



**SHRINERS HOSPITALS FOR CHILDREN**

Combined Financial Statements

December 31, 2009 and 2008

(With Independent Auditors' Report Thereon)

# SHRINERS HOSPITALS FOR CHILDREN

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**KPMG LLP**  
Suite 1700  
100 North Tampa Street  
Tampa, FL 33602

## **Independent Auditors' Report**

The Board of Directors  
Shriners Hospitals for Children:

We have audited the accompanying combined statements of financial position of Shriners Hospitals for Children as of December 31, 2009 and 2008, and the related combined statements of operations, changes in net assets, and cash flows for the years then ended. These combined financial statements are the responsibility of the management of Shriners Hospitals for Children. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Shriners Hospitals for Children's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Shriners Hospitals for Children as of December 31, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in note 1(o) to the combined financial statements, Shriners Hospitals for Children has elected to change its method of accounting for the subsequent valuation of donated real estate, mineral interests, and other miscellaneous assets in 2009.

**KPMG LLP**

March 29, 2010  
Certified Public Accountants

## SHRINERS HOSPITALS FOR CHILDREN

### Combined Statements of Financial Position

December 31, 2009 and 2008

(In thousands)

<b>Assets</b>	<b>2009</b>	<b>2008</b>
Cash and cash equivalents	\$ 7,830	4,979
Cash and cash equivalents held as collateral under securities lending transactions	781,883	848,406
Receivables	9,067	5,059
Accrued interest and dividends	24,773	27,605
Patient transportation funds held by Shrine temples	43,479	44,493
Inventories and deferred charges	10,937	17,505
Long-term investments:		
Marketable securities	6,325,300	5,704,474
Charitable gift annuities	23,763	22,614
Beneficial interest in trusts	465,835	417,942
Real estate and mineral interests	149,925	161,373
Miscellaneous investments	12,770	13,371
Estates in process	299,568	203,913
Land, buildings, and equipment, net of accumulated depreciation	766,860	729,962
Total assets	\$ 8,921,990	8,201,696
<b>Liabilities and Net Assets</b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 89,562	89,940
Pension benefits	147,606	165,858
Liabilities under securities lending transactions	781,883	848,406
Other liabilities	36,540	36,493
Total liabilities	1,055,591	1,140,697
Net assets (net of cumulative foreign currency translation adjustment of \$9,539 in 2009 and \$8,610 in 2008):		
Unrestricted:		
Operations	5,773,860	5,153,952
Land, buildings, and equipment	766,860	729,962
Total unrestricted	6,540,720	5,883,914
Temporarily restricted	380,319	278,887
Permanently restricted	945,360	898,198
Total net assets	7,866,399	7,060,999
Total liabilities and net assets	\$ 8,921,990	8,201,696

See accompanying notes to combined financial statements.

## SHRINERS HOSPITALS FOR CHILDREN

### Combined Statements of Operations

Years ended December 31, 2009 and 2008

(In thousands)

	2009	2008
Operating revenues and other support:		
Investment income:		
Interest	\$ 99,708	123,331
Dividends	78,738	117,121
Other investment income	36,028	34,115
Investment management fees	(14,272)	(20,150)
Bequests released from restrictions used for operations	182,784	216,445
Donations	35,633	35,195
Fund raising and special events	23,991	34,078
Hospital assessments	1,544	1,633
Reimbursements from Canadian Provinces	5,707	5,958
Other	6,670	2,392
	456,531	550,118
Operating expenses:		
Hospitals	573,790	611,430
Research	33,101	33,240
Headquarters, administrative, and board related	46,824	52,854
Fund raising and special events	18,057	24,948
	671,772	722,472
Decrease in net assets from operating activities	(215,241)	(172,354)
Nonoperating gains (losses):		
Gain (loss) on investments:		
Net realized losses from investments	(294,643)	(488,392)
Net unrealized gains (losses) on investments	1,171,083	(1,907,119)
	876,440	(2,395,511)
Life memberships	143	148
Change in patient transportation funds held by Shrine temples	(1,014)	522
Pension-related changes other than net periodic pension costs	(907)	(65,561)
Other, net	(3,544)	(5,690)
Foreign currency translation adjustments	929	(1,682)
	872,047	(2,467,774)
Increase (decrease) in unrestricted net assets	\$ 656,806	(2,640,128)

See accompanying notes to combined financial statements.

## SHRINERS HOSPITALS FOR CHILDREN

### Combined Statements of Changes in Net Assets

Years ended December 31, 2009 and 2008

(In thousands)

	<b>2009</b>	<b>2008</b>
Unrestricted net assets:		
Decrease in net assets from operating activities	\$ (215,241)	(172,354)
Nonoperating gains (losses):		
Gain (loss) on investments:		
Net realized losses from investments	(294,643)	(488,392)
Net unrealized gains (losses) on investments	1,171,083	(1,907,119)
Total gain (loss) on investments	876,440	(2,395,511)
Life memberships	143	148
Change in patient transportation funds held by Shrine temples	(1,014)	522
Pension related changes other than net periodic pension costs	(907)	(65,561)
Other, net	(3,544)	(5,690)
Foreign currency translation adjustments	929	(1,682)
Total nonoperating gains (losses)	872,047	(2,467,774)
Increase (decrease) in unrestricted net assets	656,806	(2,640,128)
Temporarily restricted net assets:		
Bequests	264,613	188,027
Donations	11,318	5,577
Other, net	(991)	(1,340)
Net realized gain from investment	1,085	—
Net unrealized gains from investments	8,191	7,526
Net assets released from restrictions used for operations	(182,784)	(216,445)
Increase (decrease) in temporarily restricted net assets	101,432	(16,655)
Permanently restricted net assets:		
Bequests	8,384	2,824
Donations	12,339	5,370
Other investment income	7	—
Other, net	—	23
Net realized loss from investment	(107)	—
Net unrealized gains (losses) from investments	26,539	(106,160)
Increase (decrease) in permanently restricted net assets	47,162	(97,943)
Increase (decrease) in net assets	805,400	(2,754,726)
Net assets, beginning of year, as restated (see note 1(o))	7,060,999	9,815,725
Net assets, end of year	\$ 7,866,399	7,060,999

See accompanying notes to combined financial statements.

