

Audited Financial Statements

**MARK TWAIN
HEALTH CARE DISTRICT**

June 30, 2012

**TCA Partners, LLP
Certified Public Accountants**

Audited Financial Statements

MARK TWAIN HEALTH CARE DISTRICT

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Management's Discussion and Analysis

MARK TWAIN HEALTH CARE DISTRICT

June 30, 2012

The management of the Mark Twain Health Care District (the District) has prepared this annual discussion and analysis in order to provide an overview of the District's performance for the fiscal year ended June 30, 2012 in accordance with the Governmental Accounting Standards Board Statement No. 34, *Basic Financials Statements; Management's Discussion and Analysis for State and Local Governments*. The intent of this document is to provide additional information on the District's financial performance as a whole in addition to providing a prospective look at revenue growth, operating expenses, and capital development plans. This discussion should be reviewed in conjunction with the audited financial statements for the fiscal year ended June 30, 2012 and accompanying notes to the financial statements to enhance one's understanding of the District's financial performance.

Financial Highlights

The District's financial statements consist of three statements: balance sheet; statement of revenues, expenses, and changes in net assets; and statement of cash flows. These financial statements and related notes provide information about the activities of the District, including resources held by the District but restricted for specific purposes by contributors, grantors, or enabling legislation.

The balance sheet includes all of the District's assets and liabilities, using the accrual basis of accounting, as well as an indication about which assets can be used for general purposes and which are designated for a specific purpose.

Highlights within the balance sheet for the year are: (1) total assets decreased by approximately \$2.0 million due to the \$2.1 million decrease in the District's interest in Mark Twain St. Joseph's Healthcare; (2) other receivables increased by approximately \$438,000 due mainly to a large property tax check of \$327,298 issued by the County on May 30, 2012 but not deposited by the District until July, 2012; and (3) a shift of \$86,115 of property taxes receivable shown as other assets in 2011 and now shown as a current receivable in 2012. These were funds borrowed by the County in 2009 which become due from the County on June 30, 2013.

The statement of revenues, expenses and changes in net assets reports all of the revenues earned and expenses incurred during the time period indicated. Net assets (the difference between total assets and total liabilities) is one way to measure the financial health of the District.

Highlights within the statement of revenues, expenses and changes in net assets for the year are: (1) total increase in revenues over expenses of approximately \$69,000 as compare to the prior year increase of \$117,000; and (2) a \$2.1 million 2012 loss in the interest in Mark Twain St Joseph's Healthcare due to the Hospital experiencing significant losses for the year. In 2011, the gain in the interest was approximately \$2.3 million.

The statement of cash flows reports the cash provided by and used by the District's operating activities, as well as other cash sources such as investment income and cash payments for capital additions and improvements. This statement provides meaningful information on how the District's cash was generated and how it was used during the fiscal year.

Management's Discussion and Analysis (continued)

MARK TWAIN HEALTH CARE DISTRICT

Cash and Investments

For the fiscal year ended June 30, 2012, the District's operating cash and investments totaled \$1.9 million as compared to \$2.1 million in fiscal year 2011. At June 30, 2012, days cash on hand were 632 as compared to June 30, 2011 when days cash on hand were 729. The District maintains sufficient cash and cash equivalent balances to pay all short-term liabilities.

Current Assets and Liabilities

Current assets increased by \$272,126 due to a decrease in cash and cash equivalents of \$165,742 and an increase in other receivables of \$437,871 for reasons previously described. Current liabilities of the District decreased by \$18,790. This was due to a \$12,497 increase in accounts payable and accrued expenses coupled with a decrease of \$31,287 in the amount due to Mark Twain St. Joseph's Healthcare. These changes produced a current ratio of 7.99 for June 30, 2012 as compared to 6.68 for June 30, 2011.

Capital Assets

There were slight increases in property and equipment coupled with \$138,951 in depreciation expense for the year for a net decrease in capital assets of \$135,150. There were no construction in progress projects as of June 30, 2012 or June 30, 2011.

District Revenues

The District receives approximately 65% of its operating support from property taxes. These funds are used to support operations of the District. They are classified as operating revenue as the revenue is directly linked to the operations of the District. Property taxes are levied by the County on the District's behalf during the year, and are intended to help finance the District's activities during the same year. Amounts are levied on the basis of the most current property values on record with the County. Revenues decreased slightly from 2011 by only \$11,913 or 1.4%.

