Report of Independent Auditors and
Financial Statements with Supplemental Information

West Contra Costa Healthcare District

December 31, 2011 and 2010

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

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CONTENTS

MANAGEMENT DISCUSSION AND ANALYSIS

Our discussion and analysis of West Contra Costa County Healthcare District's (the "District") financial performance provides an overview of the District's financial activities for the fiscal years ended December 31, 2011, 2010, and 2009. Please read it in conjunction with the District's financial statements, which begin on page 7.

Financial Highlights

- The District's net assets decreased in 2011 from 2010 by $18.7 million (65.9%) after an increase in 2010 from 2009 by $2.5 million (9.8%) and an increase in 2009 from 2008 of $11.0 million (74.6%).
- The District reported an operating loss of $31.2 million in 2011 after operating losses of $15.5 million in 2010 and $13.2 million in 2009.
- The District's net nonoperating revenues were $12.4 million in 2011 as compared to $18.0 million in 2010 and $24.3 million in 2009.

Using This Annual Report

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

The Balance Sheet and Statement of Revenues, Expenses, and Changes in Net Assets

Our analysis of the District's finances begins on page 1. One of the most important questions asked about the finances is, "Is the District as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses, and changes in net assets report information about the District's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the District's net assets and changes in them. You can think of the District's net assets – the difference between assets and liabilities – as one way to measure the District's financial health, or financial position. Over time, increases or decreases in the District's assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the District's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the District. Overall, the District is worse off at December 31, 2011 than it was December 31, 2010.

The Statement of Cash Flows

The final required statement is the statement of cash flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It provides answers to such questions as "Where did cash come from?" "What was cash used for?" and "What was the change in cash balance during the reporting period?"

The District's Net Assets

The District's net assets are the difference between its assets and liabilities reported in the balance sheets on page 7. The net assets decreased in 2011 by $18.7 million over 2010 after an increase in 2010 by $2.5 million over 2009 and an increase in 2009 by $11.0 million over 2008.

Table 1: Assets, Liabilities, and Net Assets

	2011	2010	2009
Assets			
Current assets	$ 67,264,000	$ 37,105,000	$ 39,577,000
Capital assets, net	44,782,000	45,407,000	44,033,000
Other noncurrent assets	1,992,000	1,186,000	1,228,000
Total assets	$ 114,038,000	$ 83,698,000	$ 84,838,000
Liabilities			
Current liabilities	$ 35,514,000	$ 32,316,000	$ 31,906,000
Other	68,852,000	22,982,000	27,077,000
Total liabilities	104,366,000	55,298,000	58,983,000
Net Assets (deficit)			
Invested in capital assets, net of related debt	8,380,000	21,890,000	18,667,000
Restricted expendable net assets	2,829,000	4,006,000	4,435,000
Unrestricted	(1,537,000)	2,504,000	2,753,000
Total net assets (deficit)	9,672,000	28,400,000	25,855,000
Total net assets and liabilities	$ 114,038,000	$ 83,698,000	$ 84,838,000

Net patient service revenue decreased in 2011 from 2010 by $13.8 million (-10.6%), while operating expenses increased by $2.0 million (1.3%). The two significant changes in the financial position of the District was an increase in operating cash due to the issuance of a $40 million COP bond in December 2011 and a $10 million borrowing from Contra Costa County. Both the borrowings had the impact of increasing cash and increasing long term debt. The District also was able to lower the other long term debt by making the scheduled payments on the bond, certificates of participation, and pay off the original Contra Costa County tax advance. During 2011, the District was advanced $17.3 million on their revolving line of credit, backed by accounts receivables of which $13.9 million was paid back by the end of the year. This loan was necessary as a cash bridge prior to the borrowing of the $40 million bond.