## SHRINERS HOSPITALS FOR CHILDREN

### Combined Statements of Cash Flows

Years ended December 31, 2009 and 2008

(In thousands)

	<b>2009</b>	<b>2008</b>
Cash flows from operating activities:		
Change in net assets	\$ 805,400	(2,754,726)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation	45,425	45,529
Loss (gain) on disposal of property and equipment	1,411	(403)
Realized and unrealized (gains) losses on investments	(912,148)	2,494,145
Gifts and bequests designated by the board or restricted by donor for long-term investment	(273,140)	(190,999)
Pension related changes other than net period pension costs	907	65,561
Changes in operating assets and liabilities:		
Receivables	(4,008)	8,069
Accrued interest and dividends	(2,832)	(1,763)
Patient transportation funds held by Shrine temples	1,014	(522)
Inventories and deferred charges	6,568	(16,676)
Beneficial interest in trusts	(47,893)	92,433
Estates in process	(95,655)	33,830
Accounts payable and accrued expenses	(378)	5,796
Pension benefits	(19,159)	(303)
Net cash used in operating activities	(494,488)	(220,029)
Cash flows from investing activities:		
Additions to property and equipment	(83,734)	(66,655)
Proceeds from sale of investments	4,183,691	11,557,682
Investment purchases	(3,875,805)	(11,465,681)
Net cash provided by investing activities	224,152	25,346
Cash flows from financing activities:		
Gifts and bequests designated for board endowment	264,613	188,027
Gifts and bequests permanently restricted by donors	8,384	2,824
Life memberships	143	148
Change in other liabilities	47	(5,001)
Net cash provided by financing activities	273,187	185,998
Net increase (decrease) in cash and cash equivalents	2,851	(8,685)
Cash and cash equivalents at beginning of year	4,979	13,664
Cash and cash equivalents at end of year	\$ 7,830	4,979

See accompanying notes to combined financial statements.

## SHRINERS HOSPITALS FOR CHILDREN

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

### (1) Summary of Significant Accounting Policies

#### (a) Combined Organizations

Shriners Hospitals for Children (the Hospitals) provide quality, specialized medical care, in the areas of orthopaedics, severe burns, and spinal cord injuries, through a network of 22 hospitals located throughout the United States, Canada, and Mexico. This medical care is provided at no cost to patients, families, or third-party payors. The Hospitals also fund intensive programs in pediatric orthopaedic and burns research. The Hospitals rely principally on gifts and investment earnings to support their operations and research programs.

The combined financial statements of Shriners Hospitals for Children include the following organizations:

- Shriners Hospitals for Children, a Colorado Corporation
- Shriners Hospitals for Children, a Canadian Corporation
- Shriners Hospitals for Children (Quebec) Inc.
- The Shriners' Hospital for Children, a Massachusetts Corporation
- Shriners Hospitals for Children, a Mexican Association

Additionally, the combined financial statements include the activities of Promotora Mexicana de Servicios Medicos S.A. de C.V., a Mexican Corporation, which was organized to facilitate the construction of the Mexico City hospital. All significant accounts and transactions between Hospital corporations have been eliminated in combination.

Shriners Hospitals for Children, a Colorado Corporation and The Shriners' Hospital for Children, a Massachusetts Corporation, have been recognized as exempt from U.S. federal income tax on related income under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) of the Internal Revenue Code. The Canadian and Quebec Corporations and the Mexican Association and Corporation are also exempt from income tax on related income in accordance with the laws of their respective countries.

Shriners Hospitals for Children Employee Disaster Relief Fund, a District of Columbia Nonprofit Corporation, which has been recognized as exempt from U.S. federal income tax on related income under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) of the Internal Revenue Code, was organized to provide "qualified disaster relief payments" to employees of Shriners Hospitals for Children, the family members of such employees, and other persons who are victims of and suffer from a "qualified disaster."

On January 1, 2009, the Hospitals adopted Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 740, *Income Taxes*. There was no impact on the Hospitals' combined financial statements as a result of the adoption of FASB ASC 740.



# SHRINERS HOSPITALS FOR CHILDREN

## Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

**(b) Use of Estimates**

The preparation of the combined financial statements in accordance with generally accepted accounting principles requires management of the Hospitals to make a number of estimates and assumptions that affect the reported amounts in the combined financial statements and accompanying notes to combined financial statements. Actual results could differ from those estimates.

Significant estimates have been made by management with regards to estates in process and beneficial interests in trusts. These estimates are subject to significant fluctuation due to changes that occur in the valuation of assets associated with these estates and trusts and the timing of information received from trustees and executors of these estates and trusts. Actual results could differ materially from these estimates, making it reasonably possible that a material change in these estimates could occur in the near term.

**(c) Basis of Presentation**

The combined financial statements are presented on the accrual basis of accounting. Contributions received and unconditional promises to give are measured at their fair values and are reported as increases in net assets. The Hospitals report gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets, or if they are designated as support for future periods. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the combined statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted support.

- Unrestricted net assets consist of investments and otherwise unrestricted amounts that are available for use in carrying out the activities of the Hospitals. The majority of unrestricted net assets as of December 31, 2009 and 2008 represent board designated endowment.
- Temporarily restricted net assets represent those amounts which are not available until future periods or are donor restricted for specific purposes. The Hospitals report estates in process, charitable lead trusts, and charitable remainder trusts, as increases in temporarily restricted net assets as these assets are not available for expenditure until future periods.
- Permanently restricted net assets result from gifts and bequests from donors who place restrictions on the use of the funds, which mandate that the original principal be invested in perpetuity. Permanently restricted net assets also include perpetual lead trusts.

