

THE HEALTH TRUST

FINANCIAL STATEMENTS
WITH SUPPLEMENTAL INFORMATION

JUNE 30, 2005 AND 2004

(With Independent Auditors' Report Thereon)

Table of Contents

	<u>Page</u>
Independent Auditors' Report	1
Statements of Financial Position as of June 30, 2005 and 2004	3
Statements of Activities for the years ended June 30, 2005 and 2004	5
Statements of Functional Expenses for the years ended June 30, 2005 and 2004	6
Statements of Cash Flows for the years ended June 30, 2005 and 2004	8
Notes to Financial Statements as of June 30, 2005 and 2004	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	19
Schedule of Expenditures of Federal Awards for the year ended June 30, 2005	21
Notes to Schedule of Federal Awards for the year ended June 30, 2005	22
Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133	23
Schedule of Findings and Questioned Costs	25
Schedule of Prior Audit Findings	27

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
MARIA ANGELIDES
CRYSTAL K. HOFER

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, 2005 and 2004, 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 audit 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 audit 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, 2005 and 2004, and the changes in its net assets 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, 2005 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, 2005

THE HEALTH TRUST
STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2005 AND 2004

ASSETS

	<u>2005</u>	<u>2004</u>
CURRENT ASSETS:		
Cash and cash equivalents	\$ 3,682,000	\$ 1,701,000
Investment in marketable securities	109,366,000	111,025,000
Accounts receivable	2,110,000	1,932,000
Other receivables	404,000	66,000
Prepays	<u>216,000</u>	<u>204,000</u>
Total current assets	<u>115,778,000</u>	<u>114,928,000</u>
 PROPERTY AND EQUIPMENT, net of accumulated depreciation of \$1,066,000 and \$930,000, respectively	 <u>4,392,000</u>	 <u>4,438,000</u>
 OTHER ASSETS:		
Restricted cash	1,284,000	1,203,000
Other investments	1,569,000	1,348,000
Note receivable	<u>800,000</u>	<u>800,000</u>
Total other assets	<u>3,653,000</u>	<u>3,351,000</u>
 TOTAL ASSETS	 <u>\$ 123,823,000</u>	 <u>\$ 122,717,000</u>

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

THE HEALTH TRUST
STATEMENTS OF FINANCIAL POSITION (CONTINUED)
JUNE 30, 2005 AND 2004

LIABILITIES AND NET ASSETS

	<u>2005</u>	<u>2004</u>
CURRENT LIABILITIES:		
Accounts payable	\$ 543,000	\$ 474,000
Accrued payroll and related liabilities	587,000	636,000
Accrued expenses due to discontinued operations	68,000	116,000
Accrued expenses	162,000	323,000
Grants payable	<u>2,364,000</u>	<u>3,090,000</u>
Total current liabilities	<u>3,724,000</u>	<u>4,639,000</u>
 LONG-TERM LIABILITIES:		
Grants payable	343,000	343,000
Estimated third-party settlements - net	0	1,066,000
Accrued expenses due to discontinued operations	<u>2,115,000</u>	<u>2,070,000</u>
Total long-term liabilities	<u>2,458,000</u>	<u>3,479,000</u>
 TOTAL LIABILITIES	 <u>6,182,000</u>	 <u>8,118,000</u>
 NET ASSETS:		
Unrestricted net assets:		
Designated by the Board of Trustees for medically related services and expenditures	87,070,000	86,862,000
Undesignated	<u>26,807,000</u>	<u>24,294,000</u>
Total unrestricted net assets	113,877,000	111,156,000
Temporarily restricted net assets	3,420,000	3,132,000
Permanently restricted net assets	<u>344,000</u>	<u>311,000</u>
Total net assets	<u>117,641,000</u>	<u>114,599,000</u>
 TOTAL LIABILITIES AND NET ASSETS	 <u>\$ 123,823,000</u>	 <u>\$ 122,717,000</u>