In 2011, the District also paid down its long term debt by $5.6 million, including the final $1.8 million payment on the District's bankruptcy debt. The balance of the long term debt payments were to Contra Costa County and for the District's bonds. The estimates from third party settlements decreased in 2011. This was the result of a component of the Medicare payment calculation being updated. This caused management to revise Medicare cost report estimates back to 2007 cost reports. This was reflected in the 2011 balances only.

The District's operating loss increased by $15.7 million from 2010 to 2011. Management's 2011 operating budget was established to reduce the operating loss by 2012 to a level that is fully supported by only the property tax revenue. That goal was not achieved due to changes in payor mix and a significant loss in non-operating revenues that will be explained below. There was also significant turnover in executive level management during 2010 and 2011.

In 2011, the District reported an operating loss of $31.2 million. The increase in the District's operating loss was directly related to the District's change in payor mix and continued loss of outside funding from other sources. The District has experienced losses in managed care revenue and increases in Medi-Cal and patients without insurance. The District believes that this shift is directly related to the economic conditions. These losses are partially offset by the California Hospital Tax. The District received $1.6 million in 2011. This amount is reported in net patient service revenue.

The new interim management team started developing a turnaround plan for the District in May of 2011. In August 2011, a reduction in force was implemented with 33 FTE's eliminated saving the hospital $2.5 million annually. During the 2012 budget process, additional cuts were made to expenses bringing the total annual savings to $5.5 million. In November, a new parcel tax was passed by the voters in the district that will create $5.1 million of additional annual tax income. The district also secured $40 million from a bond measure in December which gives the hospital funds to operate for approximately 5 years while a complete strategic plan is developed. By incorporating the changes made to operations, the loss run rate will have been cut to an $8.1 million loss in 2012 and with a full year effect of $5.5 million when compensating for the full year effect of the new parcel tax.

Net patient service revenue increased in 2010 from 2009 by $7.6 million (6.2%), while operating expenses increased by $9.8 million (7.2%). The significant change in the financial position of the District was a decrease in operating cash caused by not receiving the anticipated CMAC payment discussed below. Not receiving this $8.0 million payment caused the District to delay payment to vendors and to cancel or put on hold anticipated capital projects. The District was able to lower the long term debt by making the scheduled payments on the bond, certificates of participation, and Contra Costa County tax advance.

In 2010, the District also paid down its long term debt by $7.0 million, including a $3.2 million payment on the District's bankruptcy debt. The balance of the long term debt payments were to Contra Costa County and for the District's bonds. The estimates from third party settlements decreased in 2010. This was the result of a component of the Medicare payment calculation being updated. This caused management to revise Medicare cost report estimates back to 2007 cost reports. This was reflected in the 2010 balances only.

The District's operating loss increased by $2.2 million from 2009 to 2010. The District's property tax revenue was approved by the residents to supplement operations. Management's 2010 operating budget was established to reduce the operating loss by 2011 to a level that is fully supported by only the property tax revenue. That goal was not achieved due to changes in payor mix and a significant loss in nonoperating revenues that will be explained below. There was also significant turnover in executive level management during 2010 and in January 2011. The new management team is currently developing a turnaround plan for the District.

In 2010, the District reported an operating loss of $15.5 million. The increase in the District's operating loss was directly related to the District's change in payor mix. The District has experienced losses in managed care revenue and increases in Medi-Cal and patients without insurance. The District believes that this shift is directly related to the economic conditions. The District also had higher inpatient lengths of stay than anticipated in the first half of 2010. Management put processes in place to better manage patients' length of stay to more medically appropriate stays. These were practically offset by the implementation of the California Hospital Tax. The District received $1.4 million in 2010. This amount is reported in net patient service revenue.

In the District's 2010 operating budget, there was an anticipated receipt of $12.0 million in Federal Matching Funding. The District anticipated three $4.0 million payments; the first in March, second in August and the third in December. In September, the District was notified that the second and third payments would not be received. The loss of the anticipated $8.0 million has caused significant cash flow issues and accelerated the District's strained financial condition caused by the payor mix shift as discussed above.

