



Report of Independent Auditors  
and Financial Statements for  
**Public Hospital District No. 4,  
King County, Washington**

December 31, 2010 and 2009

**MOSS ADAMS** LLP

Certified Public Accountants | Business Consultants

*Acumen. Agility. Answers.*

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## REPORT OF INDEPENDENT AUDITORS

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

We have audited the balance sheet of Public Hospital District No. 4, King County, Washington, as of December 31, 2010 and 2009, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the District's management. 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 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 the District'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, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our 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, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As disclosed in Note 1 to the financial statements, the District sold its hospital campus in July 2008. The District continues to use the existing facility until the note associated with the sale is paid in full. Continued use of the facility, after the note is paid, is subject to mutually agreed-upon market-rate terms.

The accompanying management's discussion and analysis on pages 2 through 6 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

*Moss Adams LLP*

Everett, Washington  
May 2, 2011

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

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**Introduction**

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

**Operational Highlights**

This year, the District continued making progress in our plan to build a new hospital. We have begun the process to apply for HUD 242 financing for the new hospital, and we expect to make the initial application to HUD in the third quarter of 2011.

Inpatient days continued to grow in 2010, increasing by 32% over 2009 levels. The driver of this growth was our growth in swing-bed patient days, which increased by 40%. This led to a bottom line for the District and an increase in net assets of \$151,579. This is the second consecutive year of profitable operations for the District. The District anticipates a continuing trend of profit in future years.

The District issued limited tax general obligation bonds in June 2009 with a par value of \$21,645,000. The proceeds from the bonds were used to pay off existing debt and to pay operating and capital costs of the District, including land acquisition and predevelopment costs for the new hospital.

In November 2010, the District successfully settled a land use lawsuit with MHC LTRA, Inc. that resulted in the District's acquisition of a 22-acre parcel for approximately \$6,700,000. Under the terms of the settlement agreement, the District will make monthly installment payments to MHC LTRA, Inc. in the amount of \$25,000 until May 15, 2015, at which time the balance will be due in full. The District intends to hold this site for future health care expansion needs.

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

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**Statement of Revenues, Expenses, and Changes in Net Assets**

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

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Net operating revenue	\$ 21,423,400	\$ 19,801,954	\$ 13,748,447
Net operating expenses	<u>23,124,432</u>	<u>20,577,119</u>	<u>17,237,404</u>
Operating loss	(1,701,032)	(775,165)	(3,488,957)
Nonoperating income, net	<u>1,852,611</u>	<u>1,103,952</u>	<u>548,449</u>
Change in net assets	151,579	328,787	(2,940,508)
Net deficit, beginning of year	<u>(15,579,092)</u>	<u>(15,907,879)</u>	<u>(12,967,371)</u>
Net deficit, end of year	<u><u>\$ (15,427,513)</u></u>	<u><u>\$ (15,579,092)</u></u>	<u><u>\$ (15,907,879)</u></u>

**Operating Revenue**

District revenues included \$21.4 million in operating revenue adjusted for contractual allowances, bad debts, and charity care. The provision for uncollectible accounts (bad debt plus charity care) decreased from \$1,434,819 in 2009 to \$1,106,059 in 2010, compared with a 16% increase in gross patient revenue from \$21,019,127 in 2009 to \$24,320,173 in 2010.

The increase in gross patient revenue was primarily due to the increase in inpatient (acute and swing patient) days of 32%.

**Operating Expenses**

Operating expense increased by 12%, which matched the 12% increase in net patient revenue. Wages, employee benefits, and contract labor comprised 68% of total operating expenses in 2010, which was the same as the 2009 percentage. There was a 14% increase in salaries due to the increased inpatient volumes.

There was an increase of 7.4% in non-labor expense over 2009 due to the increase in inpatient volumes.

**Nonoperating Income (Expense)**

Taxation for bond principal and interest increased \$707,949 based on bond debt service schedules. Taxation for debt service will decrease in 2011 as the District retires its UTGO debt.

