SHRINERS HOSPITALS FOR CHILDREN

Combined Financial Statements

December 31, 2008 and 2007

(With Independent Auditors' Report Thereon)

SHRINERS HOSPITALS FOR CHILDREN

Table of Contents

KPMG

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, 2008 and 2007, 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, 2008 and 2007, 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 notes 1(o) and 10 to the combined financial statements, the Shriners Hospitals for Children adopted the recognition and disclosure provisions of Statement of Financial Accounting Standards No. 157, *Fair Value Measurements*, and Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, as of December 31, 2008.

KPMG LLP

April 27, 2009
Certified Public Accountants

SHRINERS HOSPITALS FOR CHILDREN

Combined Statements of Financial Position

December 31, 2008 and 2007

(In thousands)

Assets		**2008**	**2007**
Cash and cash equivalents	$	4,979	13,664
Cash and cash equivalents held as collateral under securities lending transactions		848,406	1,348,842
Receivables		5,059	3,381
Accrued interest and dividends		31,563	39,547
Patient transportation funds held by Shrine temples		44,493	43,971
Inventories and deferred charges		36,472	19,796
Long-term investments:			
Marketable securities		5,700,516	8,291,222
Charitable gift annuities		22,614	20,855
Beneficial interest in trusts		417,942	510,375
Real estate and mineral interests		53,984	53,725
Miscellaneous investments		13,539	18,639
Estates in process		203,913	237,743
Land, buildings, and equipment, net of accumulated depreciation		710,995	689,466
Total assets	$	8,094,475	11,291,226
Liabilities and Net Assets			
Liabilities:			
Accounts payable and accrued expenses	$	89,940	84,144
Pension benefits		165,858	100,600
Liabilities under securities lending transactions		848,406	1,348,842
Other liabilities		36,493	41,494
Total liabilities		1,140,697	1,575,080
Net assets (net of cumulative foreign currency translation adjustment of $8,610 in 2008 and $6,928 in 2007):			
Unrestricted:			
Operations		5,065,698	7,734,997
Land, buildings, and equipment		710,995	689,466
Total unrestricted		5,776,693	8,424,463
Temporarily restricted		278,887	295,542
Permanently restricted		898,198	996,141
Total net assets		6,953,778	9,716,146
Total liabilities and net assets	$	8,094,475	11,291,226

See accompanying notes to combined financial statements.

SHRINERS HOSPITALS FOR CHILDREN

Combined Statements of Operations

Years ended December 31, 2008 and 2007

(In thousands)

		2008	2007
Operating revenues and other support:			
Investment income:			
Interest	$	123,331	147,282
Dividends		117,121	106,902
Other investment income		34,115	28,189
Investment management fees		(20,150)	(19,512)
Bequests released from restrictions used for operations		216,445	213,241
Donations		35,195	41,397
Fund raising and special events		34,078	25,570
Hospital assessments		1,633	1,726
Reimbursements from Canadian Provinces		5,958	6,362
Other		2,392	3,017
Total revenues and other support		550,118	554,174
Operating expenses:			
Hospitals		611,430	579,494
Research		33,240	33,158
Headquarters, administrative, and board related		52,854	41,485
Fund raising and special events		24,948	12,151
Total operating expenses		722,472	666,288
Decrease in net assets from operating activities		(172,354)	(112,114)
Nonoperating (losses) gains:			
(Loss) gain on investments:			
Net realized (losses) gains from investments		(488,392)	392,805
Net unrealized losses on investments		(1,914,761)	(83,316)
Total (loss) gain on investments		(2,403,153)	309,489
Life memberships		148	109
Change in patient transportation funds held by Shrine temples		522	3,303
Pension related changes other than net periodic pension costs		(65,561)	22,058
Other, net		(5,690)	(5,830)
Foreign currency translation adjustments		(1,682)	1,779
Total nonoperating (losses) gains		(2,475,416)	330,908
(Decrease) increase in unrestricted net assets	$	(2,647,770)	218,794

See accompanying notes to combined financial statements.