Net patient service revenue increased in 2009 by $6.5 million (5.5%), patient accounts receivable, net of estimated uncollectible amounts, increased by $7.2 million (60.4%) in 2009. The increase in accounts receivable from 2008 to 2009 is due to several factors. At December 2008, the gross accounts receivable had a large amount of aged self pay accounts and accounts older than 151 days. The self pay accounts were 100% reserved as uncollectable. During 2009, management put a significant amount of effort in resolving the self pay and 151 days plus accounts. The self pay accounts receivable was reduced during 2009 from a high of $33.2 million to a December 31, 2009 balance of $9.4 million (70.6%). Accounts older than 151 days were reduced from a high of $56.4 million to $21.2 million at December 31, 2009 (61.5%). The cash collections goal on patient accounts for 2009 was $114.0 million. The actual cash collections were $117.0 million or $3.0 million over the goal. The net accounts receivable increased by $10.5 million from 2008 to 2009. This increase is the result of decreases in gross accounts receivable from 2008 to 2009 by $54.5 million due to improvements in the age of accounts and the decrease in self pay accounts.

In 2009, the District also paid down its long term debt by $10.4 million, including a $3.4 million payment on the District's bankruptcy debt. The balance of the long term debt payments were to Contra Costa County and for the District's bonds. The estimates from third party settlements increased in 2009. This was the result of a component of the Medicare payment calculation being updated. This caused management to revise Medicare cost report estimates back to 2007 cost reports. This was reflected in the 2009 balances only.

The primary reasons for the decrease in operating income from 2010 to 2011 are:

- Decrease in CMAC funding.
- Decrease in length of stay for payers that reimburse based on days in the hospital.
- Decrease in managed care revenue due to a payor mix shift from managed care payor to Medi-Cal and self pay.
- Increase in benefit costs in employee medical insurance plan.

The primary reasons for the decrease in operating income from 2009 to 2010 are:

- Decrease in CMAC funding.
- Decrease in managed care revenue due to a payor mix shift from managed care payor to Medi-Cal and self pay.
- Increase in salaries due to increased inpatient lengths of stay related to a higher portion of non surgical medicine patients than in prior years.
- Increases in supply costs that were related to higher surgical volumes for joint replacement and other major implant surgeries.

Table 2: Operating Results and Changes in Net Assets

	2011	2010	2009
Operating revenues			
Net patient service revenue	$ 116,419,000	$ 130,185,000	$ 122,576,000
Other operating revenue	1,166,000	1,130,000	1,149,000
Total operating revenues	117,585,000	131,315,000	123,725,000
Operating expenses			
Salaries and benefits	96,749,000	95,529,000	92,915,000
Supplies	18,777,000	20,928,000	18,275,000
Depreciation and amortization	4,165,000	3,593,000	3,511,000
Other operating expenses	29,056,000	26,721,000	22,251,000
Total operating expenses	148,747,000	146,771,000	136,952,000
Operating loss	(31,162,000)	(15,456,000)	(13,227,000)
Nonoperating revenues (expenses):			
District tax revenue	8,498,000	8,492,000	8,591,000
Investment income	46,000	92,000	198,000
Noncapital grants and contributions	5,443,000	10,813,000	17,000,000
Interest expense	(1,553,000)	(1,396,000)	(1,514,000)
Total net nonoperating revenues	12,434,000	18,001,000	24,275,000
(Deficit) Excess of revenues over expenses	(18,728,000)	2,545,000	11,048,000
Increase in net assets	(18,728,000)	2,545,000	11,048,000
Net assets at beginning of the year	28,400,000	25,855,000	14,807,000
Net assets at end of the year	$ 9,672,000	$ 28,400,000	$ 25,855,000