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

**Balance Sheet**

The following is a presentation of certain condensed financial information derived from the District's balance sheet:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
<b>ASSETS</b>			
Current assets	\$ 4,900,336	\$ 4,098,659	\$ 3,569,220
Capital assets, net	18,469,497	9,921,998	3,885,225
Other noncurrent assets	<u>31,095,198</u>	<u>32,813,093</u>	<u>30,130,543</u>
Total assets	<u>\$ 54,465,031</u>	<u>\$ 46,833,750</u>	<u>\$ 37,584,988</u>
<b>LIABILITIES</b>			
Current liabilities	\$ 6,090,837	\$ 4,353,080	\$ 3,425,954
Noncurrent liabilities	<u>63,801,707</u>	<u>58,059,762</u>	<u>50,066,913</u>
Total liabilities	<u>\$ 69,892,544</u>	<u>\$ 62,412,842</u>	<u>\$ 53,492,867</u>
<b>NET ASSETS (DEFICIT)</b>			
Invested in capital assets, net of related debt	\$ (8,581,907)	\$(11,469,656)	\$(12,768,374)
Restricted for debt service	550,174	507,987	460,493
Unrestricted	<u>(7,395,780)</u>	<u>(4,617,423)</u>	<u>(3,599,998)</u>
Total net deficit	<u>(15,427,513)</u>	<u>(15,579,092)</u>	<u>(15,907,879)</u>
Total liabilities and net deficit	<u>\$ 54,465,031</u>	<u>\$ 46,833,750</u>	<u>\$ 37,584,988</u>

**Assets**

Assets increased by \$7,631,281 due to land acquired as a result of the settlement of the lawsuit with MHC LTRA, in which the District agreed to purchase the MHC LTRA property. Additional capital investments associated with the new hospital project also increased assets. Current assets increased primarily due to the increase in accounts receivable, which was greater than the decrease in cash.

**Liabilities and Net Assets (Deficit)**

Current liabilities increased from \$4,353,080 to \$6,090,837 due to an increase in accounts payable associated with the increase in inpatient volumes and an outstanding balance on a line of credit the District entered into in June 2010.

Net deficit decreased due to the District's profits in 2010.

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

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**Balance Sheet (continued)**

**Deferred Gain**

Deferred gain was recorded on the sale of the hospital campus in 2008. This decreased with payments on the note from the purchasers of the current hospital property.

**Long-Term Debt**

Long-term debt increased as a result of the settlement with MHC LTRA. The purchase of the property over time is treated as a long-term liability.

**Net Income**

The District had net income of \$151,579. This was the second consecutive year of profit for the District. The continued improved results were due to the increase in inpatient revenue resulting from the law change in April 2009 that increased the hospital's swing-bed allowance to 25 beds.

The District has been able to successfully market its inpatient and outpatient programs to the community and to tertiary hospitals, which led to the increase in inpatient volumes. We expect our continued marketing programs along with the building of a new hospital to continue to increase our patient volumes.

**Statement of Cash Flows**

Net cash from operating activities (\$1,759,172) represents a decrease from 2009's (\$619,962). Tax revenue increased from \$3,889,926 in 2009 to \$4,042,695 in 2010.

**Other Factors Influencing District Operations**

The District currently plans to begin construction of a new facility on a seven-acre site near the intersection of State Highway 18 and Interstate 90 in the spring of 2013 or sooner. 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, a 10-room emergency department, and rehabilitation, radiology, and pharmacy services.

In July 2008, the District sold the existing hospital and campus for \$30,000,000. The sale was financed by the District, which holds a note from the purchaser for that amount. The note matures on May 1, 2015. The purchaser began making payments of \$50,000 per month in May of 2010; payments will continue until May 1, 2015, at which time the remaining balance on the sale is due in full. The District will continue to use the hospital and campus while it completes a replacement facility to be located at the intersection of Interstate 90 and State Highway 18. Continued use of the facility after the note is paid is subject to mutually agreeable, market-rate lease terms.