**(d) Operating Measure**

Changes in net assets from operating activities represents the revenues, gains, and other support designated to operate the Hospitals, less expenses and other costs associated with Hospital operating and research activities and costs to generate operating revenues.

## SHRINERS HOSPITALS FOR CHILDREN

### Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

**(e) Liquidity**

Assets are presented in the accompanying combined statements of financial position according to their nearness of conversion to cash, and liabilities according to the nearness of their maturity and resulting use of cash.

**(f) Cash and Cash Equivalents**

The Hospitals consider all highly liquid investments made from operating cash accounts and with a maturity of three months or less when purchased to be cash equivalents.

**(g) Securities Loaned**

FASB ASC 860, *Transferring and Servicing*, requires the Hospitals to recognize cash received as collateral for assets transferred to brokers in security lending transactions along with the obligation to return the cash. The Hospitals generally receive collateral in the form of cash in an amount in excess of the fair value of securities loaned. The Hospitals monitor the fair value of securities loaned on a monthly basis with additional collateral obtained as necessary. At December 31, 2009 and 2008, the Hospitals held \$781,883 and \$848,406, respectively of cash and marketable securities as collateral deposits. The collateral is included as both an asset and a liability in the Hospitals' combined statements of financial position. The securities on loan had a fair value of \$757,883 and \$828,958 at December 31, 2009 and 2008, respectively, and are included in marketable securities in the accompanying combined statements of financial position.

**(h) Inventories**

Inventories of supplies are stated at the lower of cost (first-in, first-out method) or market.

**(i) Long-Term Investments**

The following long-term investments comprise the Hospitals board-designated endowment: marketable securities, charitable gift annuities, beneficial interest in trusts, real estate and mineral interests and miscellaneous investments. It is the Board's policy to maintain a long-term investment portfolio to support the operating and research activities of the Hospitals.

Marketable securities are measured at fair value based on quoted market prices at the reporting date for these or similar investments. Investments in real estate and mineral interests and miscellaneous investments are reported at fair value at the date of contribution and subsequently measured at fair value based on various sources of information depending on the asset type (see note 1(o)). Investment income (including gains and losses on investments, interest, and dividends) is included in the combined statements of operations as increases or decreases in unrestricted net assets unless the income is restricted by donor or law.

The Hospitals have a beneficial interest in a variety of trust agreements. Many of these trusts are charitable lead trusts where the Hospitals receive distributions from the trust, which in most cases are administered by a third party. Perpetual lead trusts are recorded at the fair value of the trust underlying assets and are classified as permanently restricted net assets. All other charitable lead

## SHRINERS HOSPITALS FOR CHILDREN

### Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

trusts are recorded at the present value of the estimated future distributions expected to be received by the Hospitals, and are classified as temporarily restricted net assets.

Charitable remainder trusts and pooled income funds represent trust agreements where the Hospitals maintain custody of the related assets and make specified distributions to a designated beneficiary or beneficiaries over the term of the trust. Assets under both types of trusts are recorded at fair value. Annuity liabilities associated with charitable remainder trusts are determined based on the present value of the estimated future payments to be paid to the designated beneficiaries. Deferred income is recognized on gifts to pooled income funds representing the discounted value of the assets for the estimated time period until the donor's death. The difference between the recorded assets and the annuity liabilities or deferred income associated with pooled income funds is classified as temporarily restricted net assets.

Subsequent adjustments to the carrying value of the respective assets and related liabilities or deferred income are recognized in the combined statements of operations and combined statements of changes in net assets and are included in unrealized gains and losses in their respective net asset category.

Included in other liabilities in the accompanying combined statements of financial position are annuity liabilities of \$25,026 and \$25,338 and deferred income of \$11,514 and \$11,155 at December 31, 2009 and 2008, respectively.

**(j) *Estates in Process***

The Hospitals recognize a receivable and revenue for their interest in estates in process based on the inventories of estate assets and conditions contained in the respective wills. Amounts expected to be received in future years are discounted to provide estimates in current year dollars. The Hospitals record estates in process (when the court declares the related will valid) as either temporarily restricted net assets, as these assets will not be available for expenditures until future periods (typically one to five years), or as permanently restricted net assets. As funds from an estate (other than permanently restricted) are collected, temporarily restricted net assets are reclassified to unrestricted net assets, and reported in the combined statements of operations and changes in net assets as net assets released from restrictions.

**(k) *Land, Buildings, and Equipment***

Land, land improvements, buildings, and equipment are stated at cost, if purchased, or at estimated fair value at date of receipt if acquired by gift. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets.

**(l) *Impairment or Disposal of Long-Lived Assets***

The Hospitals account for long-lived assets in accordance with the provisions of FASB ASC Topic 360-10-35 which requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

# SHRINERS HOSPITALS FOR CHILDREN

## Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. There are no such impairment losses recorded as of December 31, 2009 and 2008.

**(m) *Foreign Currency Translation***

Revenues and expenses of the Canadian and Quebec corporations and the Mexican Association and Corporation are translated using average exchange rates during the year, while monetary assets and liabilities are translated into U.S. dollars using current exchange rates at the end of the year. Nonmonetary asset and liability items (land, buildings, and equipment) and related revenues, expenses, gains and losses are remeasured using historical exchange rates. Resulting translation adjustments are accumulated in the combined statements of financial position caption "Cumulative foreign currency translation adjustment," a separate component of net assets.