The District sometimes provides care for patients who have little or no health insurance or other means of repayment. As discussed, this service to the community is consistent with the goals established for the District when it was founded. Because there is no expectation of repayment, charity care is not reported as patient service revenues of the District. The cost of providing care to the uninsured patients was approximately $6.9 million in 2011 and $3.6 million in 2010. The majority of charity care amounts written off in 2009 aggregated roughly $46,649,000 of which $23,663,000 is related to charity care accounts from prior years. In 2009, management performed a detailed review of prior year accounts to determine if these accounts met the criteria in the District's charity care policy even though these accounts were previously included in their allowance for doubtful accounts. Because these accounts were included in the allowance for doubtful accounts in previous years, there was no income effect of writing the amounts off as charity care in 2009. The amount of charges foregone for services and supplies furnished under the District's charity care policy aggregated approximately $6,940,000 and $6,658,000 in 2011 and 2010, respectively.

Nonoperating Revenues and Expenses

Nonoperating revenues consist primarily of property taxes levied by the District, noncapital grants and contributions, interest revenue, and investment earnings. The change in non-operating revenues was discussed above.

The District's Cash Flows

Changes in the District's cash flows are consistent with changes in operating losses and nonoperating revenues and expenses, discussed earlier.

Capital Assets

At the end of 2011, the District had $44.8 million invested in capital assets, net of accumulated depreciation, as detailed in Note 8 to the financial statements. In 2011, the District purchased new equipment costing $3.9 million.

At the end of 2010, the District had $45.4 million invested in capital assets, net of accumulated depreciation, as detailed in Note 8 to the financial statements. In 2010, the District purchased new equipment costing $4.9 million.

At the end of 2009, the District had $44.0 million invested in capital assets, net of accumulated depreciation, as detailed in Note 8 to the financial statements. In 2009, the District purchased new equipment costing $4.1 million.

Contacting the District's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Chief Financial Officer's office at Doctors Medical Center, 2000 Vale Road, San Pablo, CA 94806.

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors
West Contra Costa Healthcare District

We have audited the accompanying balance sheets of West Contra Costa Healthcare District (the "District") as of December 31, 2011 and 2010, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform our audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. An audit 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 provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 1 through 5 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. This schedule is the responsibility of the District's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

The accompanying Required Supplementary Information - Pension on page 26 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. This schedule is the responsibility of the District's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit such information and we do not express an opinion on it.

Moss Adams LLP

San Francisco, California
March 29, 2012

FINANCIAL STATEMENTS

		2011		2010
ASSETS				
Current assets				
Cash and cash equivalents	$	13,972,000	$	5,229,000
Patient accounts receivable, net of estimated uncollectibles of $12,105,000 and $7,092,000 at 2011 and 2010, respectively		19,177,000		19,942,000
Other receivables		1,160,000		4,055,000
Current portion of board designated and trusteed assets		29,847,000		4,006,000
Supplies		2,109,000		2,252,000
Prepaid expenses and deposits		999,000		1,621,000
Total current assets		67,264,000		37,105,000
Board designated and trusteed assets, net of current portion		642,000		642,000
Capital assets, net of accumulated depreciation		44,782,000		45,407,000
Other assets		1,350,000		544,000
Total assets	$	114,038,000	$	83,698,000
LIABILITIES AND NET ASSETS				
Current liabilities				
Current maturities of debt borrowings	$	4,979,000	$	3,646,000
Accounts payable and accrued expenses		12,675,000		14,012,000
Accrued payroll and related liabilities		13,640,000		11,356,000
Other current liabilities		2,880,000		801,000
Estimated third-party payor settlements		1,340,000		2,501,000
Total current liabilities		35,514,000		32,316,000
Debt borrowings, net of current maturities		62,747,000		22,982,000
Other long-term liabilities		6,105,000		-
Total liabilities		104,366,000		55,298,000
Net assets				
Invested in capital assets, net of related debt		21,312,000		21,890,000
Restricted expendable		2,829,000		4,006,000
Unrestricted		(14,469,000)		2,504,000
Total net assets		9,672,000		28,400,000
Total liabilities and net assets	$	114,038,000	$	83,698,000

See accompanying notes.

