

UNIVERSAL HEALTH SERVICES INC

Form 10-Q

May 08, 2009

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(MARK ONE)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2009

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-10765

**UNIVERSAL HEALTH SERVICES, INC.**

(Exact name of registrant as specified in its charter)

**DELAWARE**  
 (State or other jurisdiction of  
 incorporation or organization)

**23-2077891**  
 (I.R.S. Employer  
 Identification No.)

**UNIVERSAL CORPORATE CENTER**

**367 SOUTH GULPH ROAD**

**KING OF PRUSSIA, PENNSYLVANIA 19406**

(Address of principal executive offices) (Zip Code)

**Registrant's telephone number, including area code (610) 768-3300**

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common shares outstanding, as of April 30, 2009:

Class A	3,328,404
Class B	45,415,619
Class C	335,800
Class D	21,441

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**Table of Contents****PART I. FINANCIAL INFORMATION****UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(amounts in thousands, except per share amounts)

(unaudited)

	<b>Three Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
Net revenues	\$ 1,312,419	\$ 1,277,976
Operating charges:		
Salaries, wages and benefits	541,297	541,575
Other operating expenses	273,221	248,645
Supplies expense	173,967	179,239
Provision for doubtful accounts	118,978	119,797
Depreciation and amortization	51,134	46,743
Lease and rental expense	17,072	17,555
	1,175,669	1,153,554
Income from continuing operations before interest expense and income taxes	136,750	124,422
Interest expense, net	12,638	13,479
Income from continuing operations before income taxes	124,112	110,943
Provision for income taxes	42,078	37,611
Income from continuing operations	82,034	73,332
Income from continuing operations attributable to minority interests	14,493	13,279
Income from continuing operations attributable to UHS	67,541	60,053
Income from discontinued operations, net of income tax expense		1,610
Net income attributable to UHS	\$ 67,541	\$ 61,663
Basic and diluted earnings per share attributable to UHS:		
From continuing operations	\$ 1.37	\$ 1.17
From discontinued operations		0.03
Total basic and diluted earnings per share	\$ 1.37	\$ 1.20
Weighted average number of common shares - basic	49,206	51,263
Other share equivalents		17
Weighted average number of common shares and equivalents - diluted	49,206	51,280

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Net income attributable to UHS and minority interest:

Net income attributable to UHS	\$ 67,541	\$ 61,663
Net income attributable to minority interests	14,493	13,279
Net income	\$ 82,034	\$ 74,942

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

**Table of Contents****UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(amounts in thousands, unaudited)

	March 31, 2009	December 31, 2008
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 9,423	\$ 5,460
Accounts receivable, net	652,854	625,437
Supplies	77,022	76,043
Other current assets	32,392	26,375
Deferred income taxes	39,249	34,522
Current assets held for sale	21,580	21,580
<b>Total current assets</b>	<b>832,520</b>	<b>789,417</b>
Property and equipment	3,446,127	3,355,974
Less: accumulated depreciation	(1,300,845)	(1,255,682)
	2,145,282	2,100,292
Other assets:		
Goodwill	733,882	732,937
Deferred charges	11,440	10,428
Other	112,193	109,388
	<b>\$ 3,835,317</b>	<b>\$ 3,742,462</b>
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Current maturities of long-term debt	\$ 8,725	\$ 8,708
Accounts payable and accrued liabilities	591,427	542,008
Federal and state taxes	44,211	10,409
<b>Total current liabilities</b>	<b>644,363</b>	<b>561,125</b>
Other noncurrent liabilities	403,325	407,652
Long-term debt	938,844	990,661
Deferred income taxes	11,267	12,439
UHS common stockholders' equity	1,596,544	1,543,850
Minority interest	240,974	226,735
<b>Total equity</b>	<b>1,837,518</b>	<b>1,770,585</b>
	<b>\$ 3,835,317</b>	<b>\$ 3,742,462</b>

See accompanying notes to these condensed consolidated financial statements.