**(n) *Contributed Services***

No amounts have been reflected in the combined financial statements for contributed services. The Hospitals' programs pay for most services requiring specific expertise. However, many individuals (Shriners and non-Shriners) volunteer their time at the Hospitals and perform a variety of tasks that assist the Hospitals with specific programs and various committee assignments.

**(o) *Change in Accounting Principle***

During the year ended December 31, 2009, the Hospitals' management and Investment Committee determined that it would be preferable to change the valuation method used for subsequent measurement of real estate, mineral interests and other miscellaneous assets from a cost basis to a fair value valuation. This change was preferable as it will provide users of the financial statements with the true financial condition of the Hospital's endowment. This is important, as many decisions are made throughout the year and for future strategic planning based on these values. In addition, this change will then enable all assets of the endowment to be consistently valued at fair value.

This change results in recognition in the Hospitals' combined financial statements of approximately \$7,642 of nonoperating unrealized gains on investments for the year ended December 31, 2008, and approximately \$99,579 change to beginning net assets in 2008.

**(p) *Reclassifications***

Certain amounts from the 2008 financial statements have been reclassified to conform with the 2009 financial statement presentation.

**SHRINERS HOSPITALS FOR CHILDREN**

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

**(2) Long-Term Investments**

Marketable securities at December 31, 2009 and 2008 consist of:

	<b>2009</b>		<b>2008</b>	
	<b>Cost</b>	<b>Fair value</b>	<b>Cost</b>	<b>Fair value</b>
Short-term investments	\$ 84,295	84,295	329,113	329,113
U.S. government securities	1,429,259	1,473,380	1,406,937	1,496,164
Corporate bonds	564,855	571,912	591,201	510,376
International stocks	820,604	944,178	963,032	780,501
Common and preferred stocks	3,096,449	3,251,535	3,273,245	2,588,320
	\$ 5,995,462	6,325,300	6,563,528	5,704,474

Investment income and total return on all long-term investments was comprised of the following components for the years ended December 31, 2009 and 2008:

	<b>2009</b>	<b>2008</b>
Interest	\$ 99,708	123,331
Dividends	78,738	117,121
Trust income	17,704	19,961
Rents and royalties	8,334	13,330
Other income	9,997	824
Less investment management fees	(14,272)	(20,150)
Total income from investments	200,209	254,417
Net realized losses from investments	(293,665)	(488,392)
Net unrealized gains (losses) from investments	1,205,813	(2,005,753)
Total return on investments	\$ 1,112,357	(2,239,728)

**SHRINERS HOSPITALS FOR CHILDREN**

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

**(3) Land, Buildings, and Equipment**

Land, buildings, and equipment at December 31, 2009 and 2008 consist of:

	<u>2009</u>	<u>2008</u>	<u>Estimated useful lives</u>
Land	\$ 29,744	25,573	—
Land improvements	11,578	11,384	5 – 20 years
Buildings	822,256	821,775	40 – 50 years
Equipment	<u>338,397</u>	<u>334,875</u>	4 – 25 years
	1,201,975	1,193,607	
Less accumulated depreciation	<u>(566,964)</u>	<u>(546,216)</u>	
	635,011	647,391	
Projects in process	22,972	18,967	
Construction in progress	<u>108,877</u>	<u>63,604</u>	
Land, buildings, and equipment, net	<u>\$ 766,860</u>	<u>729,962</u>	

**(4) Construction and Other Major Capital Projects**

Construction and other major capital projects committed to by the Board are as follows:

<u>Project</u>	<u>Total appropriation</u>	<u>Unexpended at December 31, 2009</u>
Honolulu	\$ 78,000	19,448
St. Louis	172,000	164,588
Portland	74,240	37,223
Philadelphia	14,172	11,924
Twin Cities	7,000	7,000
Other	10,008	4,072
Approved equipment expenditures:		
PACS imaging	22,417	6,115
Information systems projects	16,053	4,885
Other equipment	<u>13,852</u>	<u>13,852</u>
	<u>\$ 407,742</u>	<u>269,107</u>

## SHRINERS HOSPITALS FOR CHILDREN

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

### (5) **Transactions with the Imperial Council of the Ancient Arabic Order of the Nobles of the Mystic Shrine for North America**

The Hospitals' organizations were founded by the Imperial Council of the Ancient Arabic Order of the Nobles of the Mystic Shrine for North America (Imperial Council).

The International Headquarters building and equipment is owned by the Hospitals. A portion of the building is occupied by the Imperial Council, which is allocated a share of the operating costs and depreciation of the building and equipment. The allocation of the costs is based upon the portion of the building occupied by the Imperial Council in relation to the total occupied space in the building.

The Hospitals and the Imperial Council also share other costs based on the estimated fair value received by each organization. Additionally, hospital assessments, donations, and other charitable receipts from Shrine temples are collected and remitted to the Hospitals by the Imperial Council.

At December 31, 2009 and 2008, amounts of \$255 and \$1,431, respectively, were due from the Imperial Council, and are included in receivables in the accompanying combined statements of financial position.

### (6) **Fund-Raising Activities and Special Events**

The Hospitals are financially supported through each Shriner's annual hospital assessment, income from investments, gifts and bequests from the general public and from Shriners, and certain fund-raising activities conducted by Shriners. Shrine temples and Shriners raise funds for both fraternal and charitable purposes. Shrine fund-raising activities consist of paper sale donations, football games, golf tournaments, and other miscellaneous activities. The name "Shriners Hospitals for Children" may be used in connection with a fund raising activity by a Shrine temple or Shriner only with the written consent of the Imperial Council and the Hospitals when the proceeds are to benefit Shriners Hospitals for Children. Some of these funds are retained by individual Shrine temples for the support of their respective hospital patient transportation fund.