	2011	2010
Operating revenues		
Net patient service revenue (net of provision for bad debts of $60,603,000 in 2011 and $59,707,000 in 2010)	$ 116,419,000	$ 130,185,000
Other operating revenue	1,166,000	1,130,000
Total operating revenues	117,585,000	131,315,000
Operating expenses		
Salaries and wages	61,659,000	64,690,000
Employee benefits	35,090,000	30,839,000
Supplies	18,777,000	20,928,000
Professional fees	10,907,000	10,022,000
Purchased services	10,309,000	9,507,000
Other operating expenses	3,845,000	4,344,000
Depreciation and amortization	4,165,000	3,593,000
Rentals and leases	3,995,000	2,848,000
Total operating expenses	148,747,000	146,771,000
Operating loss	(31,162,000)	(15,456,000)
Nonoperating revenues (expenses):		
District tax revenue	8,498,000	8,492,000
Investment income	46,000	92,000
Noncapital grants and contributions	5,443,000	10,813,000
Interest expense	(1,553,000)	(1,396,000)
Total nonoperating revenues	12,434,000	18,001,000
(Deficit) excess of revenues over expenses	(18,728,000)	2,545,000
Net assets beginning of the year	28,400,000	25,855,000
Net assets end of the year	$ 9,672,000	$ 28,400,000

See accompanying notes.

WEST CONTRA COSTA HEALTHCARE DISTRICT
STATEMENTS OF CASH FLOWS
Years Ended December 31, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Cash received from patients and third-parties on behalf of patients	$ 116,023,000	$ 128,430,000
Cash received from operations, other than patient services	4,057,000	2,442,000
Cash payments to suppliers and contractors	(48,243,000)	(48,443,000)
Cash payments to employees and benefits programs	(94,465,000)	(93,576,000)
Net cash used in operating activities	(22,628,000)	(11,147,000)
Cash flows from noncapital financing activities:		
Noncapital grants and contributions	5,443,000	10,813,000
Proceeds from county loan	10,000,000	-
Payments on county loan	(801,000)	(2,849,000)
Proceeds from debt borrowings	39,833,000	-
Principal payments on debt borrowings	(799,000)	(779,000)
Interest payments on debt borrowings	(1,327,000)	(1,143,000)
Proceeds from line of credit, net	3,346,000	-
Cash paid for debt issuance costs	(840,000)	-
Parcel tax revenues levied for debt service	5,618,000	5,643,000
Ad valorem tax revenues to support operations	1,865,000	2,849,000
Net cash provided by noncapital and related financing activities	62,338,000	14,534,000
Cash flows from capital and related financing activities:		
Purchases of capital assets	(1,875,000)	(4,942,000)
Proceeds from sale of capital assets	20,000	-
Proceeds from debt borrowings	-	1,500,000
Principal payments on debt borrowings	(3,091,000)	(3,033,000)
Interest payments on debt borrowings	(226,000)	(156,000)
Net cash used in capital and related financing activities	(5,172,000)	(6,631,000)
Cash flows from investing activities:		
Proceeds from sale of investments	1,228,000	715,000
Purchases of investments	(27,069,000)	-
Interest and dividends received from investments	46,000	92,000
Net cash (used in) provided by investing activities	(25,795,000)	807,000
Net increase (decrease) in cash and cash equivalents	8,743,000	(2,437,000)
Cash and cash equivalents at beginning of year	5,229,000	7,666,000
Cash and cash equivalents at end of year	$ 13,972,000	$ 5,229,000

See accompanying notes.