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

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**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  
BALANCE SHEET**

**ASSETS**

	DECEMBER 31,	
	2010	2009
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 316,018	\$ 599,445
Assets limited as to use required for current liabilities	416,936	533,091
Patient accounts receivable, net of allowances for doubtful accounts and contractual adjustments of \$208,484 in 2010 and \$303,200 in 2009	3,553,925	2,516,123
Other receivables	13,457	
Note receivable	600,000	450,000
Total current assets	<u>4,900,336</u>	<u>4,098,659</u>
ASSETS LIMITED AS TO USE, net of current portion	<u>1,571,954</u>	<u>2,681,528</u>
NOTE RECEIVABLE, net of current portion	<u>29,000,000</u>	<u>29,550,000</u>
<b>CAPITAL ASSETS</b>		
Land	11,763,838	5,008,850
Construction in progress	5,324,491	3,895,220
Depreciable capital assets, net of accumulated depreciation and amortization	<u>1,381,168</u>	<u>1,017,928</u>
Total capital assets, net of accumulated depreciation and amortization	<u>18,469,497</u>	<u>9,921,998</u>
DEFERRED FINANCING COSTS	<u>523,244</u>	<u>581,565</u>
	<u>\$ 54,465,031</u>	<u>\$ 46,833,750</u>

**LIABILITIES AND NET ASSETS**

<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 2,092,882	\$ 1,051,747
Accrued compensation and related liabilities	1,064,218	656,792
Accrued interest payable	191,423	189,862
Estimated third-party payor settlements	1,470,314	1,516,346
Line of credit	742,000	
Current maturities of long-term debt	<u>530,000</u>	<u>938,333</u>
Total current liabilities	6,090,837	4,353,080
DEFERRED GAIN	24,223,008	24,602,287
LONG-TERM DEBT, net of current maturities	<u>39,578,699</u>	<u>33,457,475</u>
Total liabilities	<u>69,892,544</u>	<u>62,412,842</u>
<b>NET ASSETS (DEFICIT)</b>		
Invested in capital assets net of related debt	(8,581,907)	(11,469,656)
Restricted for debt service	550,174	507,987
Unrestricted	<u>(7,395,780)</u>	<u>(4,617,423)</u>
Total net assets (deficit)	<u>(15,427,513)</u>	<u>(15,579,092)</u>
	<u>\$ 54,465,031</u>	<u>\$ 46,833,750</u>

**PUBLIC HOSPITAL DISTRICT NO. 4,  
KING COUNTY, WASHINGTON  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**

	YEAR ENDED DECEMBER 31,	
	2010	2009
<b>OPERATING REVENUE</b>		
Net patient service revenue (net of provision for bad debts of \$643,069 in 2010 and \$905,619 in 2009)	\$ 20,614,208	\$ 18,421,239
Taxation for operations	755,260	1,310,689
Other	53,932	70,026
Total operating revenue	<u>21,423,400</u>	<u>19,801,954</u>
<b>OPERATING EXPENSES</b>		
Salaries and wages	13,072,768	11,464,379
Employee benefits	2,582,360	2,162,025
Professional fees	1,469,345	1,406,205
Supplies	1,932,311	1,810,278
Repairs and maintenance	49,540	66,967
Utilities	351,956	358,211
Purchased services	1,452,298	1,248,102
Insurance	329,837	365,187
Leases and rentals	842,484	717,727
Depreciation and amortization	345,850	335,347
Other	695,683	642,691
Total operating expenses	<u>23,124,432</u>	<u>20,577,119</u>
<b>OPERATING LOSS</b>	<u>(1,701,032)</u>	<u>(775,165)</u>
<b>NONOPERATING INCOME (EXPENSE)</b>		
Investment income, net of accounts capitalized	36,656	49,353
Taxation for bond principal and interest	3,287,186	2,579,237
Interest expense, net of amount capitalized	(1,795,449)	(1,356,783)
Gain (loss) on disposal of capital assets	309,435	(178,823)
Other, net	14,783	10,968
Nonoperating income, net	<u>1,852,611</u>	<u>1,103,952</u>
<b>CHANGE IN NET ASSETS</b>	151,579	328,787
<b>NET DEFICIT, beginning of year</b>	<u>(15,579,092)</u>	<u>(15,907,879)</u>
<b>NET DEFICIT, end of year</b>	<u>\$ (15,427,513)</u>	<u>\$ (15,579,092)</u>

