliance outpatient services.

UW Medicine Health System	Operating Revenue (in millions)	
	2011	2012
Harborview Medical Center	\$725.3	\$765.7
UW Medical Center	847.9	881.3
Northwest Hospital & Medical Center	275.8	300.0
Valley Medical Center	N/A	428.2
UW Physicians	231.0	252.7
UW Neighborhood Clinics	25.2	27.2
Airlift Northwest	33.6	38.6
Eliminations and Other	(18.3)	(20.7)
Total	\$2,120.5	\$2,673.0

Net operating income from UW Medicine clinical operations for FY 2012, after adjusting for revenues counted in more than one entity (e.g., UWP billings for physicians working in UWNC), was \$56.1 million or 2.1 percent of operating revenue. UWMC generated \$65.3 million in operating income, Harborview generated \$18.2 million, Northwest Hospital had an operating loss of (\$4.6) million, and Valley Medical Center reported an operating loss of (\$7.1) million. Airlift NW generated \$2.0 million of operating income. The UW Neighborhood Clinics required \$16.2 million in support from UWMC and Harborview in order to offset expenses. The net income (operating and non-operating) generated by UWP (\$75.9 million) and CUMG (\$33.6 million) is distributed to the School of Medicine departments, the Dean's office, and Seattle Children's Hospital (for a portion of CUMG revenue) in order to support operations.

The following tables provide comparisons of key financial indicators for the four medical centers:

Ratio/Indicator	UW Medical Center	Harborview Medical Center	Northwest Hospital & Medical Center	Valley Medical Center
Operating margin	7.4%	2.4%	-1.5%	-1.6%
Debt to capitalization	23.3%	0.7%	54.0%	60.3%
Days cash on hand	119.7	105.1	67.9	125.7
Days in A/R (net)	52.1	57.3	44.9	46.9

- Harborview provided over \$210 million of charity care in FY 2012, as measured by foregone charges – an increase of \$21 million over FY 2011. Total charity care across all UW Medicine hospitals was \$292 million, an increase of \$43 million over FY2011.
- The Harborview low debt-to-capitalization number reflects the capital support provided by King County through voter-approved general obligation bonds.

5-YEAR PERFORMANCE COMPARISON

The overall patient care activity of the UW Medicine clinical entities remains stable. The following tables summarize the clinical activities for the owned and managed components of UW Medicine.

Harborview Medical Center

Statistic	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Admissions & Short Stays	21,764	20,463	20,984	19,879	19,094
Patient Days	136,662	136,687	135,124	136,619	134,930
Outpatient Visits	230,315	224,769	246,420	241,924	247,246
Emergency Visits	68,987	65,515	62,174	61,307	62,432
Average Length of Stay	7.4 days	7.0 days	6.9 days	6.9 days	7.1 days
Case Mix Index (CMI)	1.84	1.86	1.84	1.83	1.91

UW Medical Center

Statistic	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Admissions	18,993	19,322	19,260	18,919	17,915
Patient Days	115,270	113,468	114,362	115,447	120,745
Outpatient Visits	324,812	333,675	323,393	306,825	300,487
Emergency Visits	29,038	27,046	25,602	24,119	23,487
Average Length of Stay	6.1 days	5.9 days	5.9 days	6.1 days	6.7 days
Case Mix Index (CMI)	1.66	1.70	1.78	1.87	1.99

Northwest Hospital & Medical Center

Statistic	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Admissions				10,743	10,383
Patient Days				47,194	45,754
Outpatient Visits				418,442	455,768
Emergency Visits				35,146	33,832
Average Length of Stay				4.4 days	4.4 days
Case Mix Index (CMI)				1.45	1.37

Valley Medical Center

Statistic	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Admissions					16,842
Patient days					63,001
Outpatient Visits					551,796
Emergency Visits					75,586
Average Length of Stay					3.7 days
Case Mix Index (CMI)					1.30

UW Neighborhood Clinics

Statistic	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Clinic Visits	201,645	188,148	193,280	189,597	204,094
New Patients	11,768	10,264	11,567	11,894	13,097

Inpatient admissions for the SCCA 20-bed unit at UWMC are included in the UWMC admission total.

RESEARCH PROGRAMS

UW Medicine research continues to grow. UW School of Medicine grant and contract awards through the University of Washington totaled \$610.8 million in FY 12. This was a \$37 million 6.4% increase over FY11. ARRA awards were \$2.2 million in FY 12 and \$94.3 million in FY11, \$90.4M in FY10 and \$3.5M in FY 09.

