

THE HEALTH TRUST

FINANCIAL STATEMENTS  
WITH SUPPLEMENTAL INFORMATION

JUNE 30, 2006 AND 2005

(With Independent Auditors' Report Thereon)

## Table of Contents

	<u>Page</u>
Independent Auditors' Report .....	1
Statements of Financial Position as of June 30, 2006 and 2005 .....	3
Statements of Activities for the years ended June 30, 2006 and 2005 .....	5
Statements of Functional Expenses for the years ended June 30, 2006 and 2005 .....	6
Statements of Cash Flows for the years ended June 30, 2006 and 2005 .....	8
Notes to Financial Statements as of June 30, 2006 and 2005 .....	9
Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Governmental Auditing Standards .....	18
Schedule of Expenditures of Federal Awards for the year ended June 30, 2006 .....	20
Notes to Schedule of Federal Awards for the year ended June 30, 2006 .....	21
Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133 .....	22
Schedule of Findings and Questioned Costs .....	24
Schedule of Prior Audit Findings .....	26

# BOITANO, SARGENT & LILLY, LLP

## *Certified Public Accountants*

1760 THE ALAMEDA  
SAN JOSE, CALIFORNIA 95126  
TELEPHONE (408) 287-2123

www.bsllcpa.com  
FAX (408) 294-1856

## *Certified Staff*

CHRIS COLLINS MADRID  
JIMMIE MAGDALENO  
KATHLEEN MATRANGA BENSON  
JAMES C. WAI  
DARRYL WONG  
ANTHIE KARVOUNIS  
CRYSTAL K. HOFER

LOUIS F. BOITANO  
FRANK L. BOITANO  
STEVEN F. BOITANO  
H. OGDEN LILLY

FRANCES V. SARGENT  
(1957-1988)

## Independent Auditors' Report

To the Board of Trustees  
The Health Trust  
San Jose, California

We have audited the accompanying statements of financial position of The Health Trust as of June 30, 2006 and 2005, and the related statements of activities, functional expenses and cash flows for the years then ended. These financial statements are the responsibility of The Health Trust'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 and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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 provides 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 The Health Trust as of June 30, 2006 and 2005, and the statements of activities and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2006 on our consideration of The Health Trust's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audits were performed for the purpose of forming an opinion on the basic financial statements of The Health Trust taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

BOITANO, SARGENT & LILLY, LLP

September 30, 2006

THE HEALTH TRUST  
STATEMENTS OF FINANCIAL POSITION  
JUNE 30, 2006 AND 2005

ASSETS

	<u>2006</u>	<u>2005</u>
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 1,525,000	\$ 3,682,000
Investment in marketable securities	114,961,000	109,366,000
Accounts receivable, net of allowance	1,371,000	2,110,000
Other receivables	125,000	404,000
Prepays	<u>187,000</u>	<u>216,000</u>
Total current assets	<u>118,169,000</u>	<u>115,778,000</u>
PROPERTY AND EQUIPMENT, net of accumulated depreciation of \$1,044,000 and \$886,000, respectively	<u>473,000</u>	<u>569,000</u>
<b>OTHER ASSETS:</b>		
Restricted cash	1,312,000	1,284,000
Other investments	1,729,000	1,569,000
Note receivable	800,000	800,000
Land and building held for investment, net of accumulated depreciation of \$229,000 and \$180,000, respectively	<u>3,774,000</u>	<u>3,823,000</u>
Total other assets	<u>7,615,000</u>	<u>7,476,000</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 126,257,000</u></u>	<u><u>\$ 123,823,000</u></u>

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

THE HEALTH TRUST  
STATEMENTS OF FINANCIAL POSITION (CONTINUED)  
JUNE 30, 2006 AND 2005

LIABILITIES AND NET ASSETS

	2006	2005
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 337,000	\$ 543,000
Accrued payroll and related liabilities	566,000	587,000
Accrued expenses due to discontinued operations	35,000	68,000
Accrued expenses	214,000	162,000
Grants payable	2,648,000	2,364,000
Total current liabilities	3,800,000	3,724,000
 <b>LONG-TERM LIABILITIES:</b>		
Grants payable	343,000	343,000
Accrued expenses due to discontinued operations	2,100,000	2,115,000
Total long-term liabilities	2,443,000	2,458,000
 <b>TOTAL LIABILITIES</b>	 6,243,000	 6,182,000
 <b>NET ASSETS:</b>		
Unrestricted net assets:		
Designated by the Board of Trustees for medically related services and expenditures	92,369,000	89,887,000
Undesignated	23,717,000	23,990,000
Total unrestricted net assets	116,086,000	113,877,000
Temporarily restricted net assets	3,411,000	3,420,000
Permanently restricted net assets	517,000	344,000
Total net assets	120,014,000	117,641,000
 <b>TOTAL LIABILITIES AND NET ASSETS</b>	 \$ 126,257,000	 \$ 123,823,000