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

THE HEALTH TRUST
STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>2004</u>
CHANGES IN UNRESTRICTED NET ASSETS:		
Support:		
Contributions	\$ 194,000	\$ 110,000
United Way of Santa Clara County	128,000	151,000
Government grants	3,355,000	3,745,000
In kind contribution	<u>457,000</u>	<u>265,000</u>
Total support	<u>4,134,000</u>	<u>4,271,000</u>
Revenue:		
Fee for services	1,021,000	1,685,000
Investment income, net of investment expenses of \$629,000 and \$714,000, respectively	2,643,000	2,278,000
Net realized/unrealized gain	<u>5,607,000</u>	<u>12,828,000</u>
Total revenue	<u>9,271,000</u>	<u>16,791,000</u>
Net assets released from restrictions	<u>1,468,000</u>	<u>1,868,000</u>
Total support and revenue	<u>14,873,000</u>	<u>22,930,000</u>
Expenses:		
Program services	<u>11,964,000</u>	<u>12,562,000</u>
Support services:		
Management and general	1,361,000	1,060,000
Fundraising	<u>761,000</u>	<u>535,000</u>
Total support services	<u>2,122,000</u>	<u>1,595,000</u>
Total expenses	<u>14,086,000</u>	<u>14,157,000</u>
Operating gain	787,000	8,773,000
Gain from discontinued operations	<u>1,933,000</u>	<u>445,000</u>
Increase in unrestricted net assets	<u>2,720,000</u>	<u>9,218,000</u>
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS:		
Contributions	1,583,000	1,555,000
Government grants	20,000	5,000
Investment income, net of investment expenses of \$21,000 and \$20,000, respectively	154,000	264,000
Net assets released from restrictions	<u>(1,468,000)</u>	<u>(1,868,000)</u>
Increase (decrease) in temporarily restricted net assets	<u>289,000</u>	<u>(44,000)</u>
CHANGES IN PERMANENTLY RESTRICTED NET ASSETS:		
Contributions	<u>33,000</u>	<u>11,000</u>
Increase in permanently restricted net assets	<u>33,000</u>	<u>11,000</u>
Increase in net assets	3,042,000	9,185,000
NET ASSETS AT BEGINNING OF YEAR	<u>114,599,000</u>	<u>105,414,000</u>
NET ASSETS AT END OF YEAR	<u>\$ 117,641,000</u>	<u>\$ 114,599,000</u>

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

THE HEALTH TRUST
STATEMENTS 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 FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2004

	2004			
	Program Services	Management and General	Fund Raising	Total Expenses
Allocation to agencies	\$ 4,406,000	\$ 0	\$ 0	\$ 4,406,000
Salaries and related expenses				
Salaries and wages	3,056,000	379,000	235,000	3,670,000
Contracted services	34,000	16,000	0	50,000
Payroll taxes	244,000	30,000	21,000	295,000
Employee benefits	879,000	147,000	79,000	1,105,000
Total salaries and related expenses	4,213,000	572,000	335,000	5,120,000
Services and supplies				
Purchased services	1,823,000	24,000	12,000	1,859,000
Professional fees	188,000	127,000	0	315,000
Supplies	803,000	32,000	79,000	914,000
Building and equipment rental	402,000	98,000	53,000	553,000
Utilities	111,000	12,000	8,000	131,000
Insurance	68,000	89,000	0	157,000
Travel	125,000	16,000	8,000	149,000
Advertising	12,000	6,000	1,000	19,000
Training	16,000	4,000	7,000	27,000
Dues and subscriptions	2,000	7,000	3,000	12,000
Depreciation	113,000	22,000	8,000	143,000
Other expenses	280,000	51,000	21,000	352,000
Total services and supplies	3,943,000	488,000	200,000	4,631,000
 Total expenses	 \$ 12,562,000	 \$ 1,060,000	 \$ 535,000	 \$ 14,157,000

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

THE HEALTH TRUST
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 3,042,000	\$ 9,185,000
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	193,000	191,000
Loss on sale of assets	0	13,000
Unrealized (gain) loss on investment	2,101,000	(9,117,000)
Decrease (increase) in:		
Accounts receivable	(432,000)	(589,000)
Other receivables and prepaids	(94,000)	(195,000)
Increase (decrease) in:		
Accounts payable and other accrued expenses	(91,000)	46,000
Accrued payroll and related liabilities	(49,000)	(21,000)
Accrued expenses due to discontinued operations	(4,000)	258,000
Estimated third party settlements	(1,066,000)	(2,046,000)
Grants payable	(726,000)	19,000
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>2,874,000</u>	<u>(2,256,000)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of fixed assets	(147,000)	(105,000)
Purchases of other investments	(222,000)	(311,000)
Net sales (purchases) of marketable securities	<u>(443,000)</u>	<u>3,217,000</u>
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	<u>(812,000)</u>	<u>2,801,000</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	2,062,000	545,000
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>2,904,000</u>	<u>2,359,000</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 4,966,000</u>	<u>\$ 2,904,000</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR:		
Cash and cash equivalents	\$ 3,682,000	\$ 1,701,000
Restricted cash	1,284,000	1,203,000
Total	<u>\$ 4,966,000</u>	<u>\$ 2,904,000</u>

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

THE HEALTH TRUST
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005 AND 2004

NOTE 1 - ORGANIZATION AND BUSINESS

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, 2005 AND 2004

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 debt instruments 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, 2005 AND 2004

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. 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) Estimated Third-Party Settlements

Estimated third-party settlements are reported as the net payable/receivable amounts due to or from the various government programs in accordance with the applicable program regulations. Prior period adjustments were accrued on an estimated basis in the period in which the related services were rendered and are adjusted in future periods as final settlements are determined (Note 11). Adjustments to the estimated settlements are recorded against discontinued operations.