The following table summarizes the UW based SOM research awards over the past five years excluding ARRA awards:

(\$ in millions)

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012 (prelim)	5-year CAGR
Federal	\$371.5	\$358.3	\$388.4	\$389.3	\$414.2	2.8%
Non-Federal	\$145.8	\$204.4	\$177.1	\$184.5	\$196.6	7.8%
Total	\$517.3	\$562.7	\$565.5	\$573.8	\$610.8	4.2%

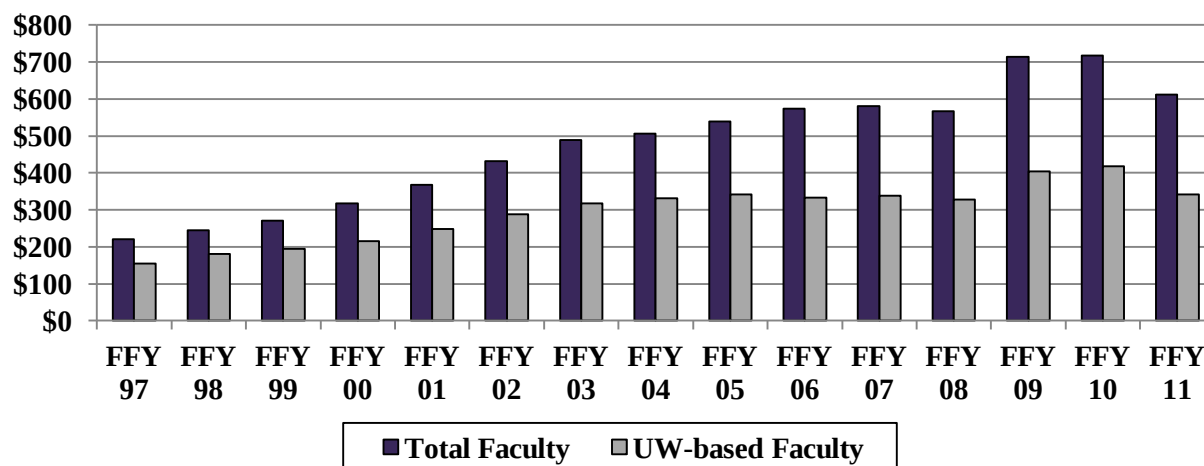
The following table summarizes the UW-based SOM research awards over the past five years including ARRA awards:

(\$ in millions)

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	Average Annual Change
Federal	\$371.5	\$361.8	\$470.6	\$475.3	\$414.2	2.8%
Non-federal	\$145.8	\$204.4	\$185.2	\$192.8	\$198.9	8.1%
Total	\$517.3	\$566.2	\$655.8	\$668.1	\$613.1	4.3%

NIH awards represent the single largest source of awards received by UW Medicine faculty. The following chart tracks the growth of NIH awards to UW Medicine faculty over the past 15 federal fiscal years ending in federal fiscal year 2011. NIH funding is on a federal fiscal year basis and comparative information is not available until several months after the close of the federal fiscal year on September 30.

NIH Grant Awards to UW Medicine
(\$ in millions)



15-year Compound Annual Growth Rate (CAGR) (FFY 97-11): 28.9% for Total Faculty, 21.9% for UW-based Faculty
5-year CAGR (FFY 07-11): 1.3% for Total Faculty, 0.4% for UW-based Faculty

In federal fiscal year 2011, there were 737 separate NIH awards to 491 UW-based SOM principal investigators. An estimated 826 UW-based SOM regular and research faculty worked on those grants. In addition to these NIH awards managed by the University of Washington, 358 NIH awards were received by UW School of Medicine faculty and were managed by affiliated institutions (e.g., Fred Hutchinson Cancer Research Center, Seattle Children's Hospital, and Seattle Biomedical Research Institute). In total, NIH awards to UW Medicine faculty were \$611.4 million in federal fiscal year 2011, an increase of \$24.1 million (4%) over federal fiscal year 2010 when excluding ARRA funding received in federal fiscal year 2010. ARRA funding was a factor in federal fiscal years 2009 and 2010, with UW Medicine receiving \$129.1 million in 2009 and \$130.5 million in 2010.

UW Medicine faculty were second in the United States among all medical schools, and first among all public medical schools, in NIH research funding based on federal fiscal year 2011 awards.