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

THE HEALTH TRUST  
STATEMENTS OF ACTIVITIES  
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
UNRESTRICTED NET ASSETS:		
Support:		
Contributions	\$ 100,000	\$ 194,000
United Way of Santa Clara County	128,000	128,000
Government grants	3,775,000	3,355,000
In-kind contribution	214,000	457,000
Total support	4,217,000	4,134,000
Revenue:		
Fee for services	1,431,000	1,021,000
Investment income, net of investment expenses of \$644,000 and \$714,000, respectively	2,484,000	2,643,000
Net realized/unrealized gain	6,407,000	5,607,000
Total revenue	10,322,000	9,271,000
Net assets released from restrictions	1,364,000	1,468,000
Total support and revenue	15,903,000	14,873,000
Expenses:		
Program services	11,595,000	11,964,000
Support services:		
Management and general	1,452,000	1,361,000
Fundraising	715,000	761,000
Total support services	2,167,000	2,122,000
Total expenses	13,762,000	14,086,000
Operating gain	2,141,000	787,000
Gain from discontinued operations	68,000	1,933,000
Increase in unrestricted net assets	2,209,000	2,720,000
TEMPORARILY RESTRICTED NET ASSETS:		
Contributions	1,167,000	1,583,000
Government grants	8,000	20,000
Investment income, net of investment expenses of \$25,000 and \$21,000, respectively	180,000	154,000
Net assets released from restrictions	(1,364,000)	(1,468,000)
Increase (decrease) in temporarily restricted net assets	(9,000)	289,000
PERMANENTLY RESTRICTED NET ASSETS:		
Contributions	173,000	33,000
Increase in permanently restricted net assets	173,000	33,000
INCREASE IN NET ASSETS	2,373,000	3,042,000
NET ASSETS AT BEGINNING OF YEAR	117,641,000	114,599,000
NET ASSETS AT END OF YEAR	\$ 120,014,000	\$ 117,641,000

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

THE HEALTH TRUST  
STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2006

	2006			
	Program Services	Management and General	Fund Raising	Total Expenses
Allocation to agencies	\$ 3,578,000	\$ 0	\$ 0	\$ 3,578,000
Salaries and related expenses				
Salaries and wages	3,205,000	529,000	316,000	4,050,000
Payroll taxes	270,000	40,000	23,000	333,000
Employee benefits	946,000	213,000	82,000	1,241,000
Total salaries and related expenses	4,421,000	782,000	421,000	5,624,000
Services and supplies				
Purchased services	1,944,000	51,000	118,000	2,113,000
Professional fees	251,000	278,000	17,000	546,000
Supplies	601,000	66,000	21,000	688,000
Building and equipment rental	312,000	75,000	49,000	436,000
Utilities	90,000	14,000	9,000	113,000
Insurance	46,000	85,000	0	131,000
Travel	109,000	18,000	4,000	131,000
Advertising	14,000	4,000	0	18,000
Training	19,000	18,000	2,000	39,000
Dues and subscriptions	4,000	3,000	3,000	10,000
Depreciation	128,000	18,000	12,000	158,000
Other expenses	78,000	40,000	59,000	177,000
Total services and supplies	3,596,000	670,000	294,000	4,560,000
Total expenses	\$ 11,595,000	\$ 1,452,000	\$ 715,000	\$ 13,762,000