	2011	2010
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$ (31,162,000)	$ (15,456,000)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization	4,165,000	3,593,000
Gain on disposal of capital assets	(4,000)	-
Provision for bad debts	60,603,000	59,707,000
Changes in operating assets and liabilities:		
Patient accounts receivables	(59,838,000)	(60,492,000)
Other receivables	2,895,000	1,312,000
Supplies	143,000	(196,000)
Prepaid expenses and deposits	622,000	(1,011,000)
Accounts payable and accrued expenses	(1,175,000)	3,598,000
Accrued payroll and related liabilities	2,284,000	1,953,000
Other liabilities related to operating activities	-	(3,185,000)
Estimated third-party payor settlements	(1,161,000)	(970,000)
Net cash used in operating activities	$ (22,628,000)	$ (11,147,000)
Non cash disclosures		
Purchase of capital assets with capital lease	$ 1,809,000	$ -
Non cash proceeds from sale of capital assets	$ 162,000	$ -
Non cash payments on county loan	$ 1,015,000	$ -

See accompanying notes.

NOTE 1 – ORGANIZATION AND ACCOUNTING POLICIES

Reporting entity – West Contra Costa Healthcare District (the "District") is a public agency organized under Local Hospital District Law as set forth in the Health and Safety Code of the State of California. The District is a political subdivision of the State of California and is not subject to federal or state income taxes. The District was formed in 1948 for the purpose of building and operating a hospital to benefit the residents of West Contra Costa County. The District is governed by a Board of Directors elected from within the Healthcare District to specified terms of office. The District operates a full-service acute care facility and provides services to both inpatients and outpatients. The District provides health care services primarily to individuals who reside in the local geographic area.

WCCHD Financing Corporation II – The Corporation is a nonprofit public benefit corporation to provide financial assistance to the District by financing, refinancing, acquiring, constructing, improving, leasing and selling buildings, building improvements, equipment, and any other real or personal property (collectively, the "Facilities"), for the use, benefit and enjoyment of the public served by the District and any other purpose incidental thereto.

Basis of preparation – The District is a governmental health care provider and, accordingly, follows governmental accounting standards. The accrual basis of accounting is used in accordance with provisions for proprietary fund types.

Pursuant to Governmental Accounting Standards Board ("GASB") Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements, the District's proprietary fund accounting and financial reporting practices are based on all applicable GASB pronouncements as well as codified pronouncements issued on or before November 30, 1989.

Use of estimates – The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents – The District considers cash and cash equivalents to include certain investments in highly liquid debt instruments, when present, with an original maturity of three months or less or subject to withdrawal upon request.

Patient accounts receivable – Patient accounts receivable consist of amounts reimbursable by various governmental agencies and insurance companies through the assignment process and private patients. The District manages its receivables by regularly reviewing the accounts, inquiring with respective payors as to collectability and providing for allowances on their accounting records for estimates, contractual adjustments, and uncollectible accounts. Significant concentrations of patient accounts receivable are discussed further in the footnotes.

Investments in marketable securities – Investments in marketable securities consist primarily of short-term, interest-bearing certificates of deposit, money market funds, and mutual funds and include assets held by trustees under indenture agreements and designated assets set aside by the Board of Directors for future funding of certain District obligations.

Supplies – Inventories are stated at cost, which is determined using the first-in, first-out method.

Capital assets – Capital assets consist of property and equipment and are reported on the basis of cost, or in the case of donated items, on the basis of fair market value at the date of donation. Capital purchases over $1,000 are capitalized. Routine maintenance and repairs are charged to expense as incurred. Expenditures which increase values, change capacities, or extend useful lives are capitalized. Depreciation of property and equipment and amortization of property under capital leases are computed by the straight-line method for both financial reporting and cost reimbursement purposes over the estimated useful lives of the assets, which range from 10 to 30 years for buildings and improvements, and 3 to 10 years for equipment. Leasehold improvements are amortized using the straight-line method over the shorter of the lease term or the estimated useful life of the related assets. The District periodically reviews its capital assets for value impairment. As of December 31, 2011 and 2010, the District has determined that no capital assets are impaired.