----- (\$ in millions) -----

Institution	2007 NIH Awards	2008 NIH Awards	2009 NIH Awards	2010 NIH Awards	2011 NIH Awards	Average Annual
Harvard	\$1,178.5	\$1,228.7	\$1,413.1	\$1,729.2	\$1,346.3	3.4%
U of Washington	\$579.7	\$566.1	\$713.2	\$717.8	\$611.4	1.3%
Johns Hopkins	\$450.8	\$471.9	\$444.7	\$480.0	\$586.6	6.8%
UCLA	\$426.7	\$493.9	\$468.7	\$569.4	\$552.1	6.7%
UCSF	\$442.7	\$457.3	\$471.2	\$535.9	\$539.6	5.1%
U of Pennsylvania	\$486.7	\$516.2	\$641.6	\$662.0	\$533.6	2.3%
Columbia	\$362.3	\$342.9	\$468.3	\$473.1	\$424.6	4.0%
Yale	\$320.2	\$340.5	\$353.9	\$408.8	\$398.1	5.6%
Michigan	\$320.2	\$347.5	\$443.4	\$447.1	\$382.1	4.5%
Washington Univ.	\$347.0	\$347.2	\$348.0	\$431.6	\$372.3	1.8%
U of Pittsburgh	\$358.3	\$354.6	\$410.2	\$410.9	\$368.2	0.7%
Vanderbilt	\$285.8	\$306.1	\$315.1	\$406.9	\$353.9	5.5%
Cornell	\$239.7	\$233.1	\$275.2	\$321.6	\$339.3	9.1%
Stanford	\$259.0	\$236.2	\$265.0	\$344.9	\$329.7	6.2%
Duke	\$369.4	\$338.7	\$398.8	\$412.6	\$328.8	-2.9%

UW Medicine's comparative success in NIH funding is due to a number of factors, including the interdisciplinary breadth of our research programs, the addition of new laboratory space at South Lake Union, and the increased emphasis on 21st century science, such as genomics, proteomics, regenerative medicine, and global health research.

LOOKING FORWARD – FY 2013

Several key internal and external factors will continue to influence UW Medicine's financial performance in FY 2013 and beyond. External factors include the general state of the economy, the impact of state budget reductions on healthcare funding for governmental programs, federal health reform legislation, and the federal budget. Significant internal factors influencing performance include UW Medicine's continued success in implementing rapid and system-wide process improvements that mitigate the impact of state healthcare program budget reductions as well as executing on our strategic priorities. We recognize and acknowledge the major demands and challenges to UW Medicine in the short and long term and are proactively addressing them. This section presents some of our actions to date, as well as going forward, that will allow UW Medicine to perform and remain financially healthy.

Imperative to reduce costs with declining payments for services from all payers

- Performance improvement initiatives that have been built into FY13 budgets total \$80 million. Explicit operating plans have been developed and are being implemented to assure that these improvements occur and continue to support quality of care and patient safety.
- Specific services have been moved and consolidated into our community hospitals to optimize efficiency and access to care.

Balancing our social responsibility to provide the highest quality of care to all we serve with the recognition that not all health care systems in our region share this obligation

- UW Medicine provided \$292 million in charity care in 2012, an increase of \$43 million over the prior year.
- Leadership has worked proactively with other hospitals and health care providers in the community to share in this responsibility, which has resulted in an increase in charity care reported by others.
- Contracting with all the new Medicaid Managed Care plans in 2013 and beyond will assure that we are able to continue to serve the newly eligible Medicaid beneficiaries in 2014 as well as beginning to receive payment for the currently uninsured that will be eligible for the new insurance exchange products.

The ability to be successful in the health care environment of the future requires that UW Medicine continue to successfully accomplish its internal integration activities and execute its priorities as reflected in its strategic plan

- Priorities for the strategic plan are focused on providing better care for patients, better health for the populations, and reduced per capita costs.
- Significant accomplishments have occurred over the past four years in the five priority areas of building clinical programs, building networks and affiliations, delivering excellent service, delivering high-quality, safe and effective patient care, and enhancing the integration of research, teaching, and patient care.
- The UW Medicine Operational Integration Oversight Committee (OIOC) began its work at Valley Medical Center in August 2011. More than 20 clinical initiatives have been completed or are in process.

Financing health care in the future will require that UW Medicine be prepared to assume financial risk as the transition takes place from being paid for each service provided to accepting fixed payments for taking care of a specific population

- UW Medicine is in the process of creating an Accountable Care Organization (ACO) to contract with payers, large employers, and others.
- Competencies to be successful as an ACO are being developed and/or refined including care management, performance management, network operations, compliance, administration, and information management/analytics.
- A relationship has been established with an actuarial firm to provide consultation on potential risk arrangements.

Payment for services in the future will be based on UW Medicine's ability to deliver high quality, safe and effective care

- The UW Medicine Board Patient Safety and Quality Committee was established.
- Specific metrics have been identified and goals established across a broad range of appropriate indicators.
- Five additional safety and quality improvement initiatives have been launched and funded.

UW Medicine needs to continue to deliver world class research as the federal government experiences significant fiscal challenges

- The development of new research space at South Lake Union is a major step in ensuring the continued growth of UW Medicine's research programs.
- Continued development of information technology platforms to support the needs of researchers are occurring.
- Aggressive recruitment continues to attract strong research professionals to UW Medicine.
- Work to assure a supportive environment for interdisciplinary and translational research continues with a focus on retaining leaders of important research areas.