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

THE HEALTH TRUST  
STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2005

	2005			
	Program Services	Management and General	Fund Raising	Total Expenses
Allocation to agencies	\$ 3,999,000	\$ 0	\$ 0	\$ 3,999,000
Salaries and related expenses				
Salaries and wages	3,020,000	427,000	302,000	3,750,000
Payroll taxes	246,000	38,000	23,000	307,000
Employee benefits	829,000	172,000	93,000	1,093,000
Total salaries and related expenses	4,095,000	637,000	418,000	5,150,000
Services and supplies				
Purchased services	2,013,000	15,000	147,000	2,175,000
Professional fees	480,000	371,000	21,000	872,000
Supplies	540,000	38,000	40,000	618,000
Building and equipment rental	338,000	85,000	51,000	474,000
Utilities	76,000	13,000	9,000	98,000
Insurance	63,000	94,000	0	157,000
Travel	104,000	16,000	7,000	127,000
Advertising	46,000	8,000	2,000	56,000
Training	21,000	12,000	5,000	38,000
Dues and subscriptions	6,000	3,000	3,000	12,000
Depreciation	116,000	20,000	9,000	145,000
Other expenses	67,000	49,000	49,000	165,000
Total services and supplies	3,870,000	724,000	343,000	4,937,000
Total expenses	\$ 11,964,000	\$ 1,361,000	\$ 761,000	\$ 14,086,000

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

THE HEALTH TRUST  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Increase in net assets	\$ 2,373,000	\$ 3,042,000
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation	207,000	193,000
Unrealized (gain) loss on investment	(1,222,000)	2,101,000
Decrease (increase) in operating assets:		
Accounts receivable	740,000	(432,000)
Other receivables and prepaids	307,000	(94,000)
Increase (decrease) in operating liabilities:		
Accounts payable and other accrued expenses	(153,000)	(91,000)
Accrued payroll and related liabilities	(21,000)	(49,000)
Accrued expenses due to discontinued operations	(48,000)	(4,000)
Estimated third party settlements	0	(1,066,000)
Grants payable	<u>284,000</u>	<u>(726,000)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>2,467,000</u>	<u>2,874,000</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net purchases of marketable securities	(4,374,000)	(443,000)
Purchases of fixed assets	(62,000)	(147,000)
Purchases of other investments	<u>(160,000)</u>	<u>(222,000)</u>
NET CASH USED BY INVESTING ACTIVITIES	<u>(4,596,000)</u>	<u>(812,000)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2,129,000)	2,062,000
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>4,966,000</u>	<u>2,904,000</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 2,837,000</u>	<u>\$ 4,966,000</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR:		
Cash and cash equivalents	\$ 1,525,000	\$ 3,682,000
Restricted cash	<u>1,312,000</u>	<u>1,284,000</u>
Total	<u>\$ 2,837,000</u>	<u>\$ 4,966,000</u>

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

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 1 - ORGANIZATION AND NATURE OF ACTIVITIES

The Health Trust is a California nonprofit public benefit corporation that operates and provides funding for health care services and community health programs, primarily in Santa Clara County. The Health Trust is a tax-exempt entity under Section 501(c)(3) of the Internal Revenue Code.

Prior to January 5, 1996, The Health Trust and various prior affiliates owned and operated an integrated healthcare system, including three hospitals. On that date, The Health Trust and the prior affiliates sold substantially all of their operating assets to Notami Hospitals of California, Inc. (Notami), a wholly owned subsidiary of HCA – The Healthcare Company, for approximately \$165,000,000 in cash. Proceeds from the sale were utilized to decrease and extinguish substantially all of The Health Trust's and the prior affiliates' debt. Subsequent contingencies of the sale are still pending.

Under California charitable trust law, The Health Trust's assets and income derived therefrom must be used consistently with the purposes set forth in The Health Trust's Articles of Incorporation at the time the assets were obtained. After the sale to Notami, The Health Trust engaged in extensive negotiations with the Office of the California Attorney General to define permissible uses of its assets and related income. An agreement was reached and court approved in October 1997. On June 8, 1998, The Health Trust amended its bylaws to reflect a new agreement with the Attorney General with respect to the future use of its assets. The permitted uses defined in the agreement are set forth in Note 12.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Presentation

The Health Trust adopted Statements of Financial Accounting Standards (SFAS) No.116, *Accounting For Contributions Received and Contributions Made*, SFAS No.117, *Financial Statements of Not-for-Profit Organizations*, and SFAS No.136, *Transfer of Assets to a Not-for-Profit Organization That Raises or Holds Contributions for Other*.

- (i) As required by SFAS No. 117, the accompanying financial statements have been prepared to focus on The Health Trust as a whole and to present balances and transactions according to the existence or absence of donor-imposed restrictions. This has been accomplished by classification of fund balances and transactions into the following classes of net assets:

Unrestricted Net Assets - Net assets not subject to donor-imposed stipulations.

Temporarily Restricted Net Assets - Net assets subject to donor-imposed stipulations that may or will be met by actions of The Health Trust and/or the passage of time.

