



Report of Independent Auditors
and Financial Statements for

**Public Hospital District No. 4,
King County, Washington**

December 31, 2012 and 2011

MOSS ADAMS LLP

Certified Public Accountants | Business Consultants

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CONTENTS

	PAGE
REPORT OF INDEPENDENT AUDITORS	1-2
MANAGEMENT'S DISCUSSION AND ANALYSIS	3-7
FINANCIAL STATEMENTS	
Statements of net position	8
Statements of revenues, expenses, and changes in net position	9
Statements of cash flows	10-11
Notes to financial statements	12-23

REPORT OF INDEPENDENT AUDITORS

To the Board of Commissioners
Public Hospital District No. 4,
King County, Washington

Report on Financial Statements

We have audited the accompanying financial statements of Public Hospital District No. 4, King County, Washington (the District), which comprise the statements of net position as of December 31, 2012 and 2011, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Public Hospital District No. 4, King County, Washington, as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in the appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

A handwritten signature in cursive script that reads "Moss Adams LLP".

Everett, Washington
July 15, 2013

**PUBLIC HOSPITAL DISTRICT NO. 4,
KING COUNTY, WASHINGTON
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Introduction

Our discussion and analysis provides an overview of the financial position and activities of Public Hospital District No. 4, King County, Washington, doing business as Snoqualmie Valley Hospital and Hospital District No. 4 Clinics (the District). It should be read in conjunction with the financial statements and accompanying notes that follow.

Change in Net Position for 2012

The District had a change in net position of \$9,668,500 for 2012. The majority of the change (\$9,264,764) is due to the settlement of the note with the Snoqualmie Tribe that is discussed below. Excluding the settlement of the note with the Snoqualmie Tribe, the District had an increase in net position of \$403,376. The District has shown a profit (excluding the gain on sale of the hospital campus) in three out of the last four years.

The District implemented a number of programs in 2012 that will support our long-term profitability in the future. Some of these programs are:

- The District restructured its marketing for sub-acute rehabilitation (swing beds) in 2012; this led to an increase of 4.2% in inpatient days. We expect this growth to increase when we move into the new hospital facility, as we will have 25 single occupancy patient rooms, versus 14 inpatient rooms in our current facility.
- In early 2012, the District made changes to its expense base to bring it in line with revenues. The District decreased its operating expense base by \$1.6 million annually.

Note From the Snoqualmie Tribe

In July 2008, the District sold the existing hospital and campus for \$30,000,000. The sale was financed by the District, which held a note from the purchaser for that amount. In June 2012, the District negotiated an early payout with the Snoqualmie Tribe. The District received cash and free rent on the current hospital valued at \$19.9 million in the settlement. The terms of the settlement allow the District to use the current hospital facility rent-free until its replacement facility is completed.

\$7.6 million of these proceeds were used to pay off a note payable to MHC LTRA, Inc. for the purchase of property. The District improved its cash position by \$5.6 million in 2012 with the settlement of the note with the Snoqualmie Tribe and a positive cash flow from operations. The discounted payment was in line with current appraisals of the value of the hospital property.

**PUBLIC HOSPITAL DISTRICT NO. 4,
KING COUNTY, WASHINGTON
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

Operational Highlights

The District currently plans to begin construction of a new facility on a 13-acre site near the intersection of State Highway 18 and Interstate 90 in the fall of 2013. The facility is planned as a 70,000-square-foot replacement for the District's existing 25,000-square-foot hospital facility. The new facility will include 25 inpatient beds (versus 14 rooms in our current facility), a six-room emergency department, and rehabilitation, radiology, and pharmacy services.

In 2011, the District requested quotes from developers to build and finance the new hospital. The District entered into negotiations with developers to build the new hospital in 2011. The District also continued predevelopment work on the new hospital and completed the clearing and grading of the site for the new hospital in 2012.

The District is currently in the process of finalizing the agreement with the developer of the new hospital to build the new hospital. Under the terms of the agreement, the District will enter into a capital lease with the developer to lease the hospital for 30 years and purchase the hospital for \$1.00 at the end of the lease term. The District also has the option to purchase the hospital after substantial completion by the developer.

The new hospital will allow the District to expand its health care services to the community. We are currently constrained by the size of our existing hospital and its location. The advantages of the new facility are:

- The new facility will have 25 inpatient rooms, versus our current facility, which has 14 inpatient rooms. The current facility limits the number of inpatients we can accommodate to 20 or fewer. We frequently hit our maximum inpatient capacity and have to turn away inpatients.
- The new facility will enjoy easier access from I-90, the major east-west freeway in the Snoqualmie area. The current facility is difficult to access for residents driving west on the freeway.
- The new, modern facility will drive an increase in emergency room and outpatient visits. Experience has shown that critical access hospitals that open new facilities experience a 30%+ increase in patient volumes. Our current facility was built in 1984 and although well maintained, does not allow for state-of-the-art health care operations.

Overall we expect the new hospital to increase service to our community and further improve our financial performance. The improvement in financial performance has been validated by a number of independent financial analyses we have had performed while going through the due diligence process for the financing of the new hospital.

Medical Services Utilization

Inpatient days continued to grow in 2012, increasing by 4.2% over 2011 levels. This is the fourth consecutive year inpatient days have increased. Clinic visits decreased by 11.5% in 2012 due to a decrease in providers in the clinic system. The District will add a clinic provider in 2013, which will increase clinic volumes in the future.

**PUBLIC HOSPITAL DISTRICT NO. 4,
KING COUNTY, WASHINGTON
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

Change in Liabilities

The District decreased its long-term liabilities in 2012 by \$14.7 million due to the repayment of the note to MHC LTRA and recognition of the deferred loss.