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

**Increase (Decrease) in Cash and Cash Equivalents**

	YEAR ENDED DECEMBER 31,	
	2010	2009
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash received from and on behalf of patients	\$ 19,530,374	\$ 19,556,733
Cash paid to suppliers	(15,247,702)	(13,917,440)
Cash paid to employees	(6,082,319)	(6,453,992)
Other cash receipts	40,475	194,737
Net cash from operating activities	<u>(1,759,172)</u>	<u>(619,962)</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
Cash from tax levies considered a noncapital financing activity	755,260	1,310,689
Other	14,783	10,968
Net cash from noncapital financing activities	<u>770,043</u>	<u>1,321,657</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchase of capital assets	(2,248,741)	(6,566,997)
Cash received for sale of capital assets	(34,464)	16,054
Cash from tax levies for general obligation bonds	3,293,467	2,549,207
Change in line of credit	742,000	
Payment received from note receivable	400,000	
Principal payments on long-term debt	(967,097)	(13,195,039)
Proceeds from long-term debt, net of discount		21,018,493
Cash paid for issuance of long-term debt		(541,125)
Interest paid on bonds and capital lease obligations, net of amount capitalized	<u>(1,735,567)</u>	<u>(1,558,285)</u>
Net cash from capital and related financing activities	<u>(550,402)</u>	<u>1,722,308</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Investment income, net of amount capitalized	<u>36,656</u>	<u>49,353</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<u>(1,502,875)</u>	<u>2,473,356</u>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<u>3,677,191</u>	<u>1,203,835</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<u><u>\$ 2,174,316</u></u>	<u><u>\$ 3,677,191</u></u>
<b>RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET ASSETS</b>		
Cash and cash equivalents	\$ 316,018	\$ 599,445
Cash and cash equivalents in assets whose use is limited	<u>1,858,298</u>	<u>3,077,746</u>
	<u><u>\$ 2,174,316</u></u>	<u><u>\$ 3,677,191</u></u>

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

**Increase (Decrease) in Cash and Cash Equivalents**

	YEAR ENDED DECEMBER 31,	
	2010	2009
<b>RECONCILIATION OF OPERATING LOSS TO NET CASH FROM OPERATING ACTIVITIES</b>		
Operating loss	\$ (1,701,032)	\$ (775,165)
Adjustments to reconcile operating loss to net cash from operating activities		
Revenue from tax levies considered noncapital financing activity	(755,260)	(1,310,689)
Depreciation and amortization	345,850	335,347
Provision for bad debts	643,069	905,619
Change in assets and liabilities		
Patient accounts receivable	(1,680,871)	(1,302,962)
Other receivables	(13,457)	124,711
Estimated third-party payor settlements	(46,032)	1,532,837
Inventories, prepaid expenses, and other		1,231
Accounts payable	1,041,135	160,145
Accrued compensation and related liabilities	407,426	(291,036)
Net cash from operating activities	<b>\$ (1,759,172)</b>	<b>\$ (619,962)</b>
 <b>SUPPLEMENTAL DISCLOSURE OF NONCASH CAPITAL ACTIVITY</b>		
Acquisition of property with note payable to seller	<b>\$ 6,754,988</b>	

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

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**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 was 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 were identified and preliminary site evaluations performed.