Permanently Restricted Net Assets - Net assets subject to donor-imposed stipulations that they be permanently maintained by The Health Trust.

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(ii) Temporarily Restricted Net Assets

With respect to temporarily restricted net assets, The Health Trust has adopted the following optional accounting policies as permitted by various provisions of SFAS No. 116:

The Health Trust has adopted the provisions of SFAS No. 116 which provide for release from restrictions on temporarily restricted net assets upon the incurrence of an expense when both unrestricted and temporarily restricted net assets are available for that purpose.

Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenue of the temporarily restricted net asset class, and a reclassification to unrestricted net assets is made to reflect the expiration of such restrictions.

(iii) Revenue

Revenue is reported as increases in unrestricted net assets unless uses of the related assets are limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has lapsed) are reported as reclassifications between the applicable classes of net assets.

(iv) Contributions

Contributions, including unconditional promises to give, are recognized in the period received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of the discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contributions receivable is provided based upon management's judgment including such factors as prior collection history, type of contribution and nature of fund-raising activity.

With respect to contribution revenue, The Health Trust has adopted SFAS No. 136, *Transfer of Assets to a Not-for-Profit Organization That Raises or Holds Contributions for Other*.

(b) Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid investments with original maturities of 90 days or less, excluding cash received with a donor-imposed restriction that limits its use to long-term purposes.

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Investments and Investment Income

As required by SFAS No. 124, investments in marketable equity securities are stated at their readily determinable fair value. Unrealized gains and losses on the increase or decrease in fair values are included in the Statement of Activities.

Income and realized net gains on investments of permanently restricted net assets are reported as follows:

- . as increases in permanently restricted net assets if the terms of the gift require that they be added to the principal of a permanent endowment fund;
- . as increases in temporarily restricted net assets if the terms of the gift impose restrictions on the use of income;
- . as increases in unrestricted net assets in all other cases.

(d) Fair Value of Financial Instruments

The fair value of investments in marketable securities is determined using quoted market rates.

The carrying amount of cash and cash equivalents, accounts receivable, prepaids, other current assets, accounts payable, accrued payroll and related liabilities, and other current liabilities approximates fair value due to the short-term maturities of these instruments and obligations.

Management has determined the carrying amount of other investments, and other assets held long-term as well as other long-term liabilities approximates fair values.

(e) Property and Equipment

Property and equipment are recorded at cost. Depreciation is provided over the estimated useful life of the asset and is computed on the straight-line method.

(f) Income Taxes

The Health Trust is a nonprofit organization under Section 501(c)(3) of the Internal Revenue Code, and therefore, is generally exempt from federal and state income taxes.

(g) 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, the disclosure of contingent assets and liabilities at the date of financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(h) Contributed Materials, Equipment and Services

Contributions of property and equipment without donor stipulations concerning the use of such long-lived assets are reported as revenue in the unrestricted net asset class. Contributions of cash or other assets with donor-imposed restrictions to be used to acquire property and equipment are reported as revenue in the temporarily restricted net asset class. The restrictions are considered to be released at the time of acquisition of such long-lived assets.

Contributed materials and equipment are reflected as contributions in the accompanying financial statements at their estimated values at date of receipt.

Contributed services are reflected in the financial statements at the fair value of the services received. The contributions of services are recognized if the services (a) create or enhance non-financial assets or (b) require specialized skills that are provided by individuals possessing those skills and would normally need to be purchased if not provided by donation.

NOTE 3 - INVESTMENTS IN MARKETABLE SECURITIES

Investments are stated at readily determinable fair value, and consist of the following:

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Gain(Loss)</u>
June 30, 2006			
Available for sale:			
Cash Management Fund	\$ 3,572,000	\$ 3,572,000	\$ 0
Large Cap Value Fund	18,632,000	21,071,000	2,439,000
Large Cap Growth Fund	18,028,000	21,453,000	3,425,000
Small Cap Funds	9,817,000	10,546,000	729,000
International Fund	8,248,000	10,952,000	2,704,000
R.E.I.T.	4,293,000	5,802,000	1,509,000
Hedge Fund of Funds	11,330,000	12,119,000	789,000
Fixed Income Fund	<u>30,549,000</u>	<u>29,446,000</u>	<u>(1,103,000)</u>
Total	<u>\$ 104,469,000</u>	<u>\$ 114,961,000</u>	<u>\$ 10,492,000</u>