The District also rents and/or leases hospital facilities, private office for physicians and land to various entities and individuals for purposes of supplying healthcare to the residents in the surrounding area. Rental income for the year increased by \$25,877 or 6% over the prior year.

Management's Discussion and Analysis (continued)

MARK TWAIN HEALTH CARE DISTRICT

Operating Expenses

Total operating expenses were \$1,261,000 for fiscal year 2012 compared to \$1,193,000 for the prior fiscal year. The 5.8% increase is mainly due primarily to:

A \$44,000 decrease in contracted salaries and benefits for the year due one-time expenditures in 2011 which did not exist in 2012.

A \$53,000 increase in professional fees due to added legal fees in 2012 as the District is restructuring certain agreements.

A \$22,000 increase in utilities due mainly to inflationary factors.

A \$29,000 increase in other expenses of various types for the year.

Economic Factors and Next Fiscal Year's Budget

The District's board approved the fiscal year ending June 30, 2013 budget at a recent 2012 Board meeting. For fiscal year 2013, the District is budgeted to decrease net assets by \$68,000. The decrease is due to several assumptions:

Property taxes were budgeted at the same levels of 2012 while rents increased slightly.

Utilities were budgeted to increase by 5%.

Professional fees and other operating expenses are expected to increase for the year as compared to 2012 levels due to the hiring of a new interim CEO and increased legal fees as certain existing agreements are scheduled to be restructured.

In order to increase the public awareness of health care expenditures, the District is restructuring major agreements which will change the emphasis of District expenditures as they relate to the operations of the Hospital.

TCA Partners, LLP

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Report of Independent Auditors

The Board of Directors
Mark Twain Health Care District
San Andreas, California

We have audited the accompanying balance sheets of Mark Twain Health Care District (the District) as of June 30, 2012 and 2011, 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. Our audits included consideration of internal controls over financial reporting as a basis of designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal controls over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mark Twain Health Care District at June 30, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied limited procedures, which consisted principally of inquiries of District management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

TCA Partners, LLP

November 30, 2012

Balance Sheets

MARK TWAIN HEALTH CARE DISTRICT

	June 30	
	<u>2012</u>	<u>2011</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,937,587	\$ 2,103,329
Other receivables	495,117	57,246
Prepaid expenses and deposits	<u>6,446</u>	<u>6,449</u>
Total current assets	2,439,150	2,167,024
Property and equipment:		
Land	734,306	734,306
Land improvements	150,308	146,507
Buildings and improvements	4,478,938	4,478,938
Equipment	<u>698,156</u>	<u>698,156</u>
	6,061,708	6,057,907
Less accumulated depreciation	<u>(4,839,151)</u>	<u>(4,700,200)</u>
	1,222,557	1,357,707
Interest in Mark Twain St. Joseph's Healthcare	16,339,601	18,427,886
Other assets	<u>8,819</u>	<u>96,062</u>
Total assets	<u>\$ 20,010,127</u>	<u>\$ 22,048,679</u>
Liabilities and Fund Balance		
Current liabilities:		
Accounts payable and accrued expenses	\$ 68,159	\$ 55,662
Due to Mark Twain St. Joseph's Healthcare	<u>237,291</u>	<u>268,578</u>
Total current liabilities	305,450	324,240
Unrestricted fund balance	<u>19,704,677</u>	<u>21,724,439</u>
Total liabilities and fund balance	<u>\$ 20,010,127</u>	<u>\$ 22,048,679</u>

See accompanying notes

Statements of Revenues, Expenses and Changes in Net Assets

MARK TWAIN HEALTH CARE DISTRICT

	Year Ended June 30	
	<u>2012</u>	<u>2011</u>
Revenues:		
District taxes	\$ 844,885	\$ 856,798
Rental income	462,600	436,723
Interest and other income	<u>22,416</u>	<u>16,200</u>
Total revenues, gains and losses	1,329,901	1,309,721
Expenses:		
Salaries and wages		47,635
Employee benefits	21,330	17,945
Professional fees	76,543	23,281
Programs and events	54,763	50,891
Tenant services	42,000	42,000
Medical office building rent	193,542	189,259
Utilities and phone	664,923	642,856
Insurance	12,896	12,672
Repairs and maintenance	564	120
Depreciation and amortization	140,079	139,838
Other operating expenses	<u>54,738</u>	<u>26,057</u>
Total expenses	<u>1,261,378</u>	<u>1,192,554</u>
Excess of revenues over expenses	68,523	117,167
Nonoperating revenues (expenses):		
Gain (loss) in interest in Mark Twain St. Joseph's Healthcare	<u>(2,088,285)</u>	<u>2,309,932</u>
Increase (decrease) in net assets	(2,019,762)	2,427,099
Net assets at the beginning of the year	<u>21,724,439</u>	<u>19,297,340</u>
Net assets at the end of the year	<u>\$ 19,704,677</u>	<u>\$ 21,724,439</u>