Other assets – Other assets include debt issuance costs. Debt issuance costs incurred in connection with the issuance of tax-exempt bonds have been deferred and are being amortized over the term of the bonds using a straight-line method.

Costs of borrowing – Except for capital assets acquired through gifts, contributions, or capital grants, interest cost on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. None of the District's interest cost was capitalized for the years ended December 31, 2011 and 2010.

Compensated absences – District employees earn vacation benefits at varying rates depending on years of service. Employees also earn sick leave benefits based on varying rates depending on years of service. Both benefits can accumulate up to specified maximum levels. Employees are not paid for accumulated sick leave benefits if they leave either upon termination or before retirement. However, accumulated vacation benefits are paid to an employee upon either termination or retirement. Accrued vacation and sick leave liabilities as of December 31, 2011 and 2010 are $3,266,000 and $3,823,000, respectively.

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

Risk retention plans – The District maintains professional liability insurance on a claims-made basis, with liability limits of $10,000,000 per claim, and which is subject to a $25,000 deductible. Additionally, the District is self-insured for workers' compensation claims, with a self-insured retention of $350,000 per occurrence, and has excess insurance coverage for the portion of each occurrence in excess of $350,000. In the case of employee health coverage, the District is self-insured for those claims. Management estimates of uninsured losses for professional liability, workers' compensation and employee health coverage have been accrued as liabilities in the accompanying financial statements.

Net assets – Net assets of the District are classified in three components:

- Net assets invested in capital assets, net of related debt consist of capital assets net of accumulated depreciation and reduced by any outstanding borrowings used to finance the purchase or construction of those assets.

- Restricted expendable net assets are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the District, including amounts deposited with trustees as required by revenue bond indentures, discussed in Note 3.

- Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted expendable net assets.

Net patient service revenue – Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered, and adjusted in future periods as final settlements are determined.

Charity care – The District accepts all patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain established policies of the District. Essentially, these policies define charity services as those services for which no payment is anticipated. Because the District does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care amounts are included in net patient revenues in the financial statements.

Uncollectible accounts – The District provides care to patients without requiring collateral or other security. Patient charges not covered by a third-party payor are billed directly to the patient if it is determined that the patient has the ability to pay. A provision for uncollectible accounts is recognized based on management's estimate of amounts that ultimately may be uncollectible.

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

Operating revenues and expenses – The District's statement of revenues, expense and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, which is the District's principal activity. Operating expenses are all expenses incurred to provide health care services, other than financing costs. Nonoperating revenues and expenses are those transactions not considered directly linked to providing health care services.

Income taxes – The District operates under the purview of the Internal Revenue Code, Section 115, and corresponding California Revenue and Taxation Code provisions. As such, it is not subject to state or federal taxes on income.

Property taxes – The authority received approximately 6.5% in 2011 and 5.6% in 2010 of its financial support from property taxes. These funds were used as follows:

	2011	2010
Levied for debt service	$ 5,618,000	$ 5,643,000
Used to support operations	$ 2,880,000	$ 2,849,000

Property taxes are levied by the County on the District's behalf on January 1 and are intended to finance the District's activities of the same calendar year. Amounts levied are based on assessed property values as of the preceding July 1. Property taxes are considered delinquent on the day following each payment due date. Property taxes are recorded as nonoperating revenue by the District when they are earned.

Reclassifications – Certain amounts in the 2010 financial statements have been reclassified to conform to the 2011 presentation.

New accounting pronouncements – The Governmental Accounting Standards Board ("GASB") issued GASB Statement No. 61, The Financial Reporting Entity: Omnibus (November 2010). GASB 61 clarifies certain aspects of GASB 14, The Financial Reporting Entity, which establishes the criteria governing which of a governmental entity's related parties should be formally incorporated into its financial statements. The adoption of GASB 61 is effective for the District beginning January 1, 2013. The adoption of GASB 61 is not expected to have a material impact on the District's financial statements.