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Gain (Loss)</u>
June 30, 2005			
Available for sale:			
Cash Management Fund	\$ 1,914,000	\$ 1,914,000	\$ 0
Large Cap Value Fund	20,511,000	22,576,000	2,065,000
Large Cap Growth Fund	18,946,000	22,526,000	3,580,000
Small Cap Funds	10,032,000	10,572,000	540,000
International Fund	8,628,000	10,511,000	1,883,000
R.E.I.T.	4,419,000	5,461,000	1,042,000
Fixed Income Fund	<u>35,646,000</u>	<u>35,806,000</u>	<u>160,000</u>
Total	<u>\$ 100,096,000</u>	<u>\$ 109,366,000</u>	<u>\$ 9,270,000</u>

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 3 - INVESTMENTS IN MARKETABLE SECURITIES (CONTINUED)

Investment activities for the current year:

Unrealized gain in marketable securities as of June 30, 2006	\$ 10,492,000
Unrealized gain in marketable securities as of June 30, 2005	<u>9,270,000</u>
Unrealized gain change in marketable securities during the year	1,222,000
Net realized gain in marketable securities	5,050,000
Net realized/unrealized loss on other investments	<u>135,000</u>
Total net realized/unrealized loss	<u>\$ 6,407,000</u>

NOTE 4 - ACCOUNTS RECEIVABLE

Beginning in fiscal year 2006, Management utilizes the reserve method of accounting for doubtful accounts based on historical experience and Management's evaluation of outstanding accounts receivable at the end of each year. The allowance for doubtful accounts as of June 30, 2006 and 2005 was \$8,000 and \$43,000, respectively.

NOTE 5 - OTHER RECEIVABLES

At June 30, 2006 and 2005, other receivables consist of the following:

	<u>2006</u>	<u>2005</u>
Interest receivable	\$ 47,000	\$ 44,000
Rental receivable	78,000	60,000
Receivable from Columbia	0	300,000
Total	<u>\$ 125,000</u>	<u>\$ 404,000</u>

NOTE 6 - PENSION PLANS

The Health Trust maintains an employee contribution 403(b) savings plan which contains an employer matching 401(a) component. Participants may contribute a percentage of their compensation as defined in the plan agreements. The amount of contribution is matched 50% (up to six percent of an employee's salary) by The Health Trust. The Health Trust has also adopted a 401(a) defined contribution plan where the annual contribution is determined at the discretion of the Board of Trustees. A contribution was approved by The Health Trust as of December 31, 2005 in the amount of 5% of eligible employees' compensation. An accrual equal to 5% of the compensation of eligible employees and the current 50% match for the six months ended June 30, 2006 has been included in other accrued expenses.

The Health Trust also maintains 457(f) deferred compensation plans for three executives. Contribution to the plans are subject to substantial risk of forfeiture and determined by the Board of Trustees each year. As of June 30, 2006 and 2005, balances of these plans in the amount of \$79,000 and \$36,000, are recorded as accrued expenses and restricted cash on the statements of financial position.

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 7 - PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30:

	Depreciable <u>Life</u>	<u>2006</u>	<u>2005</u>
Equipment	5 to 20 years	\$ 1,316,000	\$ 1,254,000
Leasehold improvements	15 years	<u>201,000</u>	<u>201,000</u>
		1,517,000	1,455,000
Less accumulated depreciation and amortization		<u>1,044,000</u>	<u>886,000</u>
Net property and equipment		<u>\$ 473,000</u>	<u>\$ 569,000</u>

NOTE 8 - OTHER ASSETS

The Health Trust is the fiduciary of the retirement accounts for two physicians. Balances of these accounts are reported as restricted cash on the balance sheet and the offset balance is included in accrued expenses due to discontinued operations under long term liabilities. As of June 30, 2006 and 2005, balance of these retirement accounts was \$1,233,000 and \$1,248,000, respectively. Restricted cash also includes balance in 457(f) deferred compensation plans mentioned in Note 6.

In 2001, The Health Trust committed \$1,760,000 to Northgate Capital Group (NCG), a venture capital firm which invests primarily in early stage high tech companies. As of June 30, 2006, The Health Trust has invested \$1,290,000 in NCG. NCG anticipates calling capital quarterly in the range of 2% to 5%. The Health Trust is obligated to invest up to its commitment. As of June 30, 2006 and 2005, the fair market value of this investment was \$1,000,000 and \$869,000, respectively. As of June 30, 2006 and 2005, other investments also include \$729,000 and \$700,000, respectively, of minority ownership in five other entities.