SHRINERS HOSPITALS FOR CHILDREN

Combined Statements of Changes in Net Assets

Years ended December 31, 2008 and 2007

(In thousands)

		2008	2007
Unrestricted net assets:			
Decrease in net assets from operating activities	$	(172,354)	(112,114)
Nonoperating (losses) gains:			
(Loss) gain on investments:			
Net realized (losses) gains from investments		(488,392)	392,805
Net unrealized losses on investments		(1,914,761)	(83,316)
Total (loss) gain on investments		(2,403,153)	309,489
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Other, net		(5,690)	(5,830)
Foreign currency translation adjustments		(1,682)	1,779
Total nonoperating (losses) gains		(2,475,416)	330,908
(Decrease) increase in unrestricted net assets		(2,647,770)	218,794
Temporarily restricted net assets:			
Bequests		188,027	143,287
Donations		5,577	1,372
Other, net		(1,340)	(1,108)
Net unrealized gains from investments		7,526	9,675
Net assets released from restrictions used for operations		(216,445)	(213,241)
Decrease in temporarily restricted net assets		(16,655)	(60,015)
Permanently restricted net assets:			
Bequests		2,824	7,968
Donations		5,370	5,218
Other, net		23	(63)
Net unrealized (losses) gains from investments		(106,160)	8,558
(Decrease) increase in permanently restricted net assets		(97,943)	21,681
(Decrease) increase in net assets		(2,762,368)	180,460
Net assets, beginning of year		9,716,146	9,535,686
Net assets, end of year	$	6,953,778	9,716,146

See accompanying notes to combined financial statements.

SHRINERS HOSPITALS FOR CHILDREN

Combined Statements of Cash Flows

Years ended December 31, 2008 and 2007

(In thousands)

		2008	2007
Cash flows from operating activities:			
Change in net assets	$	(2,762,368)	180,460
Adjustments to reconcile change in net assets to net cash used in operating activities:			
Depreciation		45,529	47,196
(Gain) loss on disposal of property and equipment		(403)	5,387
Realized and unrealized losses (gains) on investments		2,501,787	(327,722)
Gifts and bequests designated by the board or restricted by donor for long-term investment		(190,999)	(151,364)
Pension related changes other than net period pension costs		65,561	(22,058)
Changes in operating assets and liabilities:			
Receivables		8,069	519
Accrued interest and dividends		(1,763)	(950)
Patient transportation funds held by Shrine temples		(522)	(3,303)
Inventories and deferred charges		(16,676)	(6,630)
Beneficial interest in trusts		92,433	(29,071)
Estates in process		33,830	73,934
Accounts payable and accrued expenses		5,796	9,620
Pension benefits		(303)	10,705
Net cash used in operating activities		(220,029)	(213,277)
Cash flows from investing activities:			
Additions to property and equipment		(66,655)	(41,055)
Proceeds from sale of investments		11,557,682	7,161,329
Investment purchases		(11,465,681)	(7,070,801)
Net cash provided by investing activities		25,346	49,473
Cash flows from financing activities:			
Gifts and bequests designated for board endowment		188,027	143,287
Gifts and bequests permanently restricted by donors		2,824	7,968
Life memberships		148	109
Change in other liabilities		(5,001)	1,598
Net cash provided by financing activities		185,998	152,962
Net decrease in cash and cash equivalents		(8,685)	(10,842)
Cash and cash equivalents at beginning of year		13,664	24,506
Cash and cash equivalents at end of year	$	4,979	13,664

See accompanying notes to combined financial statements.

(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 new 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".

(b) Use of Estimates

The preparation of the combined financial statements 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. 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 activities 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, 2008 and 2007 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.

(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.

(Continued)

(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

Statement of Financial Accounting Standards (SFAS) No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, 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, 2008 and 2007, the Hospitals held $848,406 and $1,348,842, 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 $828,958 and $1,308,870 at December 31, 2008 and 2007, 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. 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.

Investments in real estate and mineral interests and miscellaneous investments are carried at fair value at the date of contribution. Investment income 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 assets and are classified as permanently restricted net assets. All other charitable lead 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 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 $25,338 and $31,279 and deferred income of $11,155 and $10,093 at December 31, 2008 and 2007, 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 SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. This statement 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. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

(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) New Accounting Pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 (SFAS No. 157), *Fair Value Measurements,* which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. SFAS No. 157 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements. The Hospitals adopted SFAS No. 157, *Fair Value Measurements*, on January 1, 2008. The adoption of SFAS No. 157 did not have a material impact on the Hospitals financial statements (see note 10).

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 (SFAS No. 159), *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS No. 159 permits companies to measure certain financial assets and financial liabilities at fair value, at specified election dates. The election may be applied to financial assets and liabilities on an instrument by instrument basis, is irrevocable, and may only be applied to entire instruments. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Hospitals adopted SFAS No. 159 on January 1, 2008. Since the Hospitals did not utilize the fair value option for any allowable items not already reported at fair value, the adoption of SFAS No. 159 did not have a material impact on the Hospitals' financial statements.