See accompanying notes

Statements of Cash Flows

MARK TWAIN HEALTH CARE DISTRICT

	Year Ended June 30	
	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
Cash received from district taxes	\$ 505,992	\$ 863,086
Cash received from rental & other activities	398,866	378,917
Cash paid for employees and benefits	(21,330)	(65,580)
Cash paid for suppliers and outside vendors	<u>(1,045,469)</u>	<u>(918,666)</u>
Net cash used in operating activities	(161,941)	257,757
Cash flows from financing and investing activities:		
Purchases of property and equipment	(3,801)	(17,526)
Interest and dividend income and other	<u>22,416</u>	<u>16,200</u>
Net cash provided by (used in) financing activities	<u>18,615</u>	<u>(1,326)</u>
Net increase (decrease) in cash and cash equivalents	(165,742)	240,231
Cash and cash equivalents at beginning of year	<u>2,103,329</u>	<u>1,863,098</u>
Cash and cash equivalents at end of year	<u>\$ 1,937,587</u>	<u>\$ 2,103,329</u>
Reconciliation of changes in net assets to net cash provided by operating activities		
Excess of revenues over expenses	\$ 68,523	\$ 117,167
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Depreciation and amortization	140,079	139,838
Changes in operating assets and liabilities:		
District tax and other receivables	(351,756)	6,062
Prepaid expenses	3	(15)
Accounts payable and accrued expenses	12,497	26,696
Due to Mark Twain St. Joseph's Healthcare	<u>(31,287)</u>	<u>(31,991)</u>
Net cash provided by operating activities	<u>\$ (161,941)</u>	<u>\$ 257,757</u>

Notes to Financial Statements

MARK TWAIN HEALTH CARE DISTRICT

June 30, 2012

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity: Mark Twain Health Care District (the District) is a tax-exempt political subdivision of the State of California operating under the California Health and Safety Code and is governed by a five-member elected Board of Directors. The District was organized in 1946, and began operating a healthcare facility located in San Andreas, California, in 1951. Effective January 1, 1990, the District obtained regulatory approval to lease the hospital facilities to Mark Twain St. Joseph's Health Care Corporation (the Corporation), a nonprofit public benefit corporation organized without membership in 1987, under the California Nonprofit Public Benefit Corporation Law for the purpose of leasing the hospital facilities from the District. In January 1990, the Corporation entered into a management agreement with St. Joseph's Regional Health System ("SJRHS") of Stockton, California, an affiliate of Dignity Health ("DH"). As of September 2001, the management agreement was amended to replace SJRHS with DH, as SJRHS had been dissolved as part of a CHW reorganization. The Corporation's Board of Trustees is appointed by the District and DH whereby DH appoints three members of the seven-member Corporation Board of Trustees and holds significant reserve powers. In the event of its dissolution, the Corporation's bylaws require that its net assets be divided equally between the District and DH.

Basis of Preparation: The accounting policies and financial statements of the District generally conform with the recommendations of the audit and accounting guide, *Health Care Organizations*, published by the American Institute of Certified Public Accountants. The financial statements are presented in accordance with the pronouncements of the Governmental Accounting Standards Board (GASB). For purposes of presentation, transactions deemed by management to be ongoing, major or central to the provision of health care services are reported as operational revenues and expenses.

The District uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on GASB Statement Number 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, the District has elected to apply the provisions of all relevant pronouncements as the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

Changes in Financial Statement Presentation: The District has adopted the provisions of GASB 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* (Statement 34), as amended by GASB 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and Statement 38, *Certain Financial Statement Note Disclosures*. Statement 34 established financial reporting standards for all state and local governments and related entities. Statement 34 primarily relates to presentation and disclosure requirements. The impact of this change was related to the format of the financial statements; the inclusion of management's discussion and analysis; and the preparation of the statement of cash flows on the direct method. The application of these accounting standards had no impact on the total net assets.