Other assets also include a note receivable of \$800,000 from the sale of real property in 1996. The note is secured by a deed of trust. The note is due October 2008, with an interest rate of 7.5% per year and principal repayment of \$50,000 per year beginning October 2006.

NOTE 9 - DISCONTINUED OPERATIONS

Effective January 5, 1996, The Health Trust and various prior affiliates sold substantially all of their operating assets to Notami, a wholly owned subsidiary of HCA – The Healthcare Company, for approximately \$165,000,000 in cash, adjusted for certain purchase price adjustments, and the assumption of certain liabilities. The revenue and expenses related to the closing out of assets and liabilities associated with the prior business are reflected as discontinued operations in the accompanying Statements of Activities.

Proceeds from the sale of operations were utilized to decrease or extinguish substantially all of The Health Trust's outstanding debt. Subsequent to these transactions, The Health Trust's remaining assets consist primarily of cash and investments and its obligations consist primarily of grants payables, third-party settlements, and payroll and related liabilities. The Health Trust continues to operate and fund community health care programs.

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 10 - GRANTS PAYABLE

Grants payable consist of amounts awarded, but not yet paid, to local nonprofit and public organizations. The amounts are to be paid as follows:

	2006	2005
Payable in less than one year	\$ 2,648,000	\$ 2,364,000
Payable over more than one year	343,000	343,000
	\$ 2,991,000	\$ 2,707,000

NOTE 11 - THE HEALTH TRUST DESIGNATED NET ASSETS

In October 1997, after extensive negotiations with the Office of the California Attorney General (the AG), The Health Trust received court approval for a long-term plan for the use of its assets. On June 8, 1998 The Health Trust amended its by-laws to reflect a new agreement with the AG for an alternative plan for the use of its assets. The amended by-laws established a single board-designated fund.

The board-designated fund of \$92,369,000 and \$89,887,000 on June 30, 2006 and 2005, respectively, is to be used for medically related services and expenditures provided within Santa Clara County and Northern San Benito County by or through a public or not-for-profit tax-exempt hospital. Insurance covering medical services for the medically indigent may also be funded.

The undesignated portion of The Health Trust's net assets are available for The Health Trust's general purposes to promote and enhance the health of the greater Santa Clara County community and totaled \$23,717,000 and \$23,990,000 on June 30, 2006 and 2005, respectively.

Prior year balances of board designated and undesignated funds have been reclassified for comparative purposes to conform to the presentation in the current year financial statements. These reclassifications have no impact on the total net assets.

NOTE 12 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets of \$3,411,000 and \$3,420,000 reported in the accompanying statements of financial position as of June 30, 2006 and 2005, respectively, are available for the following purposes:

	2006	2005
Donor Advised Funds - SJMCF	\$ 1,937,000	\$ 1,914,000
Dental Initiative	820,000	902,000
Faith In Action	21,000	21,000
Family Health Insurance	22,000	45,000
Health Connections	169,000	22,000
Healthy Santa Clara County	4,000	57,000
MindsAlive	66,000	5,000
Meals on Wheels	230,000	70,000
Volunteer related	99,000	99,000
Other purposes	43,000	285,000
Total temporarily restricted net assets	\$ 3,411,000	\$ 3,420,000

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 13 – PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets of \$517,000 and \$344,000 are reported in the accompanying statements of financial position as of June 30, 2006 and 2005, respectively.

NOTE 14 - COMPENSATED ABSENCES

The Health Trust has a combined vacation and sick pay compensation policy. Vacation and sick time is accumulated on the basis of length of service. Benefits may be accrued to a total of twice the annual allowance, at which time no further time is accrued. At June 30, 2006 and 2005, an accrual for this obligation is included in accrued payroll and related liabilities in the amount of \$261,000 and \$173,000, respectively.

NOTE 15 – DONATED SERVICES

Over the last fiscal year, The Health Trust received a significant amount of donated services from unpaid volunteers who contributed over 30,000 hours to support its ongoing programs and general operations. Most of the donated services have not been recognized in the statement of activities since they do not meet the criteria for recognition under SFAS No. 116, Accounting for Contributions Received and Contributions Made.

NOTE 16 - LEASE OBLIGATIONS

The Health Trust is obligated under the following leases:

For premises at 2085 Hamilton Avenue, San Jose, California at a rate of \$20,049 per month. The lease agreement ends on November 30, 2007.