Statement of Revenues, Expenses, and Changes in Net Position

The following is a presentation of certain condensed financial information derived from the District's statement of revenues, expenses, and changes in net position:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Net operating revenue	\$ 22,522,248	\$ 21,485,049	\$ 21,423,400
Nonoperating income	<u>2,763,912</u>	<u>3,149,885</u>	<u>3,275,060</u>
	<u>25,286,160</u>	<u>24,634,934</u>	<u>24,698,460</u>
Total operating expenses	22,675,946	24,256,446	23,124,432
Nonoperating expenses	<u>2,206,478</u>	<u>2,907,200</u>	<u>1,795,449</u>
	<u>24,882,424</u>	<u>27,163,646</u>	<u>24,919,881</u>
Change in net position before gain on sale of hospital campus	403,736	(2,528,712)	(221,421)
Gain on sale of hospital campus	<u>9,264,764</u>	<u>615,000</u>	<u>373,000</u>
Change in net position	9,668,500	(1,913,712)	151,579
Net position, beginning of year	<u>(17,341,225)</u>	<u>(15,427,513)</u>	<u>(15,579,092)</u>
Net position, end of year	<u>\$ (7,672,725)</u>	<u>\$ (17,341,225)</u>	<u>\$ (15,427,513)</u>

Operating Revenue

District revenues included \$22.5 million in operating revenue adjusted for contractual allowances, bad debts, and charity care. Net operating revenue increased by \$1.0 million (+4.8%) due to an increase in inpatient volumes and rate increases implemented in 2012.

Total uncompensated care (bad debt plus charity care) for 2012 was \$1,552,148, which was consistent with the 2011 total of \$1,592,185. The District has an active charity care program that provides discounts to District residents based on income levels.

**PUBLIC HOSPITAL DISTRICT NO. 4,
KING COUNTY, WASHINGTON
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

Operating Expenses

Operating expense decreased by \$1.6 million (6.5%); this decrease was the result of expense reductions implemented by the District in 2012. Wages, employee benefits were 71.9% of total operating expenses in 2012. There was a 3.8% decrease in salary and benefit costs and a 12.8% decrease in non-salary related operating costs due to the expense reductions implemented in 2012.

The District supported an increase in inpatient volumes of 4.2% while decreasing operating expenses 6.5%.

Other Changes in Net Position

Change in net position includes \$9.3 million income (gain on sale of hospital campus) for the settlement of the note with the Snoqualmie Tribe. Excluding this income, the District had net income of \$403,736.

Statement of Net Position

The following is a presentation of certain condensed financial information derived from the District's statement of net position:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
ASSETS			
Current assets	\$ 11,261,246	\$ 19,074,172	\$ 4,900,336
Capital assets, net	23,961,055	20,704,018	18,469,497
Other noncurrent assets	<u>2,926,821</u>	<u>3,426,889</u>	<u>31,095,198</u>
Total assets	<u>\$ 38,149,122</u>	<u>\$ 43,205,079</u>	<u>\$ 54,465,031</u>
LIABILITIES			
Current liabilities	\$ 5,630,202	\$ 20,514,031	\$ 6,581,844
Noncurrent liabilities	<u>40,191,645</u>	<u>40,032,273</u>	<u>63,310,700</u>
Total liabilities	<u>45,821,847</u>	<u>60,546,304</u>	<u>69,892,544</u>
NET POSITION			
Net investment in capital assets	(1,950,347)	(10,926,151)	(8,581,907)
Restricted expendable for debt service	399,925	438,198	550,174
Unrestricted	<u>(6,122,303)</u>	<u>(6,853,272)</u>	<u>(7,395,780)</u>
Total net position	<u>(7,672,725)</u>	<u>(17,341,225)</u>	<u>(15,427,513)</u>
Total liabilities and net position	<u>\$ 38,149,122</u>	<u>\$ 43,205,079</u>	<u>\$ 54,465,031</u>

**PUBLIC HOSPITAL DISTRICT NO. 4,
KING COUNTY, WASHINGTON
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

Statement of Net Position (continued)

Assets

The District's cash balances increased by \$5.6 million in 2012 as shown on the statement of cash flows for the District. The District had a positive cash flow from operations and excess (in excess of debt service) tax levies of \$219,364. The remainder of the increase in cash is the net result of the settlement of the note with the Snoqualmie Tribe and payoff of long-term debt, which is discussed above.

The decrease in total assets is the result of the use of the proceeds from the settlement with the Snoqualmie Tribe to pay down long-term debt.

Liabilities and Net Position

Liabilities decreased by \$14.7 million due to the removal of the deferred gain that resulted from the collection of the note from the Snoqualmie Tribe in June 2012, the payoff of long-term debt (MHC LTRA and MVP, LLC), and a decrease in accounts payable.

Net position increased due to the District's profit in 2012. Total profit for the year was \$9,668,500; \$9,264,764 was due to a gain on sale of the hospital campus due to the settlement of the note with the Snoqualmie Tribe. The District had a net profit of \$403,736, excluding the proceeds from the settlement of the note with the Snoqualmie Tribe.

Deferred Gain

A deferred gain was recorded on the installment sale of the hospital campus in 2008. With the renegotiation of the note from the Snoqualmie Tribe, the deferred gain was decreased to zero.

Statement of Cash Flows

The District increased its cash by \$5.6 million from the 2011 levels. The majority of the increase was due to the payoff of the note from the Snoqualmie Tribe, net of the payoff of long-term debt, which accounted for \$5.2 million of the increase. The District also had positive cash flow from operating activities and its tax levies.