Through the efforts of the donor relations committee, which oversees the development activities of the Hospitals, gifts and bequests are solicited and received to support the operations of the Hospitals or are designated by the Board for endowment purposes. Although the costs of these activities are included in fund-raising expenses, the associated revenues are reported as bequests and donations in the accompanying combined statements of operations and combined statements of changes of net assets

The Hospitals also engage in other fund-raising activities to generate donations and to develop their donor base. These activities are conducted through an agreement with an unrelated third party.

**SHRINERS HOSPITALS FOR CHILDREN**

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

Fund raising and special events revenues and costs for the years ended December 31, 2009 and 2008 consist of the following:

	<u>2009</u>	<u>2008</u>
Revenues from Shrine temple sponsored events	\$ 9,063	9,941
Direct mail revenue	7,473	16,659
Other revenue	<u>7,455</u>	<u>7,478</u>
	\$ <u>23,991</u>	<u>34,078</u>
Fund-raising costs paid directly by Shrine temples in connection with fund-raising events	\$ 929	1,325
Donor relations expense	5,042	5,048
Direct mail expense	3,242	8,873
Other costs	<u>8,844</u>	<u>9,702</u>
	\$ <u>18,057</u>	<u>24,948</u>

Revenues from Shrine temple sponsored events are reported net of direct costs of \$2,860 and \$3,568 for 2009 and 2008, respectively.

During the year ended December 31, 2008, the Hospitals became the Host Organization and Title Sponsor of a PGA Tour golf tournament. The term of this agreement commenced with the 2008 event and will conclude after the 2012 tournament. The 2009 event yielded approximately \$6,048 in revenues. Expenses incurred on this event in 2009 were approximately \$7,415, creating a net loss on the event of \$1,367. The 2008 event yielded approximately \$6,499 in revenues. Expenses incurred on this event in 2008 were approximately \$8,684, creating a net loss on the event of \$2,185. These revenues and expenses are included above in other revenue and other costs.

**(7) Patient Transportation Funds Held by Shrine Temples**

Shrine temples pay for substantially all of the costs of transporting patients to individual Shriners Hospitals. These costs are supported by funds retained from fund-raising events held for the benefit of Shriners Hospitals for Children (see note 6), as well as local donations from Shriners and the general public. The activities of the Shrine temple patient transportation funds are reflected as a nonoperating change in patient transportation funds held by Shrine temples in the accompanying combined statements of operations.



**SHRINERS HOSPITALS FOR CHILDREN**

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

The activities of the patient transportation funds reflected for the years ended December 31, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
Temple revenues restricted for patient transportation	\$ 16,783	20,919
Patient transportation costs	<u>(17,797)</u>	<u>(20,397)</u>
Net change	<u>\$ (1,014)</u>	<u>522</u>

**(8) Retirement Plans and Other Postretirement Benefits**

The employees of U.S. hospitals are included in the Shriners Hospitals for Children Employees' Retirement Plan and the Shriners Hospitals for Children Supplemental Retirement Plan (collectively, the Pension Plans). Benefits are based on years of service and the employees' compensation during the highest five consecutive years of employment. Contributions are made to the Pension Plans in accordance with ERISA requirements. In addition, the Hospitals sponsor a postretirement life insurance plan (the Postretirement Plan).

The actuarially computed net periodic pension cost for the Shriners' Hospital Pension Plans and the Postretirement Plan for the years ended December 31, 2009 and 2008 included the following components:

	<u>Pension Plans</u>		<u>Postretirement Plan</u>	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
Service cost – benefits earned during the period	\$ 17,108	15,825	324	315
Interest cost on projected benefit obligation	19,852	18,444	529	509
Expected return on plan assets	(16,968)	(15,511)	—	—
Net amortized and deferral of unrecognized gains and losses	<u>2,460</u>	<u>2,033</u>	<u>320</u>	<u>335</u>
Net periodic pension cost	<u>\$ 22,452</u>	<u>20,791</u>	<u>1,173</u>	<u>1,159</u>

## SHRINERS HOSPITALS FOR CHILDREN

### Notes to Combined Financial Statements

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(In thousands)

The following table sets forth the Pension Plans' and the Postretirement Plan's funded status and amounts recognized in the combined statements of financial position as of December 31, 2009 and 2008, respectively (using a measurement date of December 31):

	<b>Pension Plans</b>		<b>Postretirement Plan</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 318,848	294,164	8,617	8,114
Effect of early measurement	—	6,017	—	146
Service cost	17,108	15,825	324	315
Interest cost	19,852	18,444	529	509
Actuarial (gain) loss	16,377	(5,433)	(303)	(305)
Benefits paid	(12,193)	(10,169)	(185)	(220)
Settlements	—	—	—	—
Benefit obligation at end of year	<u>359,992</u>	<u>318,848</u>	<u>8,982</u>	<u>8,559</u>
Change in plan assets:				
Fair value of plan assets at beginning of year	161,549	201,678	—	—
Effect of early measurement	—	1,713	—	—
Actual return on plan assets	29,356	(57,743)	—	—
Employer contributions	42,656	26,070	185	220
Benefits paid	(12,193)	(10,169)	(185)	(220)
Fair value of plan assets at end of year	<u>221,368</u>	<u>161,549</u>	<u>—</u>	<u>—</u>
Funded status at end of year	<u>\$ (138,624)</u>	<u>(157,299)</u>	<u>(8,982)</u>	<u>(8,559)</u>

The accumulated benefit obligation for the Pension Plans was \$288,114 and \$257,708 at December 31, 2009 and 2008, respectively. The accumulated benefit obligation differs from the benefit obligation above in that it includes no assumption about future compensation levels. It represents the actuarial present value of future payments to plan participants using current and past compensation levels.