For premises at 1701 South Bascom Avenue, Campbell, California at a rate of \$8,452 per month. The lease agreement ends on November 30, 2007.

For premises at 48A Race St, San Jose, California at a rate of \$1,500 per month. This is a month to month rental agreement.

For the premises at 1252 Park Avenue, San Jose, California at a rate of \$3,846 per month. This is a month to month rental agreement.

The minimum future rent payments under non-cancelable leases having remaining terms in excess of one year as of June 30, 2006, for each year and in the aggregate are:

<u>Fiscal Year</u>	<u>Lease Payment</u>
2007	\$ 406,000
2008	207,000
	<u>\$ 613,000</u>

THE HEALTH TRUST  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2006 AND 2005

NOTE 17 - CONCENTRATION OF CREDIT RISK

As of June 30, 2006 and 2005, and periodically throughout the year, The Health Trust maintained a balance in a bank account in excess of the federally insured limit of \$100,000.

NOTE 18 – SAN JOSE MEDICAL FOUNDATION ADMINSTRATIVE OVERHEAD

In fiscal year 2003, San Jose Medical Center Foundation (SJMCF) contributed most of its assets as donor advised funds to The Health Trust. As part of the agreement, The Health Trust will absorb the overhead expenses of the SJMCF until the foundation is completely dissolved. The overhead expenses are minimal.

NOTE 19 – CITY GRANTS

During the fiscal year ended June 30, 2006, The Health Trust received \$32,157 from City of San Jose to fund “Meals for Low Income Senior Program” and \$13,650 from City of Sunnyvale to fund the “Senior Program - Meals on Wheels”. The funds were spent in accordance to the terms set forth in the contracts.

NOTE 20 - ADMINISTRATIVE SUPPORT

During fiscal 2006, in furtherance of its mission to provide funding and support for health care services and community health programs, The Health Trust began to provide administrative support to School Health Clinics of Santa Clara County, VIA Services, Stroke Awareness, TransAccess and Center for Excellence in Nonprofits, independent California nonprofit corporations exempt from federal income tax pursuant to Section 501(c)(3) of the Internal Revenue Code. The related revenue and expenses are recorded as fee for services revenue and program expenses on the Statement of Activities. Administrative support services are provided at cost.

NOTE 21 – CONFLICT OF INTEREST POLICY

Included among the Organization’s Board of Directors and Officers are volunteers from the community who provide valuable assistance to the Organization in the development of policies and programs and in the evaluation of business transactions. The Organization has adopted a conflict of interest policy whereby Board members are disqualified from participation in the final decision regarding any action affecting their related company or agency.

# BOITANO, SARGENT & LILLY, LLP

## *Certified Public Accountants*

1760 THE ALAMEDA  
SAN JOSE, CALIFORNIA 95126  
TELEPHONE (408) 287-2123

www.bslepa.com  
FAX (408) 294-1856

## *Certified Staff*

CHRIS COLLINS MADRID  
JIMMIE MAGDALENO  
KATHLEEN MATRANGA BENSON  
JAMES C. WAI  
DARRYL WONG  
ANTHIE KARVOUNIS  
CRYSTAL K. HOFER

LOUIS F. BOITANO  
FRANK L. BOITANO  
STEVEN F. BOITANO  
H. OGDEN LILLY

FRANCES V. SARGENT  
(1957-1988)

## REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENTAL AUDITING STANDARDS

To the Board of Trustees  
The Health Trust  
San Jose, California

We have audited the financial statements of The Health Trust as of the year ended June 30, 2006, and have issued our report thereon dated September 30, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### Compliance

As part of obtaining reasonable assurance about whether The Health Trust's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

### Internal Control Over Financial Reporting

In planning and performing our audit, we considered The Health Trust's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level of risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the board of trustees, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