The increase in cash was used to increase the District's operating cash reserves and to complete clearing and grading and utility work on the new hospital site.

Contacting the District's Financial Management

This financial report is designed to provide the District's patients, suppliers, taxpayers, and creditors with a general overview of the District's finances and show its accountability for the money it receives. If you have questions about this report or need additional information, contact the District's finance office at Snoqualmie Valley Hospital, 9575 Ethan Wade Way SE, Snoqualmie, WA 98065-9577.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
STATEMENTS OF NET POSITION

ASSETS

	December 31,	
	2012	2011
CURRENT ASSETS		
Cash and cash equivalents	\$ 6,222,798	\$ 187,139
Assets limited as to use required for current liabilities	241,910	236,410
Patient accounts receivable, net of allowances for doubtful accounts of \$349,000 in 2012 and \$278,000 in 2011	4,660,966	3,419,593
Other receivables	135,572	278,239
Estimated third-party payor settlements	-	278,587
Note receivable	-	14,600,000
Prepaid expenses and other assets	-	74,204
Total current assets	<u>11,261,246</u>	<u>19,074,172</u>
ASSETS LIMITED AS TO USE, net of current portion	<u>2,034,235</u>	<u>2,491,819</u>
CAPITAL ASSETS		
Land	13,374,157	11,763,838
Construction in progress	8,457,330	8,019,723
Depreciable capital assets, net of accumulated depreciation and amortization	<u>2,129,568</u>	<u>920,457</u>
Total capital assets, net of accumulated depreciation and amortization	<u>23,961,055</u>	<u>20,704,018</u>
DEFERRED FINANCING COSTS	<u>892,586</u>	<u>935,070</u>
	<u>\$ 38,149,122</u>	<u>\$ 43,205,079</u>
LIABILITIES AND NET POSITION		
CURRENT LIABILITIES		
Accounts payable	\$ 1,272,034	\$ 1,832,352
Accrued compensation and related liabilities	1,255,074	1,262,006
Accrued interest payable	241,910	236,410
Estimated third-party payor settlements	1,438,256	-
Line of credit	1,390,000	1,286,267
Deferred gain	-	9,264,764
Current maturities of long-term debt	<u>32,928</u>	<u>6,632,232</u>
Total current liabilities	5,630,202	20,514,031
LONG-TERM DEBT, net of current maturities	<u>40,191,645</u>	<u>40,032,273</u>
Total liabilities	<u>45,821,847</u>	<u>60,546,304</u>
NET POSITION		
Net investment in capital assets	(1,950,347)	(10,926,151)
Restricted expendable for debt service	399,925	438,198
Unrestricted	<u>(6,122,303)</u>	<u>(6,853,272)</u>
Total net position	<u>(7,672,725)</u>	<u>(17,341,225)</u>
	<u>\$ 38,149,122</u>	<u>\$ 43,205,079</u>

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

	Years Ended December 31,	
	2012	2011
OPERATING REVENUE		
Net patient service revenue (net of provision for bad debts of \$540,094 in 2012 and \$1,030,971 in 2011)	\$ 22,128,762	\$ 20,603,359
Taxation for operations	346,992	843,739
Other	46,494	37,951
Total operating revenue	<u>22,522,248</u>	<u>21,485,049</u>
OPERATING EXPENSES		
Salaries and wages	13,642,194	14,224,490
Employee benefits	2,662,185	2,721,840
Professional fees	710,411	1,260,763
Supplies	1,709,091	2,066,231
Repairs and maintenance	54,836	39,916
Utilities	405,207	376,592
Purchased services	1,203,147	1,256,500
Insurance	350,666	377,125
Leases and rentals	967,458	912,279
Depreciation and amortization	390,823	280,122
Other	579,928	740,588
Total operating expenses	<u>22,675,946</u>	<u>24,256,446</u>
OPERATING LOSS	<u>(153,698)</u>	<u>(2,771,397)</u>
NONOPERATING INCOME (EXPENSE)		
Investment income, net of accounts capitalized	22,436	20,517
Taxation for bond principal and interest	2,626,076	2,343,178
Interest expense, net of amount capitalized	(2,184,301)	(2,154,299)
Gain (loss) on disposal of capital assets	-	(1,092)
Grant income	8,387	786,190
Impairment of capital assets	-	(310,933)
Settlement on early termination of lease	(22,177)	(439,413)
Other, net	107,013	(1,463)
Nonoperating income, net	<u>557,434</u>	<u>242,685</u>
CHANGE IN NET POSITION BEFORE GAIN ON SALE OF HOSPITAL CAMPUS	403,736	(2,528,712)
GAIN ON SALE OF HOSPITAL CAMPUS	<u>9,264,764</u>	<u>615,000</u>
CHANGE IN NET POSITION	9,668,500	(1,913,712)
NET POSITION, beginning of year	<u>(17,341,225)</u>	<u>(15,427,513)</u>
NET POSITION, end of year	<u>\$ (7,672,725)</u>	<u>\$ (17,341,225)</u>

See accompanying notes.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
STATEMENTS OF CASH FLOWS