Notes to Financial Statements (continued)

MARK TWAIN HEALTH CARE DISTRICT

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Management's Discussion and Analysis: Statement 34 requires that financial statements be accompanied by a narrative introduction and analytical overview of the District's financial activities in the form of "management's discussion and analysis" (MD&A). This analysis is similar to the analysis provided in the annual reports of organizations in the private sector.

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported results of operations for the period. Actual results could differ from those estimates.

Risk Management: To cover the District against various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accidental benefits, commercial insurance coverage is purchased.

Cash and Cash Equivalents and Investments: The District considers cash and cash equivalents to include certain investments in highly liquid debt instruments, when present, with an original maturity of a short-term nature or subject to withdrawal upon request. Exceptions are for those investments which are intended to be continuously invested. Investments in debt securities are reported at market value. Interest, dividends and both unrealized and realized gains and losses on investments are included as investment income in nonoperating revenues when earned.

Property and Equipment: Property and equipment are reported on the basis of cost, or in the case of donated items, on the basis of fair market value at the date of donation. Routine maintenance and repairs are charged to expense as incurred. Expenditures which increase values, change capacities, or extend useful lives are capitalized. Depreciation of property and equipment and amortization of property under capital leases are computed by the straight-line method for both financial reporting and cost reimbursement purposes over the estimated useful lives of the assets, which range from 5 to 40 years for buildings and improvements, and 5 to 20 years for equipment.

Net Assets: Net assets, under the new GASB requirements, are to be presented in three categories. The first category is net assets "invested in capital assets, net of related debt". This category of net assets consists of capital assets (both restricted and unrestricted), net of accumulated depreciation and reduced by the outstanding principal balances of any debt borrowings that were attributable to the acquisition, construction, or improvement of those capital assets.

The second category is "restricted" net assets. This category consists of externally designated constraints placed on those net assets by creditors (such as through debt covenants), grantors, contributors, law or regulations of other governments or government agencies, or law or constitutional provisions or enabling legislation.

Notes to Financial Statements (continued)

MARK TWAIN HEALTH CARE DISTRICT

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

The third category is “unrestricted” net assets. This category consists of net assets that do not meet the definition or criteria of the previous two categories.

As of June 30, 2012 and 2011, the District is only required to present unrestricted net assets in the presentation of the financial statements as there are no restrictions present under category one or two.

Restricted Funds: The District may receive certain contributions from time to time which are restricted as to use by the donor. Income derived from these funds which is restricted as to use, is transferred to unrestricted revenue in the period the income is earned. Expenditures made for the restricted purpose of acquiring property and equipment, as designated by the donor, are transferred directly from the restricted fund to the unrestricted fund balance. Expenditures made for the restricted operating purposes, as designed by the donor, are reported as other revenue in the financial statements of the period in which the expenditures are made.

District Tax Revenues: The District receives approximately 65% of its operating support from property taxes. These funds are used to support operations of the District. They are classified as operating revenue as the revenue is directly linked to the operations of the District. Property taxes are levied by the County on the District’s behalf during the year, and are intended to help finance the District’s activities during the same year. Amounts are levied on the basis of the most current property values on record with the County. The County has established certain dates to levy, lien, mail bills, and receive payments from property owners during the year. Property taxes are considered delinquent on the day following each payment due date.

Grants and Contributions: From time to time, the District may receive grants from various governmental agencies and private organizations. The District may also receive contributions from related foundation and auxiliary organizations, as well as from individuals and other private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or capital acquisitions. These amounts, when recognized upon meeting all requirements, are reported as components of the statement of revenues, expenses and changes in net assets.

Operating Revenues and Expenses: The District’s statement of revenues, expenses and changes in net assets distinguishes only operating revenues and expenses. Operating revenues result from exchange transactions associated with supporting health care services, which is the District’s principal activity. Operating expenses are all expenses incurred to support health care services.

Reclassifications: Certain financial statement amounts as presented in the prior year financial statements have been reclassified in these, the current year financial statements, in order to conform to the current year financial statement presentation.

Notes to Financial Statements (continued)

MARK TWAIN HEALTH CARE DISTRICT

NOTE B - BANK DEPOSITS

Collateral: As of June 30, 2012 and 2011, the District had deposits invested in a bank of \$1,937,587 and \$2,103,329, respectively. All of these funds were held in deposits, which are collateralized in accordance with the California Government Code (CGC), or federally insured.