**Table of Contents****UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(amounts in thousands, unaudited)

	<b>Three months ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
<b>Cash Flows from Operating Activities:</b>		
Net income attributable to UHS	\$ 67,541	\$ 61,663
<i>Adjustments to reconcile net income to net cash provided by operating activities:</i>		
Depreciation & amortization	51,135	47,370
<i>Changes in assets &amp; liabilities, net of effects from acquisitions and dispositions:</i>		
Accounts receivable	(44,894)	(63,970)
Construction management and other receivable	17,477	383
Accrued interest	10,491	8,999
Accrued and deferred income taxes	28,062	31,301
Other working capital accounts	6,581	27,777
Other assets and deferred charges	(1,902)	1,351
Other	(1,073)	(1,714)
Minority interest in earnings of consolidated entities	14,239	12,906
Accrued insurance expense, net of commercial premiums paid	20,014	19,376
Payments made in settlement of self-insurance claims	(15,669)	(13,766)
 Net cash provided by operating activities	 152,002	 131,676
 <b>Cash Flows from Investing Activities:</b>		
Property and equipment additions, net of disposals	(78,219)	(81,751)
Proceeds received from sale of assets		2,235
 Net cash used in investing activities	 (78,219)	 (79,516)
 <b>Cash Flows from Financing Activities:</b>		
Reduction of long-term debt	(51,800)	
Additional borrowings		33,180
Repurchase of common shares	(14,725)	(89,799)
Dividends paid	(3,962)	(4,072)
Issuance of common stock	667	1,093
 Net cash used in financing activities	 (69,820)	 (59,598)
 Increase (decrease) in cash and cash equivalents	 3,963	 (7,438)
Cash and cash equivalents, beginning of period	5,460	16,354
 Cash and cash equivalents, end of period	 \$ 9,423	 \$ 8,916
 <b>Supplemental Disclosures of Cash Flow Information:</b>		
Interest paid	\$ 3,966	\$ 6,407



Income taxes paid, net of refunds	\$ 13,784	\$ 7,642
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See accompanying notes to these condensed consolidated financial statements.

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**UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) General**

This Report on Form 10-Q is for the Quarterly period ended March 31, 2009. In this Quarterly Report, we, us, our, UHS and the Company refer to Universal Health Services, Inc. and its subsidiaries.

You should carefully review the information contained in this Quarterly Report, and should particularly consider any risk factors that we set forth in this Quarterly Report and in other reports or documents that we file from time to time with the Securities and Exchange Commission (the SEC). In this Quarterly Report, we state our beliefs of future events and of our future financial performance. In some cases, you can identify those so-called forward-looking statements by words such as may, will, should, expects, plans, anticipates, believes, estimates, potential, or continue or the negative of those words and other comparable words. You should be aware that those statements are only our predictions. Actual events or results may differ materially. In evaluating those statements, you should specifically consider various factors, including the risks related to healthcare industry trends and those detailed in our filings with the SEC including those set forth in our Annual Report on Form 10-K for the year ended December 31, 2008 in *Item 1A-Risk Factors* and in *Item 7 Management's Discussion and Analysis of Operations and Financial Condition - Forward Looking Statements and Risk Factors*. Those factors may cause our actual results to differ materially from any of our forward-looking statements.

The condensed consolidated financial statements include the accounts of our majority-owned subsidiaries and partnerships and limited liability companies controlled by us, or our subsidiaries, as managing general partner or managing member. The condensed consolidated financial statements included herein have been prepared by us, without audit, pursuant to the rules and regulations of the SEC and reflect all normal and recurring adjustments which, in our opinion, are necessary to fairly present results for the interim periods. The balance sheet at December 31, 2008 has been derived from the audited financial statements. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although we believe that the accompanying disclosures are adequate to make the information presented not misleading. It is suggested that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements, significant accounting policies and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2008.

**(2) Relationship with Universal Health Realty Income Trust and Related Party Transactions**

***Relationship with Universal Health Realty Income Trust:***

At March 31, 2009, we held approximately 6.6% of the outstanding shares of Universal Health Realty Income Trust (the Trust). We serve as Advisor to the Trust under an annually renewable advisory agreement pursuant to the terms of which we conduct the Trust's day-to-day affairs, provide administrative services and present investment opportunities. In addition, certain of our officers and directors are also officers and/or directors of the Trust. Management believes that it has the ability to exercise significant influence over the Trust, therefore we account for our investment in the Trust using the equity method of accounting. We earned an advisory fee from the Trust, which is included in net revenues in the accompanying condensed consolidated statements of income, of \$390,000 and \$367,000 during the three month periods ended March 31, 2009 and 2008, respectively. Our pre-tax share of income from the Trust was \$300,000 during each of the three month periods ended March 31, 2009 and 2008. The carrying value of this investment was \$8.6 million at March 31, 2009 and \$8.9 million at December 31, 2008, and is included in other assets in the accompanying condensed consolidated balance sheets. The market value of this investment, based on the closing price of the Trust's stock on the respective dates, was \$23.0 million at March 31, 2009 and \$25.9 million at December 31, 2008.