(p) Reclassifications

Certain amounts from the 2007 financial statements have been reclassified to conform with the 2008 financial statement presentation.

(In thousands)

(2) Long-Term Investments

Marketable securities at December 31, 2008 and 2007 consist of:

	2008		2007	
	Cost	**Fair value**	**Cost**	**Fair value**
Short-term investments	$ 329,113	329,113	224,323	224,323
U.S. Government securities	1,406,937	1,496,164	1,583,875	1,465,964
Corporate bonds	591,201	510,376	856,277	852,904
International stocks	963,032	780,501	1,128,532	1,459,571
Common and preferred stocks	3,269,287	2,584,362	3,426,913	4,288,460
	$ 6,559,570	5,700,516	7,219,920	8,291,222

Investment income and total return on all long-term investments was comprised of the following components for the years ended December 31, 2008 and 2007:

	2008	2007
Interest	$ 123,331	147,282
Dividends	117,121	106,902
Trust income	19,961	19,011
Rents and royalties	13,330	8,780
Other income	824	398
Less investment management fees	(20,150)	(19,512)
Total income from marketable securities	254,417	262,861
Net realized (losses) gains from marketable securities	(488,392)	392,805
Net unrealized losses from marketable securities	(2,013,395)	(65,083)
Total return on marketable securities	(2,247,370)	590,583

(In thousands)

(3) Land, Buildings, and Equipment

Land, buildings, and equipment at December 31, 2008 and 2007 consist of:

		2008	2007	Estimated useful lives
Land	$	25,573	23,941	—
Land improvements		11,384	11,659	5 – 20 years
Buildings		821,775	821,844	40 – 50 years
Equipment		334,875	328,378	4 – 25 years
		1,193,607	1,185,822	
Less accumulated depreciation		(546,216)	(513,275)	
		647,391	672,547	
Construction in progress		63,604	16,919	
Land, buildings, and equipment, net	$	710,995	689,466	

(4) Construction and other major capital projects

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

Project		Total appropriation	Unexpended at December 31, 2008
Honolulu	$	78,000	45,501
St. Louis		172,000	166,400
Portland		77,037	69,711
Philadelphia		14,172	11,933
Other		20,244	8,897
Approved equipment expenditures:			
PACS imaging		22,417	11,159
Information systems projects		15,874	6,038
Other equipment		8,207	8,207
	$	407,951	327,846

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

The Shriners Hospitals for Children 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 Shriners Hospitals for Children. 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, 2008 and 2007, amounts of $1,431 and $122, 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.

(In thousands)

Fund raising and special events revenues and costs for the years ended December 31, 2008 and 2007 consist of the following:

		2008	2007
Revenues from Shrine temple sponsored events	$	9,941	10,990
Direct mail revenue		16,659	12,140
Other revenue		7,478	2,440
	$	34,078	25,570
Fund raising costs paid directly by Shrine temples in connection with fund raising events	$	1,325	1,448
Donor relations expense		5,048	3,209
Direct mail expense		8,873	4,920
Other costs		9,702	2,574
	$	24,948	12,151

Revenues from Shrine temple sponsored events are reported net of direct costs of $3,568 and $4,176 for 2008 and 2007, 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 2008 event yielded approximately $6,499 in revenues. Expenses incurred on this event 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 change in patient transportation funds held by Shrine temples in the accompanying combined statements of operations.

The activities of the patient transportation funds reflected for the years ended December 31, 2008 and 2007 are as follows:

		2008	2007
Temple revenues restricted for patient transportation	$	20,919	17,430
Patient transportation costs		(20,397)	(14,127)
Net change	$	522	3,303

(In thousands)

(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 Shriner's Hospital Pension Plans and the Postretirement Plan for the years ended December 31, 2008 and 2007 included the following components:

	Pension Plans		Postretirement Plan	
	2008	**2007**	**2008**	**2007**
Service cost – benefits earned during the period	$ 15,825	15,045	315	334
Interest cost on projected benefit obligation	18,444	16,757	509	494
Expected return on plan assets	(15,511)	(13,956)	—	—
Net amortized and deferral of unrecognized gains and losses	2,033	2,844	335	335
Net periodic pension cost	$ 20,791	20,690	1,159	1,163