In July 2008, the District sold the existing hospital and campus for \$30,000,000. The sale was financed by the District, which holds a note from the purchaser for that amount. The note matures on May 1, 2015. The purchaser began making payments of \$50,000 per month in May of 2010 and continues until May 1, 2015, at which time the remaining balance on the sale is due in full. The District will continue to use the hospital and campus while it completes a replacement facility to be located at the intersection of Interstate 90 and State Highway 18. The District continues to use the existing facility until the note is paid in full. Continued use of the facility after the note is paid is subject to mutually agreeable, market-rate lease terms.

In November 2010, the District successfully settled a land use lawsuit with MHC LTRA, Inc. that will result in the District's acquisition of a 22-acre parcel for approximately \$6,700,000. Under the terms of the settlement agreement, the District will make monthly installment payments to MHC LTRA, Inc. in the amount of \$25,000 until May 15, 2015, at which time the balance will be due in full. The District intends to hold this site for future health care expansion needs.

**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.

**Enterprise fund accounting** - The District uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the District has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board, including those issued after November 30, 1989, that do not conflict with GASB pronouncements.

**Note 2 - Summary of Significant Accounting Policies (continued)**

**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.

**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 bankers' acceptances, repurchase agreements, obligations of the United States Government, and certificates of deposit with financial institutions in accordance with state guidelines.

All District investments are carried at market value except for debt securities purchased within one year of maturity, which are carried at amortized cost. Investment income earned on self-insurance funds and the revenue bond indenture agreements are reported as other operating revenue. Realized and unrealized investment income or losses on other investments are 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. The note matures on May 1, 2015. The purchaser began making payments of \$50,000 per month in May 2010; the payments will continue until May 1, 2015, at which time, the remaining balance on the sale is due in full.

**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.

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

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**Note 2 - Summary of Significant Accounting Policies (continued)**

**Deferred gain** - The gain on the sale of the hospital campus is recorded on the installment basis. Deferred gain was recorded in the amount of \$24,602,287 and the gain will be recorded as nonoperating revenue as payments are made on the note receivable. \$379,279 of the deferred gain was recognized as income for the year ended December 31, 2010.

**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.

**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 assets** - Net assets of the District are classified into three components: Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital assets that must be used for a specific purpose, as specified by debtors, grantors, or contributors external to the District. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital net of related debt or restricted.

**Operating revenues and expenses** - The District's statement of revenues, expenses, and changes in net assets distinguishes 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.

**Note 2 - Summary of Significant Accounting Policies (continued)**

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 2010 and 2009 measured by the District's standard charges was \$462,990 and \$529,200, respectively.

**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, 2009, financial statements have been reclassified to conform to the December 31, 2010, financial statement presentation.

**Subsequent events** - Subsequent events are events or transactions that occur after the balance sheet 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 balance sheet, 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 balance sheet but arose after the balance sheet date and before the financial statements are available to be issued.

The District has evaluated subsequent events through May 2, 2011, which is the date the financial statements are were issued.



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**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 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 \$12,597,000 and \$11,302,000 for 2010 and 2009, respectively. Net unsecured patient accounts receivable due from Medicare at December 31 was \$1,171,000 and \$1,461,000 in 2010 and 2009, 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 \$1,226,000 and \$1,497,000 for 2010 and 2009, respectively. Unsecured patient accounts receivable due from Medicaid at December 31 was \$397,000 and \$496,000 in 2010 and 2009, respectively.

The District's estimates of final settlements to or from Medicare and Medicaid for all years through 2010 have been recorded in the accompanying balance sheet. 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, 2006.