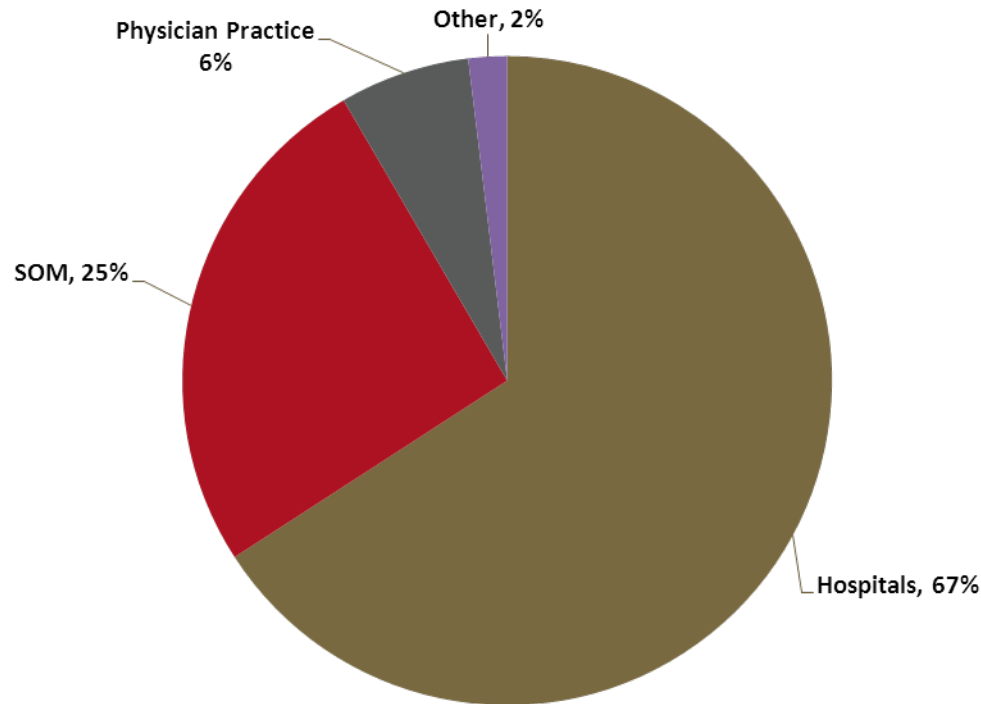
Our ability to be successful going forward in the face of these significant challenges requires that UW Medicine have strong, effective and visionary leadership, make well-informed strategic choices, recruit and retain excellent staff and faculty, implement best practices in all aspects of its business, and strengthen its financial health to be able to invest in its future.

UW Medicine
Annual Financial Report
to the University of Washington
Board of Regents

November 8, 2012

UW Medicine Annual Financial Report

FY 2012 Revenue by Entity



\$3.6 billion in total revenue
Increase of 17% over FY11

UW Medicine Annual Financial Report

Positive financial performance

	Budget FY 2012	Actual FY 2012	Increase	% Change
Hospital and Clinical Total Income (millions)	\$41.7	\$49.9	\$8.2	20%

- Overall hospital volumes remained relatively flat. However, complexity and severity of patients increased.
- Total revenue from the hospitals, clinics, and practice plan totaled \$2.6B. Net income of \$49.9M represents a 1.9% margin.

UW Medicine Annual Financial Report

School of Medicine revenue exceeded budget by 3%

	Budget FY 2012	Actual FY 2012	Increase	% Change
School of Medicine Revenue (millions)	\$1,111	\$1,149	\$38	3%

- Research continues to grow. Grant and contract awards excluding American Recovery and Reinvestment Act (ARRA) funds totaled \$611M in FY12 compared to \$574M in FY11, an increase of 6%
- UW Medicine remained second in the U.S. among medical schools in NIH research funding for FY11

UW Medicine

UW Medicine Annual Financial Report

- Operating expenses were managed to budget
- Clinical entities consolidated balance sheet remained stable
 - Cash and investments increased \$80M
 - Days in accounts receivable stable and in line with benchmarks
- School of Medicine reserves at June 30, 2012 of \$307M compared to \$289M for the prior year

UW Medicine Annual Financial Report

Looking Forward – FY2013

- Imperative to reduce costs
- Social responsibility to serve all walks of life
- Continued integration and implementation of strategic plan
- Increased assumption of financial risk under healthcare reform
- Future payments for services based on value defined by high quality, safe and effective care
- Continue to deliver world class research as the federal government experiences fiscal challenges