Increase (Decrease) in Cash and Cash Equivalents

	Years Ended December 31,	
	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from and on behalf of patients	\$ 22,604,232	\$ 18,988,790
Cash paid to suppliers	(16,311,311)	(16,748,542)
Cash paid to employees	(6,466,858)	(7,364,728)
Other cash receipts	46,309	51,593
Net cash from operating activities	(127,628)	(5,072,887)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Cash from tax levies considered a noncapital financing activity	346,992	843,739
Other	115,400	7,354
Net cash from noncapital financing activities	462,392	851,093
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of capital assets	(3,513,665)	(2,825,576)
Cash from tax levies for general obligation bonds	2,635,498	2,339,182
Change in line of credit	103,733	544,267
Payment received from note receivable	14,600,000	750,000
Grant proceeds for electronic health record	142,852	498,949
Proceeds from issuance of long-term debt	-	15,330,207
Cash paid for issuance of long-term debt	-	(447,857)
Principal payments on long-term debt	(6,659,363)	(9,227,043)
Interest paid on long-term debt, net of amount capitalized	(2,051,081)	(2,060,052)
Other, net	(22,177)	(94,336)
Net cash from capital and related financing activities	5,235,797	4,807,741
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment income, net of amount capitalized	22,436	20,517
NET CHANGE IN CASH AND CASH EQUIVALENTS	5,592,997	606,464
CASH AND CASH EQUIVALENTS, beginning of year	2,780,780	2,174,316
CASH AND CASH EQUIVALENTS, end of year	\$ 8,373,777	\$ 2,780,780
RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET ASSETS		
Cash and cash equivalents	\$ 6,222,798	\$ 187,139
Cash and cash equivalents in assets whose use is limited	2,150,979	2,593,641
	\$ 8,373,777	\$ 2,780,780

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
STATEMENTS OF CASH FLOWS

Increase (Decrease) in Cash and Cash Equivalents

	Years Ended December 31,	
	2012	2011
RECONCILIATION OF OPERATING LOSS TO		
NET CASH FROM OPERATING ACTIVITIES		
Operating loss	\$ (153,698)	\$ (2,771,397)
Adjustments to reconcile operating loss to net cash from operating activities		
Revenue from tax levies considered noncapital financing activity	(346,992)	(843,739)
Depreciation and amortization	390,823	280,122
Provision for bad debts	540,094	1,030,971
Change in assets and liabilities		
Patient accounts receivable	(1,781,467)	(896,639)
Other receivables	(185)	13,642
Prepaid expenses and other assets	74,204	(74,204)
Estimated third-party payor settlements	1,716,843	(1,748,901)
Accounts payable	(560,318)	(260,530)
Accrued compensation and related liabilities	(6,932)	197,788
	<u>\$ (127,628)</u>	<u>\$ (5,072,887)</u>
Net cash from operating activities		
SUPPLEMENTAL DISCLOSURE OF NONCASH ACTIVITIES		
Equipment financed with capital lease obligations	<u>\$ 134,195</u>	<u>\$ -</u>

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON

NOTES TO FINANCIAL STATEMENTS

Note 1 - Organization

Public Hospital District No. 4, King County, Washington, doing business as Snoqualmie Valley Hospital and as Hospital District No. 4 Clinics (the District), is organized as a municipal corporation under the laws of the state of Washington and operates a licensed 28-bed acute care hospital and primary and specialty care clinics in Eastern King County, Washington. As organized, the District is exempt from payment of federal income tax. The Board of Commissioners consists of five elected community members. The District is not considered to be a component unit of King County.

The District is working in preparation for a modernization of existing hospital facilities to improve outpatient access and expand services to improve patient care and reduce ongoing operating losses. During this process, the District recognized that the existing facility will not accommodate the growth anticipated for the communities the District serves. Possible relocation sites have been identified and pre-development work has been performed.

In July 2008, the District sold the existing hospital and campus for \$30,000,000. The sale was financed by the District, which held a note from the purchaser for that amount. The note originally matured on May 1, 2015. The purchaser began making payments of \$50,000 per month in May 2010, which increased to \$100,000 per month in October 2011 and was to continue until May 1, 2015, at which time the remaining balance on the sale was due in full. On June 20, 2012, the District and purchaser agreed to an amendment of the note. The amendment renegotiated the payment terms to be due no later than July 31, 2012, at the discounted balance of \$14,000,000. In accordance with the amendment, the District may continue to use the hospital and campus on a rent-free basis while it completes a replacement facility to be located at the intersection of Interstate 90 and State Highway 18.

Note 2 - Summary of Significant Accounting Policies

Use of estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. During the year ended December 31, 2011, the District recognized a decrease to net patient service revenue of \$545,167 related to changes in previous estimates.

Enterprise fund accounting - The District uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

Cash and cash equivalents - Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity date of three months or less, excluding amounts limited as to use by board designation, indenture agreements, or donors.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 2 - Summary of Significant Accounting Policies (continued)

Assets limited as to use - Periodically, the Board of Commissioners sets aside cash resources for the funding of future capital improvements. In addition, certain funds are restricted by bond indentures to be used solely for debt service or for the funding of future capital projects. These funds are invested in the King County Investment Pool, which is in accordance with state guidelines.

All District investments are carried at market value. Investment income is reported as nonoperating gains and losses.

Note receivable - The District received a \$30,000,000 noninterest-bearing note receivable in exchange for sale of the hospital buildings and land. Under the original terms, the note matured on May 1, 2015. The purchaser began making payments of \$50,000 per month in May 2010, which increased to \$100,000 in October 2011. The note was amended on June 20, 2012 (Note 1), which reduced the remaining payment at that date to \$14,000,000.

Capital assets - Land, buildings, and equipment acquisitions are recorded at cost. Improvements and replacements of land, buildings, and equipment are capitalized. The District's capitalization threshold is \$5,000 per item and a useful life of at least three years. Maintenance and repairs are expensed. The cost of land, buildings, and equipment sold or retired and the related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recorded.