(g) 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.

THE HEALTH TRUST
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005 AND 2004

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 of 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 of 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.

(i) 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.

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</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, 2005 AND 2004

NOTE 3 - INVESTMENTS IN MARKETABLE SECURITIES (CONTINUED)

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Gain (Loss)</u>
June 30, 2004			
Available for sale:			
Cash Management Fund	\$ 1,719,000	\$ 1,719,000	\$ 0
Large Cap Value Fund	20,770,000	24,196,000	3,426,000
Large Cap Growth Fund	20,796,000	24,004,000	3,208,000
Small Cap Funds	7,542,000	10,998,000	3,456,000
International Fund	9,508,000	10,924,000	1,416,000
R.E.I.T.	2,759,000	2,935,000	176,000
Fixed Income Fund	<u>36,560,000</u>	<u>36,249,000</u>	<u>(311,000)</u>
Total	<u>\$ 99,654,000</u>	<u>\$ 111,025,000</u>	<u>\$ 11,371,000</u>

Investment activities for the current year:

Unrealized gain in marketable securities as of June 30, 2005	\$ 9,270,000
Unrealized gain in marketable securities as of June 30, 2004	<u>11,371,000</u>
Unrealized loss change in marketable securities during the year	(2,101,000)
Net realized gain in marketable securities	7,716,000
Net realized/unrealized loss on other investments	<u>(8,000)</u>
Total net realized/unrealized loss	<u>\$ 5,607,000</u>

NOTE 4 - ACCOUNTS RECEIVABLE

Beginning in fiscal year 2005, 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, 2005 and 2004 was \$37,000 and \$43,000, respectively.

NOTE 5 - OTHER RECEIVABLES

At June 30, 2005 and 2004, other receivables consist of the following:

	<u>2005</u>	<u>2004</u>
Interest receivable	\$ 44,000	\$ 42,000
Rental receivable	60,000	24,000
Receivable from Columbia	<u>300,000</u>	<u>0</u>
Total	<u>\$ 404,000</u>	<u>\$ 66,000</u>

THE HEALTH TRUST
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005 AND 2004

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, 2004 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, 2005 has been included in other accrued expenses.

During fiscal year 2005, The Health Trust created 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, 2005, balances of these plans in the amount of \$36,000, are recorded as accrued expenses and restricted cash on the statements of financial position.

NOTE 7 - PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30:

	Depreciable Life	<u>2005</u>	<u>2004</u>
Land and land improvements*		\$ 4,003,000	\$ 4,003,000
Equipment	5 to 20 years	1,254,000	1,172,000
Leasehold improvements	15 years	<u>201,000</u>	<u>193,000</u>
		5,458,000	5,368,000
Less accumulated depreciation and amortization		<u>1,066,000</u>	<u>930,000</u>
Net property and equipment		<u>\$ 4,392,000</u>	<u>\$ 4,438,000</u>

* Held for investment, not used in operations.

NOTE 8 - OTHER ASSETS

Other assets 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.

THE HEALTH TRUST
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2005 AND 2004

NOTE 9 - DISCONTINUED OPERATIONS (CONTINUED)

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.

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:

	2005	2004
Payable in less than one year	\$ 2,364,000	\$ 3,090,000
Payable over more than one year	343,000	343,000
	\$ 2,707,000	\$ 3,433,000

NOTE 11 - ESTIMATED THIRD-PARTY SETTLEMENTS

The three hospitals formerly operated by The Health Trust, Good Samaritan Hospital (GSH), San Jose Medical Center (SJMC), and South Valley Hospital (SVH) (collectively, the Hospitals) were reimbursed for services provided to Medicare and Medi-Cal program patients based on various reimbursement methodologies. Inpatient acute care services provided to Medicare program patients were paid at prospectively determined rates per discharge. Inpatient non-acute services, certain outpatient services and medical education costs for Medicare program patients were paid at a tentative rate under cost reimbursement methodologies. Inpatient services rendered to Medi-Cal program patients were reimbursed at a tentative rate under a cost reimbursement methodology for GSH (until December 1994) and SVH. GSH (beginning December 1994) and SJMC were reimbursed for inpatient services provided to Medi-Cal program patients at a negotiated rate per day.