(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, 2008 and 2007, respectively (using a measurement date of December 31 for December 31, 2008 amounts and September 30 for December 31, 2007 amounts):

		Pension Plans		Postretirement Plan	
		2008	**2007**	**2008**	**2007**
Change in benefit obligation:					
Benefit obligation at beginning of year	$	294,164	281,278	8,114	8,360
Effect of early measurement		6,017	—	146	—
Service cost		15,825	15,045	315	334
Interest cost		18,444	16,757	509	494
Actuarial (gain) loss		(5,433)	(6,450)	(305)	(904)
Benefits paid		(10,169)	(12,466)	(220)	(170)
Settlements		—	—	—	—
Benefit obligation at end of year		318,848	294,164	8,559	8,114
Change in plan assets:					
Fair value of plan assets at beginning of year		201,678	177,685	—	—
Effect of early measurement		1,713	—	—	—
Actual return on plan assets		(57,743)	25,482	—	—
Employer contributions		26,070	10,977	220	170
Benefits paid		(10,169)	(12,466)	(220)	(170)
Fair value of plan assets at end of year		161,549	201,678	—	—
Funded status at the end of year	$	(157,299)	(92,486)	(8,559)	(8,114)

The accumulated benefit obligation for the Pension Plans was $257,708 and $237,735 at December 31, 2008 and 2007, 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, 2008 and 2007 were as follows:

	Pension Plans		Postretirement Plan	
	2008	**2007**	**2008**	**2007**
Discount rate	6.00%	6.00%	6.00%	6.00%
Rate of compensation increase	4.00	4.00	N/A	N/A

(In thousands)

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

	Pension Plans		Postretirement Plan	
	2008	2007	2008	2007
Discount rate	6.00%	5.75%	6.00%	6.00%
Expected long-term rate of return on plan assets	7.75	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, 2008. 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.

	Pension Plans		Postretirement Plan	
	Amounts recognized in unrestricted net assets at December 31, 2008	Amounts in unrestricted net assets to be recognized during the next fiscal year	Amounts recognized in unrestricted net assets at December 31, 2008	Amounts in unrestricted net assets to be recognized during the next fiscal year
Actuarial loss (gain)	$ 2,001	2,428	—	(14)
Prior service cost	32	32	300	300
Transition obligation	—	—	35	35
Total	$ 2,033	2,460	335	321

(In thousands)

Plan Assets

The weighted average allocation of the Pension Plans' assets at December 31, 2008 and 2007 were as follows:

Asset category	2008	2007
Common stocks	23%	53%
U.S. government and agency issues	—	25
Corporate and miscellaneous bonds	36	13
Mutual funds	32	6
Short-term investments	9	3
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.

Contributions

Annual contributions are determined based upon calculations prepared by the plans' actuary. Expected contributions to the Pension Plans and the Postretirement Plan are $19,134 and $270, respectively, in 2009.

Benefit Payments

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

	Pension plans	Postretirement plan
Fiscal year:		
2009	$ 10,327	270
2010	11,892	292
2011	13,108	316
2012	14,447	341
2013	16,725	368
2014-2018	111,382	2,334

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 $5,082 and $6,407 in 2008 and 2007, 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, 2008. 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.

(10) Fair Value Measurements

SFAS No. 157 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. SFAS No. 157 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.

(In thousands)

The table below summarizes the fair values of Hospitals' significant financial assets and liabilities as of December 31, 2008:

		Fair value measurements at reporting date using		
	December 31, 2008	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	$ 5,700,516	2,385,664	3,290,834	24,018
Collateral under securities lending transactions	848,406	848,406	—	—
Liabilities:				
Liabilities under securities lending transactions	$ 848,406	848,406	—	—

The Hospitals' Level 1 assets and liabilities include investments in 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, and asset-backed securities with fair values modeled by external pricing vendors.

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

The table below summarizes the changes in Level 3 assets for the year ended December 31, 2008:

	Fair value measurements using significant unobservable inputs (Level 3)			
	Fixed income investments	Equity investments	Other investments	Total
Beginning balance	$ 6,581	10,070	35,792	52,443
Total gains (losses) (realized/unrealized) included in (decrease) increase in unrestricted net assets	(4,610)	(7,975)	(12,711)	(25,296)
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	7,872	24,018

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

Total gains (losses) included in (decrease) increase in unrestricted net assets	$	(16,554)
Change in unrealized gains (losses) relating to assets still held at reporting date	$	(8,742)

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.