Depreciation is recorded over the estimated useful life of each class of depreciable asset using the American Hospital Association guidelines and is computed using the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. The estimated useful lives used by the District are as follows:

Buildings	5 - 40 years
Equipment	5 - 15 years

Interest on borrowed funds less any interest earned on temporarily invested funds is capitalized on construction projects as a cost of the related project from the date of borrowing until the construction period ends and the related asset is placed in service. Capitalized interest is depreciated over the estimated useful life of the related asset.

Deferred gain - The gain on the sale of the hospital campus is recorded on the installment basis. Deferred gain was originally recorded in the amount of \$24,602,287, with the gain recorded as nonoperating revenue as payments are made on the note receivable. Deferred gain recognized as income during the years ended December 31, 2012 and 2011, was \$9,264,764 and \$615,000, respectively.

Insurance - The District pays certain medical, dental, prescription, and vision claims for its employees on a self-insured basis. The District has purchased stop-loss insurance to cover claims that exceed stated limits and has recorded estimated reserves for the ultimate costs for both reported claims and claims incurred but not reported.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON

NOTES TO FINANCIAL STATEMENTS

Note 2 - Summary of Significant Accounting Policies (continued)

Risk management - The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illness; natural disasters; medical malpractice; and employee accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Net position - Net position of the District is classified into three components. The net investment in capital assets component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of related debt that is attributable to the acquisition, construction, or improvement of those assets. The restricted component of net position represents noncapital assets that must be used for a specific purpose. The unrestricted component of net position is the remaining net amount of the assets and liabilities that are not included in the determination of net investment in capital assets or the restricted components of net position.

Operating revenues and expenses - The District's statements of revenues, expenses, and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues, such as patient service revenue, result from exchange transactions associated with providing health care services—the District's primary business.

Nonexchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as other operating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs. Tax levy income and debt service related to general obligation bonds and peripheral or incidental transactions are reported as nonoperating income or expense.

Net patient service revenue - Patient service revenue is recorded at established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Preliminary settlements under reimbursement agreements with Medicare and Medicaid are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Reimbursements received from certain third-party payors are subject to audit and retroactive adjustment. Provision for possible adjustment as a result of audits is recorded in the financial statements. When reimbursement settlements are received, or when information becomes available with respect to reimbursement changes, any variations from amounts previously accrued are accounted for in the period in which the settlements are received or the change in information becomes available.

Charity care - The District provides care to indigent patients who meet certain criteria under its charity care policies. Because the District does not pursue collection of amounts determined to qualify as charity care, they are not reported as net patient service revenue. Forgone revenue for charity care provided during 2012 and 2011 measured by the District's standard charges was \$1,012,054 and \$561,214, respectively.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 2 - Summary of Significant Accounting Policies (continued)

Federal income taxes - The District, as a political subdivision of the state of Washington, is not subject to federal income taxes under Section 115 of the Internal Revenue Code.

Reclassifications - Certain amounts on the December 31, 2011, financial statements have been reclassified to conform to the December 31, 2012, financial statement presentation.

Subsequent events - Subsequent events are events or transactions that occur after the statement of net position date but before financial statements are available to be issued. The District recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statement of net position, including the estimates inherent in the process of preparing the financial statements. The District's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of net position but arose after the statement of net position date and before the financial statements are available to be issued.

The District has evaluated subsequent events through July 15, 2013, which is the date the financial statements are issued.

Note 3 - Net Patient Service Revenue

The District has agreements with third-party payors that provide for payments to the District at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows.

Medicare - The District converted to critical access hospital status under the Medicare program on December 1, 2005, under which inpatient, swing-bed, and outpatient services and hospital-based clinics are reimbursed on a cost basis. Inpatient acute, swing-bed, and outpatient care services rendered to Medicare program beneficiaries are paid on an interim basis at a percentage of billed charges. These interim payments will be subject to final settlement upon submission and audit of the cost report to the Medicare fiscal intermediary. The District's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization.

Net patient service revenue under the Medicare program totaled approximately \$15,011,000 and \$12,131,000 for 2012 and 2011, respectively. Net unsecured patient accounts receivable due from Medicare at December 31 was \$1,860,000 and \$1,150,000 in 2012 and 2011, respectively.

Medicaid - As a critical access hospital, the District is reimbursed for inpatient and outpatient services rendered to Medicaid program beneficiaries on a cost reimbursement methodology. Under this methodology, the District is reimbursed at a tentative rate, with final settlement determined after audits by the Medicare fiscal intermediary of annual cost reports submitted by the District. Long-term care services are paid on a cost reimbursement basis, which may not exceed allocated costs plus state-mandated cost limits. Net patient service revenue under the Medicaid program totaled approximately \$972,000 and \$1,380,000 for 2012 and 2011, respectively. Net unsecured patient accounts receivable due from Medicaid at December 31 were \$611,000 and \$395,000 in 2012 and 2011, respectively.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 3 - Net Patient Service Revenue (continued)

The District's estimates of final settlements to or from Medicare and Medicaid for all years through 2012 have been recorded in the accompanying statements of net position. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Differences between the net amounts accrued and subsequent settlements are recorded in operations at the time of settlement. The District's Medicare cost reports have been audited by the Medicare fiscal intermediary through December 31, 2009.

The following are the components of net patient service revenue for the District for the years ended December 31:

	<u>2012</u>	<u>2011</u>
Gross patient service charges	<u>\$ 29,895,162</u>	<u>\$ 27,841,296</u>
Adjustments to patient service charges		
Contractual discounts	6,214,252	5,645,752
Provision for bad debts	540,094	1,030,971
Charity care	<u>1,012,054</u>	<u>561,214</u>
	<u>7,766,400</u>	<u>7,237,937</u>
Net patient service revenue	<u><u>\$ 22,128,762</u></u>	<u><u>\$ 20,603,359</u></u>

Note 4 - Deposits and Investments

The District makes investments in accordance with Washington State law. Eligible investments include obligations secured by the U.S. Treasury, other obligations of the United States or its agencies, certificates of deposit with approved institutions, insured money market funds, commercial paper, registered warrants of local municipalities, the Washington State Local Government Investment Pool, eligible bankers' acceptances, and repurchase agreements (up to 30 days).