Total rent expense under the operating leases on the hospital facilities with the Trust was \$4.1 million and \$4.0 million during the three month periods ended March 31, 2009 and 2008, respectively. In addition, certain of our subsidiaries are tenants in several medical office buildings owned by limited liability companies in which the Trust holds non-controlling ownership interests.

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The table below details the renewal options and terms for each of our four hospital facilities leased from the Trust:

Hospital Name	Type of Facility	Annual Minimum Rent	End of Lease Term	Renewal Term (years)
McAllen Medical Center	Acute Care	\$ 5,485,000	December, 2011	20(a)
Wellington Regional Medical Center	Acute Care	\$ 3,030,000	December, 2011	20(b)
Southwest Healthcare System, Inland Valley Campus	Acute Care	\$ 2,648,000	December, 2011	20(b)
The Bridgeway	Behavioral Health	\$ 930,000	December, 2014	10(c)

- (a) We have four 5-year renewal options at existing lease rates (through 2031).  
 (b) We have two 5-year renewal options at existing lease rates (through 2021) and two 5-year renewal options at fair market value lease rates (2022 through 2031).  
 (c) We have two 5-year renewal options at fair market value lease rates (2015 through 2024).

**Other Related Party Transactions:**

A member of our Board of Directors and member of the Executive Committee is Of Counsel to the law firm used by us as our principal outside counsel. This Board member is also the trustee of certain trusts for the benefit of our CEO and his family. This law firm also provides personal legal services to our CEO.

**(3) Other Noncurrent liabilities and Third-party Minority Interests**

Other noncurrent liabilities include the long-term portion of our professional and general liability, workers' compensation reserves, and pension liability.

As of March 31, 2009 and December 31, 2008, the third-party minority interests (included in equity) of \$241.0 million and \$226.7 million, respectively, consists primarily of: (i) third-party ownership interests of approximately 28% in five acute care facilities located in Las Vegas, Nevada; (ii) a 20% third-party ownership in an acute care facility located in Washington D.C. and; (iii) third-party ownership interests of approximately 11% in an acute care facility located in Laredo, Texas.

In connection with the five acute care facilities located in Las Vegas, Nevada, the outside owners have certain put rights that may require the respective limited liabilities companies (LLCs) to purchase the minority member's interests upon the occurrence of: (i) certain specified financial conditions falling below established thresholds; (ii) breach of the management contract by the managing member (a subsidiary of ours), or; (iii) if the minority member's ownership percentage is reduced to less than certain thresholds.

**(4) Long-term debt**

We have an \$800 million, unsecured non-amortizing revolving credit agreement, as amended (Credit Agreement) which is scheduled to expire in July, 2011. The Credit Agreement includes a \$100 million sub-limit for letters of credit. The interest rate on the borrowings is determined, at our option, as either: (i) the one, two, three or six month London Inter-Bank Offer Rate (LIBOR) plus a spread of 0.33% to 0.575%; (ii) at the higher of the Agent's prime rate or the federal funds rate plus 0.50%, or; (iii) a competitive bid rate. A facility fee ranging from 0.07% to 0.175% is required on the total commitment. The applicable margins over LIBOR and the facility fee are based upon our credit ratings from Standard & Poor's Ratings Services and Moody's Investors Service, Inc. At March 31, 2009, the applicable margin over the LIBOR rate was 0.50% and the facility fee was 0.125%. There are no compensating balance requirements. As of March 31, 2009, we had \$222 million of borrowings outstanding under our revolving credit agreement and \$511 million of available borrowing capacity, net of \$67 million of outstanding letters of credit.