The final amount of reimbursement from the Medicare and Medi-Cal programs is not determined until after submission of annual cost reports by The Health Trust and audits thereof by the fiscal intermediaries (Final Settlement). Cost reports have been audited by the fiscal intermediaries through January 4, 1996. Final Settlement does not prevent The Health Trust from appealing, nor the fiscal intermediary from reopening, specific reimbursement determinations.

During fiscal year ended June 30, 2005, The Health Trust has settled all cases with Medicare and Medi-Cal Programs. No reserve was made as June 30, 2005. Since the amount reserved is our best estimate as of the end of the fiscal year, this amount is subject to change. Changes for the current year are summarized as follows:

Net beginning balance as of June 30, 2004	\$ 1,066,000
Net settlement	759,000
Less transferred to discontinued operations	(1,825,000)
Net ending balance as of June 30, 2005	\$ 0

THE HEALTH TRUST
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005 AND 2004

NOTE 12 - 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 \$87,070,000 and \$86,862,000 on June 30, 2005 and 2004, 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 \$26,807,000 and \$24,294,000 on June 30, 2005 and 2004, respectively.

Beginning July 1, 2004, income and expenses generated from discontinued operations will be allocated proportionally between the board designated fund and the undesignated fund.

NOTE 13 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets of \$3,420,000 and \$3,132,000 reported in the accompanying statements of financial position as of June 30, 2005 and 2004, respectively, are available for specific health programs.

NOTE 14 – PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets of \$344,000 and \$311,000 are reported in the accompanying statements of financial position as of June 30, 2005 and 2004, respectively.

NOTE 15 - CONTINGENT LIABILITIES

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, 2005, The Health Trust has invested \$1,126,000 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.

NOTE 16 - 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, 2005 and 2004, an accrual for this obligation is included in accrued payroll and related liabilities in the amount of \$173,000 and \$136,000, respectively.

THE HEALTH TRUST
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005 AND 2004

NOTE 17 - CONCENTRATION OF CREDIT RISK

As of June 30, 2005 and 2004, 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 - 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 \$11,067 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 \$3,468 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, 2005, for each year and in the aggregate are:

<u>Fiscal Year</u>	<u>Lease Payment</u>
2006	\$ 373,000
2007	373,000
2008	145,000
	<u>\$ 891,000</u>

NOTE 19 – 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 20 – SAN JOSE MEDICAL FOUNDATION ADMINISTRATIVE 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.

THE HEALTH TRUST
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005 AND 2004

NOTE 21 – CITY GRANTS

During the fiscal year ended June 30, 2005, the Health Trust received \$40,485 from City of San Jose to fund “Meals for Low Income Senior Program” and \$12,113 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 22 - ADMINISTRATIVE SUPPORT

During fiscal 2005, 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 and Stroke Awareness, 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 service revenue and program expenses on the Statement of Activities, and are done at or below cost.

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
MARIA ANGELIDES
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, 2005, and have issued our report thereon dated September 30, 2005. 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, 2005

THE HEALTH TRUST
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2005

<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	\$ 1,019,484
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	940,155
HIV Care Formula Grants	93.917	99-85350	328,768
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	51,100
U.S. Department of Agriculture Pass-through from County of Santa Clara Council on Aging – MOW	97.024	N/A	9,554
U.S. Department of Agriculture: Pass-through from County of Santa Clara Council on Aging – MOW	93.045	N/A	28,563
			<u>\$ 2,377,624</u>
U.S. Department of Health and Human Services: Pass-through from Council on Aging Santa Clara County Blind Center RotaCare Bay Area Books Aloud Northern Californian Presbyterian Homes and Services	93.004	N/A	\$ 10,000 10,000 10,000 10,000
			<u>\$ 40,000*</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, 2005

NOTE 1 – ORGANIZATION AND BUSINESS

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, 2005. 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, 2005.

BOITANO, SARGENT & LILLY, LLP

Certified Public Accountants

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

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

Certified Staff

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

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

FRANCES V. SARGENT
(1957-1988)

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, 2005. 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, 2005. 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, 2005

THE HEALTH TRUST
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 FOR THE YEAR ENDED JUNE 30, 2005

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>CFDA Number</u>
Housing Opportunities for Persons with AIDS	14.241
HIV Emergency Relief Project Formula Grant – Ryan White Title I	93.915

8. The threshold for distinguishing Types A and B programs was \$500,000.
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, 2005

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, 2005

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

No prior audit findings