As a political subdivision of the State, the District categorizes deposits and investments to give an indication of the risk assumed at year-end. Category 1 includes deposits and investments that are insured, registered, or held by the District's agent in the District's name. Category 2 includes uninsured and unregistered investments that are held by the broker's or dealer's trust department or agent in the District's name. Category 3 includes uninsured and unregistered deposits and investments for which the securities are held by the broker or dealer, or its trust department or agent, but not in the District's name. The Revised Code of Washington, Chapter 39, authorizes municipal governments to invest their funds in a variety of investments including federal, state, and local government certificates, notes, or bonds; the Washington State Local Government Investment Pool; savings accounts in qualified public depositories; and certain other investments. All cash and cash equivalents held by the County Treasurer's Office are insured by the State of Washington Public Deposit Protection Commission, as provided by Chapter 39.58 of the Revised Code of Washington. Qualified public depositories pledge securities with this Commission, which are available to insure public deposits within the state of Washington.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 4 - Deposits and Investments (continued)

All deposits and investments of the District are categorized as Category 1 and consist of the following at December 31:

	2012	2011
Cash and cash equivalents		
Investment in King County Investment Pool	\$ 6,222,798	\$ 187,139
Assets whose use is limited		
UTGO Bond Fund		
Investment in King County Investment Pool	282,613	270,757
Taxes receivable	8,775	15,943
LTGO Bond Fund		
Investment in King County Investment Pool	1,864,385	2,322,760
Taxes receivable	116,391	118,645
Construction Fund		
Investment in King County Investment Pool	3,981	124
	2,276,145	2,728,229
Total deposits and investments	\$ 8,498,943	\$ 2,915,368

The District participates in the King County Investment Pool (KCIP). The King County Finance and Business Operations Division (FBOD) manages and operates the KCIP. Participation by local governments is voluntary. The investment policies of the KCIP are the responsibility of the FBOD, and any proposed changes are reviewed by King County's Executive Finance Committee. The KCIP is comparable to a Rule 2a-7 money market fund recognized by the Securities and Exchange Commission (17 CFR 270.2a-7). Rule 2a-7 funds are limited to high-quality obligations with limited maximum and average maturities, the effect of which is to minimize both market and credit risk. The objectives of the FBOD's investment practices for the KCIP, in priority order, will be safety, liquidity, and return on investment. Separate financial statements for the KCIP are available from King County. The KCIP is not subject to risk evaluation.

Credit risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The District's investment policy limits the types of securities to those authorized by statute; therefore, credit risk is very limited.

Deposits - All of the District's deposits are either insured or collateralized. The District's insured deposits are covered by the Federal Deposit Insurance Corporation (FDIC). Collateral protection is provided by the Washington Public Deposit Protection Commission (PDPC).

Custodial credit risk - Custodial credit risk is the risk that, in the event of a failure of the counterparty, the District will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The District is not exposed to custodial credit risk.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON

NOTES TO FINANCIAL STATEMENTS

Note 4 - Deposits and Investments (continued)

Concentration of credit risk - Concentration of credit risk is the risk of loss attributed to the magnitude of the District's investment in a single issuer. The District is not exposed to concentration of credit risk, because all deposits and investments are insured or collateralized.

Interest rate risk - Interest rate risk is the risk that changes in interest rates of debt instruments will adversely affect the fair value of an investment. The District is not exposed to interest rate risk.

Note 5 - Property Taxes

The County Treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities. Taxes are levied annually on January 1 on property values listed as of the prior May 31. Assessed values are established by the County Assessor at 100% of the fair market value. A revaluation of all property is required every four years. Taxes are due in two equal installments on April 30 and October 31. Collections are distributed monthly to the District by the County Treasurer. Tax collections for the years ended December 31, 2012 and 2011, were 97.94% and 97.69% of the taxes levied during those respective years.

The District is permitted by law to levy up to \$0.75 per \$1,000 of assessed valuation for general District purposes. The Washington State constitution and Washington State law, RCW 84.55.010, limit the rate. The District may also levy taxes at a lower rate. Further amounts of tax need to be authorized by the vote of the people.

For 2012 and 2011, the District's regular tax levy was \$0.49 and \$0.48 per \$1,000 on a total assessed valuation of \$6,044,421,680 and \$6,293,526,535, respectively, for a total regular levy of \$2,973,068 and \$3,019,507, respectively. A portion of the tax revenue from the regular levy has been pledged toward payments of the limited tax general obligation (LTGO) bonds.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 6 - Capital Assets

Capital asset additions, retirements, and balances for the years ended December 31, 2012 and 2011, were as follows:

	Balance, December 31, 2011	Additions	Retirements	Transfers	Balance, December 31, 2012
NONDEPRECIABLE CAPITAL ASSETS					
Land	\$ 11,763,838	\$ 1,610,319	\$ -	\$ -	\$ 13,374,157
Construction in progress	8,019,723	1,911,691	-	(1,474,084)	8,457,330
Total nondepreciable capital assets	<u>19,783,561</u>	<u>3,522,010</u>	<u>-</u>	<u>(1,474,084)</u>	<u>21,831,487</u>
DEPRECIABLE CAPITAL ASSETS					
Land improvements	32,592	-	-	-	32,592
Buildings and improvements	1,165,269	4,715	-	-	1,169,984
Equipment	2,364,015	121,135	-	1,474,084	3,959,234
LESS ACCUMULATED DEPRECIATION					
Buildings and improvements	(416,593)	(209,104)	-	-	(625,697)
Equipment	<u>(2,224,826)</u>	<u>(181,719)</u>	<u>-</u>	<u>-</u>	<u>(2,406,545)</u>
Depreciable capital assets, net	<u>920,457</u>	<u>(264,973)</u>	<u>-</u>	<u>1,474,084</u>	<u>2,129,568</u>
Capital assets, net	<u>\$ 20,704,018</u>	<u>\$ 3,257,037</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 23,961,055</u>
	Balance, December 31, 2010	Additions	Retirements	Transfers	Balance, December 31, 2011
NONDEPRECIABLE CAPITAL ASSETS					
Land	\$ 11,763,838	\$ -	\$ -	\$ -	\$ 11,763,838
Construction in progress	5,324,491	2,695,232	-	-	8,019,723
Total nondepreciable capital assets	<u>17,088,329</u>	<u>2,695,232</u>	<u>-</u>	<u>-</u>	<u>19,783,561</u>
DEPRECIABLE CAPITAL ASSETS					
Land improvements	30,285	2,307	-	-	32,592
Buildings and improvements	1,126,523	38,746	-	-	1,165,269
Equipment	2,889,797	89,291	(615,073)	-	2,364,015
LESS ACCUMULATED DEPRECIATION					
Buildings and improvements	(224,054)	(192,539)	-	-	(416,593)
Equipment	<u>(2,441,383)</u>	<u>(87,583)</u>	<u>304,140</u>	<u>-</u>	<u>(2,224,826)</u>
Depreciable capital assets, net	<u>1,381,168</u>	<u>(149,778)</u>	<u>(310,933)</u>	<u>-</u>	<u>920,457</u>
Capital assets, net	<u>\$ 18,469,497</u>	<u>\$ 2,545,454</u>	<u>\$ (310,933)</u>	<u>\$ -</u>	<u>\$ 20,704,018</u>

The District capitalized interest cost of \$975,089 and \$752,396 during the years ended December 31, 2012 and 2011.

Depreciation expense for the years ended December 31, 2012 and 2011, was \$390,823 and \$280,122, respectively.

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 7 - Line of Credit

The District has a line of credit with a bank for \$1,500,000. The interest rate at December 31, 2012, was 7.0% and is payable monthly. The line of credit expires in 2013. Changes in the District's line of credit for the years ended December 31, 2012 and 2011, are as follows:

Balance, January 1, 2012	Additions	Reductions	Balance December 31, 2012
\$ 1,286,267	\$ 103,733	\$ -	\$ 1,390,000
Balance, January 1, 2011	Additions	Reductions	Balance December 31, 2011
\$ 742,000	\$ 1,944,267	\$ (1,400,000)	\$ 1,286,267

Note 8 - Long-Term Debt and Other Noncurrent Liabilities

Interest rates and maturities of long-term debt at December 31, 2012 and 2011, for the District consisted of the following:

	2012	2011
Limited tax general obligation bonds, series 2011, 6.50% to 7.00%, due semiannually on June 1 and December 1, maturing in 2040, with annual amounts ranging from \$15,000 to \$4,335,000, net of unamortized loss on refinance of \$72,007.	\$ 15,287,993	\$ 15,287,993
Limited tax general obligation bonds, series 2009, 7.00% to 7.25%, due semiannually on June 1 and December 1, maturing in 2039, with annual amounts ranging from \$240,000 to \$2,615,000, net of unamortized discount of \$560,648 and \$582,008 and unamortized loss on refinance of \$194,405 and \$260,045 in 2011 and 2010, respectively.	20,888,183	20,802,947
Limited tax general obligation and refunding bonds, series 2005A, 5.35%, due semiannually on June 1 and December 1, maturing in 2025, with annual amounts ranging from \$52,000 to \$583,333.	3,941,333	3,941,333
Capital lease obligation, stated at present value of future minimum lease payments.	107,064	-
Note payable to MHC LTRA, Inc., paid off in 2012.	-	6,304,988
Note payable to MVPB, LLC, paid off in 2012.	-	327,244
	40,224,573	46,664,505
Less current portion	(32,928)	(6,632,232)
	<u>\$ 40,191,645</u>	<u>\$ 40,032,273</u>

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 8 - Long-Term Debt and Other Noncurrent Liabilities (continued)

Changes in the District's long-term liabilities and line of credit during the years ended December 31, 2012 and 2011, are summarized below:

	Balance, December 31, 2011	Additions	Reductions	Balance, December 31, 2012	Amounts Due Within One Year
Bonds payable					
2011 LTGO bonds	\$ 15,287,993	\$ -	\$ -	\$ 15,287,993	\$ -
2009 LTGO bonds	20,802,947	-	85,236	20,888,183	-
2005A LTGO bonds	3,941,333	-	-	3,941,333	-
Note payable to MHC LTRA, Inc.	6,304,988	-	(6,304,988)	-	-
Note payable to MVPB, LLC	327,244	-	(327,244)	-	-
Capital lease obligation	-	134,195	(27,131)	107,064	32,928
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total noncurrent liabilities	<u>\$ 46,664,505</u>	<u>\$ 134,195</u>	<u>\$ (6,574,127)</u>	<u>\$ 40,224,573</u>	<u>\$ 32,928</u>
	Balance, December 31, 2010	Additions	Reductions	Balance, December 31, 2011	Amounts Due Within One Year
Bonds payable					
2011 LTGO bonds	\$ -	\$ 15,287,993	\$ -	\$ 15,287,993	\$ -
2009 LTGO bonds	20,715,947	87,000	-	20,802,947	-
2006B LTGO bonds	5,712,000	-	(5,712,000)	-	-
2005A LTGO bonds	6,874,000	-	(2,932,667)	3,941,333	-
2005 UTGO bonds	126,764	-	(126,764)	-	-
Note payable to MHC LTRA, Inc.	6,679,988	-	(375,000)	6,304,988	6,304,988
Note payable to MVPB, LLC	-	429,209	(101,965)	327,244	327,244
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total noncurrent liabilities	<u>\$ 40,108,699</u>	<u>\$ 15,804,202</u>	<u>\$ (9,248,396)</u>	<u>\$ 46,664,505</u>	<u>\$ 6,632,232</u>