Weighted average assumptions used to determine projected benefit obligations at December 31, 2009 and 2008 were as follows:

	<b>Pension Plans</b>		<b>Postretirement Plan</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Discount rate	6.00%	6.00%	6.00%	6.00%
Rate of compensation increase	4.00	4.00	N/A	N/A

**SHRINERS HOSPITALS FOR CHILDREN**

Notes to Combined Financial Statements

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(In thousands)

Weighted average assumptions used to determine the net periodic benefit costs of the Pension Plans and the Postretirement Plan are:

	<b>Pension Plans</b>		<b>Postretirement Plan</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Discount rate	6.00%	6.00%	6.00%	6.00%
Expected long-term rate of return on plan assets	7.50	7.75	N/A	N/A
Rate of compensation increase	4.00	4.00	N/A	N/A

The expected long-term rate of return is based on the portfolio as a whole and not on the sum of the returns on individual asset categories. The return is based exclusively on historical returns, without adjustments.

The following are deferred pension costs which have not yet been recognized in periodic pension expense but instead are accrued in unrestricted net assets as of December 31, 2009. Unrecognized actuarial losses represent unexpected changes in the projected benefit obligation and plan assets over time, primarily due to changes in assumed discount rates and investment experience. Unrecognized prior service cost is the impact of changes in plan benefits applied retrospectively to employee service previously rendered. Deferred pension costs are amortized into annual pension expense over the average remaining assumed service period for active employees.

	<b>Pension Plans</b>		<b>Postretirement Plan</b>	
	<b>Amounts recognized in unrestricted net assets at December 31, 2009</b>	<b>Amounts in unrestricted net assets to be recognized during the next fiscal year</b>	<b>Amounts recognized in unrestricted net assets at December 31, 2009</b>	<b>Amounts in unrestricted net assets to be recognized during the next fiscal year</b>
Actuarial loss (gain)	\$ 2,428	4,451	(14)	(34)
Prior service cost	32	32	300	300
Transition obligation	—	—	35	35
<b>Total</b>	<b>\$ 2,460</b>	<b>4,483</b>	<b>321</b>	<b>301</b>

**SHRINERS HOSPITALS FOR CHILDREN**

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

***Plan Assets***

The weighted average allocation of the Pension Plans' assets at December 31, 2009 and 2008 were as follows:

<b>Asset category</b>	<b>2009</b>	<b>2008</b>
Common stocks	27%	23%
Corporate and miscellaneous bonds	28	36
Mutual funds	43	32
Short-term investments	2	9
Total assets	100%	100%

The Hospitals' investment policies and strategies for pension benefits do not use target allocations for the individual asset categories. The Hospitals' investment goals are to maximize returns subject to specific risk management policies.

## SHRINERS HOSPITALS FOR CHILDREN

### Notes to Combined Financial Statements

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(In thousands)

The table below summarizes the Pension Plan's significant financial assets as of December 31, 2009:

	<u>December 31,</u> <u>2009</u>	<u>Fair value measurements at reporting date using</u>		
		<u>Quoted prices</u> <u>in active</u> <u>markets for</u> <u>identical assets</u> <u>(Level 1)</u>	<u>Significant</u> <u>other</u> <u>observable</u> <u>inputs</u> <u>(Level 2)</u>	<u>Significant</u> <u>unobservable</u> <u>inputs</u> <u>(Level 3)</u>
Assets:				
Investments:				
Northern Trust Global Investments Collective Funds Trust (a)	\$ 4,255	4,255	—	—
Artio International Equity Group Trust Fund (b)	21,179	—	21,179	—
Blackrock Alpha Tilts Fund (c)	24,550	—	24,550	—
Blackrock World Ex-US Alpha Tilts L Fund(d)	11,545	—	11,545	—
Nothern Trust Global Investments Collective Russell 2000 Index Fund - Nonlending (e)	21,032	—	21,032	—
Nothern Trust Global Investments Collective Extended Equity Market Index Fund - Lending (f)	3,532	—	3,532	—
Nothern Trust Global Investments Collective Daily S&P 500 Equity Index Fund - Lending (g)	34,726	—	34,726	—
Nothern Trust Global Investments Collective Daily S&P 500 Equity Index Fund - Nonlending (h)	38,682	—	38,682	—
Nothern Trust Global Investments Collective Daily Aggregate Bond Index Fund - Lending (i)	41,609	—	41,609	—
Nothern Trust Global Investments Collective Daily Aggregate Bond Index Fund - Nonlending (j)	20,258	—	20,258	—
Total	<u>221,368</u>	<u>4,255</u>	<u>217,113</u>	<u>—</u>

## SHRINERS HOSPITALS FOR CHILDREN

### Notes to Combined Financial Statements

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(In thousands)

- (a) This fund is composed of high-grade money market instruments with short maturities. The fund seeks to provide an investment vehicle for cash reserves while offering a competitive rate of return.
- (b) The fund seeks to provide long term growth of capital by investing primarily in a wide variety of international equity securities issued throughout the world, normally excluding the U.S.
- (c) This fund seeks to exceed the S&P 500.
- (d) This fund seeks to exceed the Morgan Stanley Capital International Europe Australasia Far East Free Index.
- (e) The primary objective of this fund is to approximate the risk and return characterized by the Russell 2000 Index. This index is commonly used to represent the small cap segment of the U.S. equity market. The fund does not participate in securities lending.
- (f) The primary objective of this fund is to approximate the risk and return characteristics of the Dow Jones U.S. Completion ex-LPs Total Stock Market Index. This fund may participate in securities lending.
- (g) The primary objective of this fund is to approximate the risk and return characteristics of the S&P 500 Index. The Index is commonly used to represent the large-cap segment of the U.S. equity market. This fund may participate in securities lending.
- (h) The primary objective of this fund is to approximate the risk and return characteristics of the S&P 500 Index. The Index is commonly used to represent the large-cap segment of the U.S. equity market. This fund does not participate in securities lending.
- (i) The primary objective of this fund is to provide investment results that approximate the overall performance of the Barclay's Capital Aggregate Bond Index. This fund may participate in securities lending.
- (j) The primary objective of this fund is to provide investment results that approximate the overall performance of the Barclay's Capital Aggregate Bond Index. This fund does not participate in securities lending.