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**Note 3 - Net Patient Service Revenue (continued)**

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

	2010	2009
Gross patient service charges	\$ 24,320,173	\$ 21,019,127
Adjustments to patient service charges		
Contractual discounts	2,599,906	1,163,069
Provision for bad debts	643,069	905,619
Charity care	462,990	529,200
	3,705,965	2,597,888
Net patient service revenue	\$ 20,614,208	\$ 18,421,239

**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,  
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**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:

	<u>2010</u>	<u>2009</u>
Cash and cash equivalents		
Cash on hand		\$ 540
Investment in King County Investment Pool	\$ 316,018	598,905
	<u>316,018</u>	<u>599,445</u>
Assets whose use is limited		
UTGO Bond Fund		
Investment in King County Investment Pool	381,832	276,141
Taxes receivable	31,069	32,440
LTGO Bond Fund		
Investment in King County Investment Pool	1,476,422	2,798,280
Taxes receivable	99,523	104,433
Construction Fund		
Investment in King County Investment Pool	<u>44</u>	<u>3,325</u>
	<u>1,988,890</u>	<u>3,214,619</u>
Total deposits and investments	<u>\$ 2,304,908</u>	<u>\$ 3,814,064</u>

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).

**Note 4 - Deposits and Investments (continued)**

**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.

**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, as 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.

**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.

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 2010 and 2009, the District's regular tax levy was \$0.46 and \$0.39 per \$1,000 on a total assessed valuation of \$6,454,809,181 and \$7,463,869,159, respectively, for a total regular levy of \$2,944,865 and \$2,897,756, respectively. A portion of the tax revenue from the regular levy has been pledged toward payments of the limited tax general obligation (LTGO) bonds. In addition, there is a voter-approved tax levy for service of the unlimited tax general obligation (UTGO) bonds. For 2010 and 2009, the tax levy UTGO for bond service was \$0.17 and \$0.15 per \$1,000 on a total assessed valuation, respectively, for a total UTGO bond levy of \$994,731 and \$992,170, respectively.

**PUBLIC HOSPITAL DISTRICT NO. 4,  
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NOTES TO FINANCIAL STATEMENTS**

**Note 6 - Capital Assets**

Capital asset additions, retirements, and balances for the years ended December 31, 2010 and 2009, were as follows:

	Balance, December 31, 2009	Additions	Retirements	Balance, December 31, 2010
<b>NONDEPRECIABLE CAPITAL ASSETS</b>				
Land	\$ 5,008,850	\$ 6,754,988	\$ -	\$ 11,763,838
Construction in progress	3,895,220	1,429,271		5,324,491
Total nondepreciable capital assets	<u>8,904,070</u>	<u>8,184,259</u>		<u>17,088,329</u>
<b>DEPRECIABLE CAPITAL ASSETS</b>				
Land improvements	9,459	20,826		30,285
Buildings and improvements	516,316	610,207		1,126,523
Equipment	2,811,740	78,057		2,889,797
<b>LESS ACCUMULATED DEPRECIATION</b>				
Land improvements				
Buildings and improvements	(129,583)	(94,471)		(224,054)
Equipment	(2,190,004)	(251,379)		(2,441,383)
Depreciable capital assets, net	<u>1,017,928</u>	<u>363,240</u>	<u>-</u>	<u>1,381,168</u>
Capital assets, net	<u>\$ 9,921,998</u>	<u>\$ 8,547,499</u>	<u>\$ -</u>	<u>\$ 18,469,497</u>
	Balance, December 31, 2008	Additions	Retirements	Balance, December 31, 2009
<b>NONDEPRECIABLE CAPITAL ASSETS</b>				
Land		\$ 5,008,850		\$ 5,008,850
Construction in progress	\$ 2,455,178	1,440,042		3,895,220
Total nondepreciable capital assets	<u>2,455,178</u>	<u>6,448,892</u>		<u>8,904,070</u>
<b>DEPRECIABLE CAPITAL ASSETS</b>				
Land improvements		9,459		9,459
Buildings and improvements	715,771	25,921	\$ (225,376)	516,316
Equipment	2,729,774	84,907	(2,941)	2,811,740
<b>LESS ACCUMULATED DEPRECIATION</b>				
Land improvements				
Buildings and improvements	(116,897)	(43,944)	31,258	(129,583)
Equipment	(1,898,601)	(291,403)		(2,190,004)
Depreciable capital assets, net	<u>1,430,047</u>	<u>(215,060)</u>	<u>(197,059)</u>	<u>1,017,928</u>
Capital assets, net	<u>\$ 3,885,225</u>	<u>\$ 6,233,832</u>	<u>\$ (197,059)</u>	<u>\$ 9,921,998</u>