Scheduled principal and interest repayments on long-term debt are as follows:

	Principal	Interest
2013	\$ 32,928	\$ 2,843,963
2014	87,368	2,840,132
2015	146,989	2,833,205
2016	185,778	2,823,434
2017	246,667	2,811,828
Amounts due 2018 - 2022	2,378,000	13,783,517
Amounts due 2023 - 2027	3,405,667	13,030,091
Amounts due 2028 - 2032	7,460,000	11,374,640
Amounts due 2033 - 2037	12,790,000	8,013,238
Amounts due 2038 - 2041	14,320,000	2,089,315
	<u>41,053,397</u>	<u>\$ 62,443,363</u>
Less amount representing unamortized discount and gains and losses on refinancings	<u>828,824</u>	
	<u>\$ 40,224,573</u>	

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON

NOTES TO FINANCIAL STATEMENTS

Note 9 - Retirement Plans

Deferred compensation plan - In 2006, the District began offering its employees a deferred compensation plan, the Public Hospital District No. 4, King County, Washington, 457 Plan, created in accordance with Internal Revenue Code (IRC) Section 457. The plan, available to all eligible employees, permits them to defer a portion of their salary until future years. The District makes no contributions to this plan. The deferred compensation is payable to employees upon termination, retirement, death, or unforeseen emergency.

The plan is administered by CPI Qualified Plan Consultants, Inc., and the District has limited administrative involvement and does not perform the investing function for the plan. The District does not hold the assets of the plan in a trustee capacity and does not perform fiduciary accountability for the plan. Therefore, the District employees' deferred compensation plan created in accordance with IRC 457 is not reported on the financial statements of the District. Contributions made by employees to the 457 Plan totaled approximately \$153,000 and \$63,000 in 2012 and 2011, respectively.

Defined contribution plan - In 2006, the District also began sponsoring a defined contribution plan in accordance with Internal Revenue Code Section 403(b) covering substantially all qualified employees. Plan provisions and contribution requirements are established by the District and may be amended by the District's Board of Commissioners. Active participants meeting hourly and employee contribution criteria receive an employer matching contribution based on a percentage of the employees' base salary, subject to certain limitations. The employer contribution fully vests upon completion of two qualified years or upon the occurrence of death, disability, or attainment of age 65 for qualified employees. Forfeited contributions, if any, are applied against future employer obligations.

The District's liability under the plan, which is also administered by CPI Qualified Plan Consultants, Inc., is limited to its annual contribution. The District's contributions to the employee benefit plan totaled approximately \$117,000 and \$108,000 in 2012 and 2011, respectively. Contributions made by employees to the benefit plan totaled approximately \$563,000 and \$376,000 in 2012 and 2011, respectively. For more information on the plans, contact the District's human resources office.

Note 10 - Concentrations of Credit Risk

The District grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of gross receivables from patients and third-party payors was as follows:

	<u>2012</u>	<u>2011</u>
Medicare	35%	35%
Medicaid	11%	13%
Other commercial	39%	33%
Patient and self-pay	15%	19%
	<u>100%</u>	<u>100%</u>

PUBLIC HOSPITAL DISTRICT NO. 4, KING COUNTY, WASHINGTON
NOTES TO FINANCIAL STATEMENTS

Note 11 - Commitments and Contingencies

Operating leases - The District leases certain facilities and equipment under operating lease arrangements. In 2011, the District vacated a portion of its leased facility space and terminated the related lease agreement before the end of the lease term. As a result, the District recognized a loss of \$22,177 and \$439,413 for the years ended December 31, 2012 and 2011, respectively. The following is a schedule by year of future minimum lease payments as of December 31, 2012:

2013	\$ 357,000
2014	314,000
2015	200,000
2016	<u>140,000</u>
	<u>\$ 1,011,000</u>

Litigation - The District is involved in litigation and regulatory investigations arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the District's future financial position or results from operations.

Compliance with laws and regulations - The health care industry is subject to numerous laws and regulations from federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government activity with respect to investigations and allegations regarding possible violations of these laws and regulations by health care providers, including those related to medical necessity, coding, and billing for services, has increased substantially. Violations of these laws and regulations could result in expulsion from government health care programs, together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the District is in compliance with the fraud and abuse regulations, as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

Insurance - The District has its professional liability insurance coverage with Washington Casualty Company (WCC). This policy provides protection on a "claims-made" basis whereby claims filed in the current year are covered by the current policy. If there are occurrences in the current year, they will be covered in the year the claim is filed only if claims-made coverage is obtained in that year or if the District purchases insurance to cover "prior acts." Current coverage with no deductible is for \$1,000,000 per occurrence subject to a \$5,000,000 annual limit. No liability has been accrued for future claims for acts occurring in the current or prior years. Also, it is possible that claims may exceed coverage obtained in any given year.