The Pension Plan's Level 1 assets include short-term investments that are valued at the quoted market prices.

The Pension Plan's Level 2 assets include common and collective trust funds with fair values modeled by external pricing vendors.

#### ***Contributions***

Annual contributions are determined based upon calculations prepared by the plans' actuary. Expected contributions to the Pension Plans and the Postretirement Plan are \$24,020 and \$291, respectively, in 2010.

# SHRINERS HOSPITALS FOR CHILDREN

## Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

### ***Benefit Payments***

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid out of the plans:

	<u>Pension Plans</u>	<u>Postretirement Plan</u>
Fiscal year:		
2010	\$ 12,015	291
2011	13,362	314
2012	15,021	337
2013	17,742	363
2014	19,540	391
2015-2019	129,728	2,467

The Hospitals also have a retirement savings plan for all eligible employees. Under this plan, the Hospitals match 50% of the first 6% of voluntary contributions made from eligible compensation by employees. Matching contributions by the Hospitals to the retirement savings plan were \$1,455 and \$5,082 in 2009 and 2008, respectively.

Canadian and Mexican hospital employees are included in government retirement programs.

In March 2009, the Board voted to freeze entry of new participants into the Pension Plans effective May 1, 2009.

### **(9) Estimated Malpractice Costs and Other Contingencies**

The Hospitals are self-insured for claims attributed to malpractice and workers compensation from providing professional and patient care services. Claims alleging malpractice have been asserted against the Hospitals and are currently in various stages of litigation. Additional claims may be asserted against the Hospitals arising from services provided to patients through December 31, 2009. Liabilities for malpractice and workers compensation claims are established based on specific identification and historical experience using actuarial methodologies. It is the opinion of management that estimated malpractice and workers compensation claims accrued should be adequate to provide for potential losses resulting from both reported claims and claims incurred but not reported. Such amounts are recorded in accounts payable and accrued expenses on the accompanying combined statements of financial position.

The Hospitals are also a party to various other claims and legal actions arising in the ordinary course of business. Management does not believe that the ultimate outcome of such claims and legal actions will have a material adverse effect on the financial position or activities of the Hospitals.

## SHRINERS HOSPITALS FOR CHILDREN

Notes to Combined Financial Statements

December 31, 2009 and 2008

(In thousands)

### (10) Fair Value Measurements

FASB ASC Topic 820, *Fair Value Measurements and Disclosures*, defines fair value as the exit price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants on the measurement date. FASB ASC Topic 820 requires investments to be grouped into three categories based on certain criteria as noted below:

Level 1: Fair value is determined by using quoted prices for identical assets or liabilities in active markets.

Level 2: Fair value is determined by using other than quoted prices that are observable for the asset or liability (e.g., quoted prices for identical assets or liabilities in inactive markets, quoted prices for similar assets or liabilities in active markets, observable inputs other than quoted prices, and inputs derived principally from or corroborated by observable market data by correlation or other means).

Level 3: Fair value is determined by using inputs based on management assumptions that are not directly observable.

The tables below summarize the Hospitals' significant financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2009 and 2008:

	<u>December 31,</u> <u>2009</u>	<u>Fair value measurements at reporting date using</u>		
		<u>Quoted prices</u> <u>in active</u> <u>markets for</u> <u>identical assets</u> <u>(Level 1)</u>	<u>Significant</u> <u>other</u> <u>observable</u> <u>inputs</u> <u>(Level 2)</u>	<u>Significant</u> <u>unobservable</u> <u>inputs</u> <u>(Level 3)</u>
Assets:				
Long-term investments	\$ 6,977,593	2,668,336	4,147,547	161,710
Collateral under securities lending transactions	<u>781,883</u>	<u>781,883</u>	<u>—</u>	<u>—</u>
Liabilities:				
Annuity liabilities	\$ 25,026	—	25,026	—
Liabilities under securities lending transactions	<u>781,883</u>	<u>781,883</u>	<u>—</u>	<u>—</u>



**SHRINERS HOSPITALS FOR CHILDREN**

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December 31, 2009 and 2008

(In thousands)

	December 31, 2008	Fair value measurements at reporting date using		
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets:				
Long-term investments	\$ 6,319,774	2,389,622	3,756,440	173,712
Collateral under securities lending transactions	848,406	848,406	—	—
Liabilities:				
Annuity liabilities	\$ 25,338	—	25,338	—
Liabilities under securities lending transactions	848,406	848,406	—	—

The Hospitals' Level 1 assets and liabilities include investments in cash, cash equivalents, corporate equities, and debt and are valued at the quoted market prices.

The Hospitals' Level 2 assets include investments in U.S. Treasuries, government securities, corporate debt securities, derivatives, asset-backed securities, mineral interests, charitable gift annuities, beneficial interest in trusts, and miscellaneous investments with fair values modeled by external pricing vendors. Liabilities include annuity liabilities.

Level 3 assets include real estate, fixed income investments, and asset-back securities.