**PUBLIC HOSPITAL DISTRICT NO. 4,  
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NOTES TO FINANCIAL STATEMENTS**

**Note 6 - Capital Assets (continued)**

There were no capital lease obligations as of December 31, 2010. As of December 31, 2009, the District recorded \$45,448 of amortization expense related to capital lease obligations.

The District capitalized interest cost of \$677,165 and interest earnings of \$0 during the year ended December 31, 2010. The District capitalized interest cost of \$631,012 and interest earnings of \$51 during the year ended December 31, 2009.

Depreciation expense of operating assets for the years ended December 31, 2010 and 2009, was \$345,850 and \$335,347, respectively.

**Note 7 - Long-Term Debt and Other Noncurrent Liabilities**

Interest rates and maturities of long-term debt at December 31, 2010 and 2009, for the District consisted of the following:

	2010	2009
Limited tax general obligation bonds, series 2009, 7.00% to 7.25%, due semiannually on June 1 and December 1, maturing in 2025, with annual amounts ranging from \$240,000 to \$2,615,000, net of unamortized discount of \$603,368 and unamortized loss on refinance of \$325,685.	\$ 20,715,947	\$ 20,657,947
Limited tax general obligation bonds, series 2006B, 5.35%, due semiannually on June 1 and December 1, maturing in 2025, with annual amounts ranging from \$337,000 to \$1,070,000.	5,712,000	5,797,000
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 \$58,333 to \$886,667.	6,874,000	6,932,333
Note payable to MHC LTRA, Inc., for purchase of property, 6.00%, principal payments due monthly contingent upon receipt of Snoqualmie Indian Reservation Tribe Receivable payments, final principal and accrued interest receivable due May 15, 2015.	6,679,988	
Unlimited tax general obligation and refunding bonds, series 2005, 4.40%, due serially on December 1, maturing in 2011, with annual amounts ranging from \$125,000 to \$800,000, net of unamortized gain on refinance of \$1,764 and \$3,528 in 2010 and 2009, respectively.	126,764	1,008,528
	40,108,699	34,395,808
Less current portion	(530,000)	(938,333)
	<b>\$ 39,578,699</b>	<b>\$ 33,457,475</b>

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

**Note 7 - 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, 2010 and 2009, are summarized below:

	Balance, December 31, 2009	Additions	Reductions	Balance, December 31, 2010	Amounts Due Within One Year
Bonds payable					
2009 LTGO bonds	\$ 20,657,947		\$ 58,000	\$ 20,715,947	
2006B LTGO bonds	5,797,000		(85,000)	5,712,000	
2005A LTGO bonds	6,932,333		(58,333)	6,874,000	\$ 105,000
2005 UTGO bonds	1,008,528		(881,764)	126,764	125,000
Note payable to MHC LTRA, Inc.		\$ 7,104,988	(425,000)	6,679,988	300,000
Deferred gain	24,602,287		(379,279)	24,223,008	
Total noncurrent liabilities	<u>\$ 58,998,095</u>	<u>\$ 7,104,988</u>	<u>\$ (1,771,376)</u>	<u>\$ 64,331,707</u>	<u>\$ 530,000</u>
	Balance, December 31, 2008	Additions	Reductions	Balance, December 31, 2009	Amounts Due Within One Year
Bonds payable					
2009 LTGO bonds		\$ 20,621,699	\$ 36,248	\$ 20,657,947	
2006B LTGO bonds	\$ 9,987,000		(4,190,000)	5,797,000	
2005A LTGO bonds	6,990,667		(58,334)	6,932,333	\$ 58,333
2005 UTGO bonds	1,810,292		(801,764)	1,008,528	880,000
2000 LTGO bonds	3,085,000		(3,085,000)		
Notes payable to banks	5,000,000		(5,000,000)		
Capital lease obligations	61,708		(61,708)		
Deferred gain	24,602,287			24,602,287	
Total noncurrent liabilities	<u>\$ 51,536,954</u>	<u>\$ 20,621,699</u>	<u>\$ (13,160,558)</u>	<u>\$ 58,998,095</u>	<u>\$ 938,333</u>