In August, 2007, we entered into a \$200 million accounts receivable securitization program (Securitization) with a group of conduit lenders and liquidity banks. The patient-related accounts receivable (Receivables) for substantially all of our acute care hospitals

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serve as collateral for the outstanding borrowings. The interest rate on the borrowings is based on the commercial paper rate plus a spread of .35%. The initial term of this Securitization was 364 days and the term can be extended for incremental 364 day periods upon mutual agreement of the parties. The facility was extended for a second 364-day term in August, 2008. The Securitization has a term-out feature that can be exercised by us if the banks do not extend the Securitization which would extend the maturity date to August, 2010. Under the terms of the term-out provision, the borrowing rate would be the same as our Credit Agreement rate. Outstanding borrowings which can be refinanced through available borrowings under the terms of our Credit Agreement are classified as long-term on our balance sheet. We have accounted for this Securitization as borrowings under SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. We maintain effective control over the Receivables since, pursuant to the terms of the Securitization, the Receivables are sold from certain of our subsidiaries to special purpose entities that are wholly-owned by us. The wholly-owned special purpose entities use the Receivables to collateralize the loans obtained from the group of third-party conduit lenders and liquidity banks. The group of third-party conduit lenders and liquidity banks do not have recourse to us beyond the assets of the wholly-owned special purpose entities that securitize the loans. As of March 31, 2009, we had \$100 million of borrowings outstanding pursuant to this program and \$100 million of available borrowing capacity.

In June, 2006, we issued \$250 million of senior notes (the Notes) which have a 7.125% coupon rate and mature on June 30, 2016. Interest on the Notes is payable semiannually in arrears on June 30 and December 30 of each year. In June, 2008, we issued an additional \$150 million of Notes which formed a single series with the original Notes issued in June, 2006. Other than their date of issuance and initial price to the public, the terms of the Notes issued in June, 2008 are identical to, and trade interchangeably with, the Notes which were originally issued in June, 2006.

During 2001, we issued \$200 million of senior notes which have a 6.75% coupon rate and which mature on November 15, 2011. The interest on the senior notes is paid semiannually in arrears on May 15 and November 15 of each year. The senior notes can be redeemed in whole at any time and in part from time to time.

Effective January 1, 2009, we adopted Statement of Financial Accounting Standards No. 161 (SFAS 161), Disclosures about Derivative Instruments and Hedging Activities: an amendment of FASB Statement No. 133. SFAS 161 requires additional disclosure about a company's derivative activities, but does not require any new accounting related to derivative activities. We have applied the requirements of SFAS 161 on a prospective basis. Accordingly, disclosures related to interim periods prior to the date of adoption have not been presented. During the fourth quarter of 2007, we entered into two interest rate swaps whereby we pay a fixed rate on a total notional principal amount of \$150 million and receive 3-month LIBOR. Each of the two interest rate swaps has a notional principal amount of \$75 million. The fixed rate payable on the first interest rate swap is 4.7625% and matures on October 5, 2012. The fixed rate payable on the second interest rate swap is 4.865% and the maturity date is October 17, 2011. The notional amount of the second interest rate swap reduces to \$50 million on October 18, 2010.

**(5) Commitments and Contingencies*****Professional and General Liability Claims and Property Insurance***

Effective January 1, 2008, most of our subsidiaries became self-insured for malpractice exposure up to \$10 million per occurrence, as compared to \$20 million per occurrence in the prior year. We purchased several excess policies through commercial insurance carriers which provide for coverage in excess of \$10 million up to \$195 million per occurrence and in the aggregate. However, we are liable for 10% of the claims paid pursuant to the commercially insured coverage in excess of \$10 million up to \$60 million per occurrence and in the aggregate.

Our estimated liability for self-insured professional and general liability claims is based on a number of factors including, among other things, the number of asserted claims and reported incidents, estimates of losses for these claims based on recent and historical settlement amounts, estimate of incurred but not reported claims based on historical experience, and estimates of amounts recoverable under our commercial insurance policies. While we continuously monitor these factors, our ultimate liability for professional and

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general liability claims could change materially from our current estimates due to inherent uncertainties involved in making this estimate. Given our significant self-insured exposure for professional and general liability claims, there can be no assurance that a sharp increase in claims asserted against us will not have a material adverse effect on our future results of operations.

As of March 31, 2009, the total accrual for our professional and general liability claims was \$275 million (\$274 million net of expected recoveries from state guaranty funds), of which \$42 million is included in other current liabilities. As of December 31, 2008, the total accrual for our professional and general liability claims was \$272 million (\$271 million net of expected recoveries