BOITANO, SARGENT & LILLY, LLP

September 30, 2006

THE HEALTH TRUST  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2006

<u>Federal Grantor/Pass-through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Agency or Pass-through Number</u>	<u>Federal Expenditures</u>
U.S. Department of Housing and Human Services: Pass-through from City of San Jose Housing Opportunities for Persons with AIDS	14.241	N/A	\$ 1,050,117
U.S. Department of Health and Human Services: Pass-through from County of Santa Clara HIV Emergency Relief Project and Formula Funding	93.915	99-7504/00-7504	869,119
HIV Care Formula Grants Case management program	93.917	99-85350	316,916
U.S. Department of Health and Human Services: Pass-through from County of Santa Clara Older Americans Act Council on Aging –MOW	93.045	N/A	160,835
U.S. Department of Health and Human Services: Corporation of national and community services	94.013	N/A	8,459
U.S. Department of Agriculture: Pass-through from County of Santa Clara Council on Aging – MOW	93.053	N/A	33,159
			<u>\$ 2,438,605</u>
U.S. Department of Health and Human Services: Pass-through from Council on Aging Diabetes Society Indian Health Center Loaves & Fishes	93.004	N/A	\$ 10,000 10,000 10,000
			<u>\$ 30,000*</u>

\* These grants were not recorded as revenue or program expenditures and were directly passed to beneficiaries.

See accompanying notes.

THE HEALTH TRUST  
NOTES TO SCHEDULE OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2006

NOTE 1 – ORGANIZATION AND NATURE OF ACTIVITIES

The Health Trust is a nonprofit corporation organized to financially support and operate certain health care programs in Santa Clara County, State of California. The programs operated by The Health Trust that receive federal financial support are as follows:

- Health Connections – AIDS Services
- Meals on Wheels

NOTE 2 - GENERAL

The accompanying schedule of expenditures of federal awards (the schedule) presents the activity of all federal award programs of The Health Trust for the year ended June 30, 2006. Federal awards received directly from federal agencies, as well as federal awards passed through other agencies, are included in the schedule.

NOTE 3 –BASIS OF ACCOUNTING – SCHEDULE OF FEDERAL AWARDS

The schedule has been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles for the year ended June 30, 2006.

# BOITANO, SARGENT & LILLY, LLP

*Certified Public Accountants*

1760 THE ALAMEDA  
SAN JOSE, CALIFORNIA 95126  
TELEPHONE (408) 287-2123

www.bsllcpa.com  
FAX (408) 294-1856

LOUIS F. BOITANO  
FRANK L. BOITANO  
STEVEN F. BOITANO  
H. OGDEN LILLY

FRANCES V. SARGENT  
(1957-1988)

*Certified Staff*

CHRIS COLLINS MADRID  
JIMMIE MAGDALENO  
KATHLEEN MATRANGA BENSON  
JAMES C. WAI  
DARRYL WONG  
ANTHIE KARVOUNIS  
CRYSTAL K. HOFER

## REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Trustees  
The Health Trust  
San Jose, California

### Compliance

We have audited the compliance of The Health Trust with the types of compliance requirements described in the *U.S. Office of Management and Budget OMB circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2006. The Health Trust's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of The Health Trust's management. Our responsibility is to express an opinion on The Health Trust's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about The Health Trust's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on The Health Trust's compliance with those requirements.

In our opinion, The Health Trust complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2006. The results of our auditing procedures disclosed no instances of material noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133.

### Internal Control Over Compliance

The management of The Health Trust is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered The Health Trust's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level of risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the board of trustees, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

BOITANO, SARGENT AND LILLY, LLP

September 30, 2006

THE HEALTH TRUST  
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
 FOR THE YEAR ENDED JUNE 30, 2006

A. SUMMARY OF AUDIT RESULTS

1. The auditors' report expresses an unqualified opinion on the financial statements of The Health Trust.
2. No reportable conditions relating to the audit of the financial statements were reported in the Unqualified Opinion on Financial Statements and Supplementary Schedule of Expenditures of Federal Awards.
3. No instances of noncompliance material to the financial statements of The Health Trust were disclosed during the audit.
4. No reportable conditions relating to the audit of the major federal award programs are reported in the Report on Compliance with Requirements Applicable to each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133.
5. The auditors' report on compliance for the major federal award programs for The Health Trust expresses an unqualified opinion.
6. No audit findings disclosed are required to be reported in accordance with Section 510 (a) of Circular A-133.
7. The programs tested as major programs include:

<u>Title</u>	<u>FEDERAL CFDA Number</u>
Housing Opportunities for Persons with AIDS	14.241
HIV Care Formula Grants Case Management Program	93.917

8. The threshold for distinguishing Types A and B programs was \$300,000.
9. The Health Trust was determined to be a low-risk auditee.

THE HEALTH TRUST  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2006

B. FINDINGS - FINANCIAL STATEMENTS AUDIT

None

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD  
PROGRAMS AUDIT

None

THE HEALTH TRUST  
SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2006

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

No prior audit findings