**PUBLIC HOSPITAL DISTRICT NO. 4,  
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NOTES TO FINANCIAL STATEMENTS**

**Note 7 - Long-Term Debt and Other Noncurrent Liabilities (continued)**

Scheduled principal and interest repayments on bonds and notes payable are as follows:

	Principal	Interest
2011	\$ 530,000	\$ 2,239,614
2012	763,333	2,227,872
2013	833,333	2,218,385
2014	880,000	2,205,402
2015	4,910,000	3,713,411
Amounts due 2016 - 2020	6,310,000	10,233,566
Amounts due 2021 - 2025	6,049,334	8,391,702
Amounts due 2026 - 2030	5,165,000	6,837,840
Amounts due 2031 - 2035	8,415,000	4,558,074
Amounts due 2036 - 2039	7,210,000	1,075,890
	41,066,000	\$ 43,701,756
Less amount representing unamortized discount and gains and losses on refinancings	957,301	
	<u>\$ 40,108,699</u>	

The District issued \$21,645,000 in LTGO improvement and refunding bonds in July 2009. The bond proceeds were used to refund the 2000 LTGO bonds, partially refund the 2006B LTGO bonds, refinance outstanding notes payable, and pay operating and capital costs of the District.

The refunding of the 2000 bonds resulted in the recognition of an accounting loss of \$384,000, which will be deferred and amortized over the remaining life of the 2000 LTGO bonds. The refunding increased the District's aggregate debt service payments by \$4,432,000 through 2038 and resulted in an economic loss (difference between the present values of the old and new debt service payments) of \$88,000.

The partial refunding of the 2006B bonds resulted in the recognition of an accounting loss of \$13,000, which will be deferred and amortized over the remaining life of the 2006B limited tax general obligation bonds. The refunding increased the District's aggregate debt service payments by \$5,704,000 through 2038 and resulted in an economic loss (difference between the present values of the old and new debt service payments) of \$346,000.



**PUBLIC HOSPITAL DISTRICT NO. 4,  
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**Note 8 - 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 AIG VALIC, 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 \$85,000 and \$56,000 in 2010 and 2009, 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 AIG VALIC, is limited to its annual contribution. The District's contributions to the employee benefit plan totaled approximately \$96,000 and \$73,000 in 2010 and 2009, respectively. Contributions made by employees to the benefit plan totaled approximately \$302,000 and \$263,000 in 2010 and 2009, respectively. For more information on the plans, contact the District's human resources office.

**PUBLIC HOSPITAL DISTRICT NO. 4,  
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NOTES TO FINANCIAL STATEMENTS**

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**Note 9 - 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 receivables from patients and third-party payors was as follows:

	2010	2009
Medicare	30%	28%
Medicaid	12%	10%
Regence	4%	10%
Premera	6%	13%
Other commercial	31%	19%
Patient and self-pay	17%	20%
	100%	100%

**Note 10 - Commitments and Contingencies**

**Operating leases** - The District leases certain facilities and equipment under operating lease arrangements. The following is a schedule by year of future minimum lease payments as of December 31, 2010:

YEAR ENDING DECEMBER 31,	AMOUNT
2011	\$ 445,000
2012	420,000
2013	385,000
2014	347,000
2015	227,000
2016	193,000
	\$ 2,017,000

**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.

**PUBLIC HOSPITAL DISTRICT NO. 4,  
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NOTES TO FINANCIAL STATEMENTS**

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**Note 10 - Commitments and Contingencies (continued)**

**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, these 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.