Under the provisions of the CGC, California banks and savings and loan associations are required to secure the District's deposits by pledging government securities as collateral. The market value of pledged securities must equal at least 110% of the District's deposits. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the District's total deposits. The pledged securities are held by the pledging financial institution's trust department in the name of the District.

Investments, at times, may consist of state and local agency funds invested in various permissible securities and are stated at quoted market values. Changes in market value between years are reflected as a component of investment income in the accompanying statement of revenues, expenses and changes in net assets.

Statements of Cash Flows: For purposes of the statements of cash flows, all highly liquid investments with original maturities of three months or less are considered to be cash equivalents.

NOTE C - TRANSACTIONS BETWEEN RELATED ORGANIZATIONS

The Corporation provides the District with accounting and administrative services for which the Corporation charges a fee to cover the salaries and benefits of the personnel. This fee totaled approximately \$63,330 and \$63,330 for the years ended June 30, 2012 and 2011, respectively. At June 30, 2012 and 2011, the District had \$237,291 and \$268,578, respectively, in unamortized prepaid rent income resulting from the redemption of the 1986 Bonds made by the Corporation. This amount is being amortized over the period of the lease agreement.

The Corporation leases the District's healthcare facilities in order to conduct patient care services in an acute-care hospital setting. Lease revenue from the Corporation for the years ended June 30, 2012 and 2011 were \$310,599 and \$311,744, respectively.

The hospital facility lease expires on December 31, 2019. The lease payments were initially in amounts adequate to cover payment of utilities, debt service and insurance on the Series 1986A Bonds not covered by the tax and other revenues of the District, and to maintain ratios and fund accounts pursuant to the terms of a Joint Obligor Agreement between the District and the Corporation dated December 31, 1989, and the Bond Indenture dated August 1, 1986, between the District and Harris Trust Company of California, the bond trustee.

As outlined in Note D, the Corporation repaid the Series 1986A Bond debt of the District in exchange for a prepayment of rent originally intended to fund the District's principal debt service. As of June 30, 2005, the prepaid rent transactions have completed their term.

Notes to Financial Statements (continued)

MARK TWAIN HEALTH CARE DISTRICT

NOTE C - TRANSACTIONS BETWEEN RELATED ORGANIZATIONS (continued)

During the year ended June 30, 2008, the District entered into a land and medical office building lease agreement with San Andreas Medical and Professional Office Building (SAMPO). The District leases land located at 704 Mountain Ranch Road in San Andreas to SAMPO at no cost due to the fact that the development of the property by SAMPO was deemed sufficient to offset any future lease payments. SAMPO built and owns the medical office building (MOB) located on the aforementioned land and then leases the MOB to the District. Lease expense for the years ended June 30, 2012 and 2011 regarding this agreement were \$193,542 and \$189,259, respectively. The District has subleased portions of the MOB to the Stockton Cardiology Medical Group, to Dr. Renner, and to the Corporation. Lease revenues under the subleasing arrangements were \$146,224 and \$113,222 for the years ended June 30, 2012 and 2011, respectively.

NOTE D - DEBT BORROWINGS

On May 1, 1996, the Corporation borrowed \$11,175,000 to finance a new health facility and to defease the Mark Twain Hospital District Insured Revenue Bonds Series 1986A (the Series 1986A Bonds) previously issued by the District. In exchange for assuming the District's debt obligation, the Corporation has been granted a prepaid lease payment to the District that has been recorded as a long-term liability in the accompanying financial statements. The prepaid rent will be amortized over the remaining life of the Series 1986A Bonds, originally scheduled to be repaid in full in 2004.

NOTE E - INTEREST IN MARK TWAIN ST. JOSEPH'S HEALTHCARE

In an agreement between Mark Twain St. Joseph's Healthcare (the Corporation) and Mark Twain Health Care District (the District), in the event of a dissolution or a winding up of the Corporation, 50% of its assets remaining after payment, or provision for payment, of all debts and liabilities of the Corporation, shall be distributed to Catholic Healthcare West II, a California nonprofit public benefit corporation. The other 50% shall be distributed to the District. As a result of this agreement, the District has recorded \$16,339,601 and \$18,427,886 as of June 30, 2012 and 2011, respectively, as its portion of its interest in the Corporation. These amounts represent the 50% of the net difference between the assets and the liabilities of the Corporation as of its June 30, 2012 and 2011 audited financial statements.