The tables below summarize the changes in Level 3 assets for the years ended December 31, 2009 and 2008:

	Fair value measurements using significant unobservable inputs (Level 3)			
	Fixed income investments	Equity investments	Other investments	Total
2009:				
Beginning balance	\$ 13,340	2,806	157,566	173,712
Total gains (losses) (realized/ unrealized) included in (decrease) increase in unrestricted net assets	2,502	3,596	948	7,046
Purchases, sales, issuances, and settlements	(2,014)	3,190	—	1,176
Transfers in and/or out of Level 3, net	(9,526)	(2,826)	(7,872)	(20,224)
Ending balance	\$ 4,302	6,766	150,642	161,710

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(In thousands)

	Fair value measurements using significant unobservable inputs (Level 3)			
	Fixed income investments	Equity investments	Other investments	Total
2008:				
Beginning balance	\$ 6,581	10,070	184,657	201,308
Total gains (losses) (realized/ unrealized) included in (decrease) increase in unrestricted net assets	(4,610)	(7,975)	(11,882)	(24,467)
Purchases, sales, issuances, and settlements	5,223	(3,215)	(12,335)	(10,327)
Transfers in and/or out of Level 3, net	6,146	3,926	(2,874)	7,198
Ending balance	\$ 13,340	2,806	157,566	173,712

Realized and unrealized gains (losses) included in changes in net assets for the years ended December 31, 2009 and 2008 are reported in investment income as follows:

	December 31	
	2009	2008
Total gains (losses) included in (decrease) increase in unrestricted net assets	\$ 7,046	(24,467)
Change in unrealized gains (losses) relating to assets still held at reporting date	8,064	(7,913)

## SHRINERS HOSPITALS FOR CHILDREN

### Notes to Combined Financial Statements

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(In thousands)

The fair values of the following investments have been estimated using the net asset value per share of the investments as of December 31, 2009. There are no unfunded commitments on any of these funds.

	<b>Fair value</b>	<b>Redemption frequency</b>	<b>Redemption notice period</b>
Northern Trust Global Investments			
Collective Daily S&P 500 Equity			
Index Fund – Lending (a)	\$ 1,126,397	Daily	None
Blackrock Alpha Tilts Fund (b)	485,622	Monthly	2 days
Total	\$ 1,612,019		

(a) The primary investment objective of the equity index fund is to match the risk and return characteristics of the S&P 500 Index. Funds that participate in the securities lending program have a twice-per-month redemption restriction, and a total redemption would require the Hospitals to fund its portion of any collateral shortfall.

(b) This fund seeks to exceed the S&P 500.

Estimates of fair values are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could affect the estimates.

#### (11) Endowment Funds

The Hospital's endowment consists of marketable securities, charitable gift annuities, beneficial interest in trusts, real estate and mineral interests, and miscellaneous investments. The endowment consists of both donor-restricted funds, as well as funds designated by the Board of Trustees to function as endowments.

The Hospital's Board of Directors (the Board) has interpreted the wishes of donors and state law as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Hospital's classify as permanently restricted net assets (a) the original value of gifts donated, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the endowment. Gifts given with a restriction of time or purpose, are added to the endowment as temporarily restricted funds. Upon the passage of time or completion of purpose, these funds are released as unrestricted. Funds designated by the Board as endowment funds are included as unrestricted endowment funds.

*Investment Return Objectives, Risk Parameters and Strategies.* The Hospital's have adopted investment and spending policies, approved by the Investment Committee, for endowment assets that attempt to provide a predictable stream of funding to support the hospital system, while also maintaining the purchase power of those endowment assets over the long-term. Accordingly, the investment process seeks to achieve an after-cost total real rate of return, including investment income, as well as, capital appreciation, which

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(In thousands)

exceeds the budgeted annual distribution with acceptable levels of risk. Endowment assets are invested in a well diversified asset mix, which includes equity and fixed-income securities, that is intended to result in a rate of return that has sufficient liquidity to provide a high level of cash distribution, while growing the funds, if possible. Therefore, the Hospital's expect its endowment assets, over time, to produce an average rate of return of approximately 7.25% annually. Actual returns in any given year may vary from this amount. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

*Spending policy.* The Board does not have a formal endowment spending policy. Generally, all investment return (excluding capital appreciation) is utilized in funding the Hospital's programs. In making this funding decision, the Board considers the long-term expected return on its investment assets, the nature and duration of the individual endowment funds, some of which must be maintained in perpetuity because of donor-restrictions, and the possible effects of inflation. The Board's goal is for its endowment funds to grow annually to maintain the purchasing power of the endowment assets, as well as, to provide additional real growth through new gifts and investment return.

Endowment net asset composition by type of fund, as of December 31, 2009, is as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total endowment net assets</u>
Board-designated endowment funds	\$ 6,511,758	—	—	6,511,758
Donor-restricted endowment funds	—	122,207	343,628	465,835
	<u>\$ 6,511,758</u>	<u>122,207</u>	<u>343,628</u>	<u>6,977,593</u>

Changes in endowment net assets for the year ended December 31, 2009, are as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total endowment net assets</u>
Balance, beginning of year	\$ 5,901,832	112,863	305,079	6,319,774
Contributions	—	11,318	12,110	23,428
Investment income	200,202	—	7	200,209
Net appreciation (depreciation)	876,440	9,276	26,432	912,148
Reclassifications	11,250	(11,250)	—	—
Withdrawals	(477,966)	—	—	(477,966)
Balance, end of year	<u>\$ 6,511,758</u>	<u>122,207</u>	<u>343,628</u>	<u>6,977,593</u>

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FASB ASC Topic 958-205-45-28 provides guidance on the net asset classification of donor-restricted endowment funds for a nonprofit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). FASB ASC Topic 958-205-45-28 also requires additional disclosures about an organization's endowment funds (both donor-restricted and board-designated endowment funds) whether or not the organization is subject to UPMIFA. Florida has not yet adopted UPMIFA and, therefore, the Hospitals are not subject to its provisions.

### **(12) Subsequent Events**

Effective December 31, 2009, the Hospitals adopted FASB ASC 855, *Subsequent Events*, which establishes principles and requirements for subsequent events and applies to accounting for and disclosure of subsequent events not addressed in other applicable generally accepted accounting principles. The Hospitals evaluated events subsequent to December 31, 2009 and through March 29, 2010, the date on which the financial statements were available for issuance.