NOTE 2 – CASH AND CASH EQUIVALENTS, BOARD DESIGNATED AND TRUSTEED ASSETS

As of December 31, 2011 and 2010, the District had deposits invested in various financial institutions in the form of cash and cash equivalents including amounts classified as board designated assets amounting to $44,461,000 and $9,877,000, respectively. All of these funds were held in deposits, which are collateralized in accordance with the California Government Code ("CGC"), except for $250,000 per account that is federally insured.

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

The composition of board designated and trusteed assets at December 31, 2011 and 2010, is set forth in the following table. Investments are stated at fair value.

	2011	2010
Board designated		
Cash and cash equivalents	$ 642,000	$ 642,000
Certificates of deposit	352,000	351,000
Held by trustee		
Money market	29,495,000	3,655,000
	$ 30,489,000	$ 4,648,000

Interest and dividend income for investments and gains from assets limited as to use is $46,000, and $92,000 for the years ended December 31, 2011 and 2010, respectively.

NOTE 3 – NET PATIENT SERVICE REVENUE AND REIMBURSEMENT PROGRAMS

The District renders services to patients under contractual arrangements with the Medicare and Medi-Cal programs, health maintenance organizations ("HMOs") and preferred provider organizations ("PPOs"). Patient service revenues from Medicare approximate 49% and 47% of gross patient service revenues, whereas patient service revenues from Medi-Cal approximate 24% and 25% for the years ended December 31, 2011 and 2010, respectively.

The District has agreements with third-party payors that provide for payments to the District at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, fee schedules, prepaid payments per member, and per diem payments or a combination of these methods. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated settlements under reimbursement agreements with third-party payors.

Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Inpatient nonacute services related to Medicare beneficiaries are paid based on a cost-reimbursement methodology through March 31, 2004. Inpatient nonacute services subsequent to April 1, 2004, are paid at prospectively determined rates per discharge. Payments for outpatient services are based on a stipulated amount per diagnosis. The District is reimbursed for cost reimbursable items at a tentative rate, with final settlements determined after submission of annual cost reports by the District and audits thereof by the Medicare fiscal intermediary. The effect of updating prior year estimates for Medicare and other liabilities was to decrease net operating income by $143,000 in 2011 and an increase of net operating income by $2,414,000 in 2010. The District's cost reports have been audited by the Medicare fiscal intermediary through 2008.

Medicare accounts for approximately 50% and 50% of the District's net patient service revenues whereas Medi-Cal revenue accounts for approximately 22% and 24% for the years ended December 31, 2011 and 2010, respectively. Laws and regulations governing the Medicare and Medi-Cal programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term.

In November 2009, the California Hospital Fee Program (the "Program") was signed into California state law and became effective for 2010 after approval from the Centers for Medicare and Medicaid Services ("CMS"). The program provides supplemental Medi-Cal payments to certain California hospitals. The Program is funded by a quality assurance fee (the "Fee") paid by participating hospitals and by matching federal funds. Hospitals receive supplemental payments from either the California Department of Health Care Services ("DHCS"), managed care plans or a combination of both. The Program provided payments relating to the period beginning April 1, 2009 through December 31, 2010. The District recognized total supplemental payments of $1,608,000 in 2011 and $1,358,000 in 2010 from Medi-Cal as a part of the Program and has recorded this as a part of net patient service revenue in the statement of revenues, expenses, and changes in net assets.

NOTE 4 – CONCENTRATION OF CREDIT RISK

The District grants credit without collateral to its patients and third-party payors. Patient accounts receivable from government agencies represent the only concentrated group of credit risk for the District and management does not believe that there are any credit risks associated with these governmental agencies. Contracted and other patient accounts receivable consist of various payors including individuals involved in diverse activities, subject to differing economic conditions and do not represent any concentrated credit risks to the District. The District's policy is to maintain a 100% reserve for all private pay patient accounts receivables outstanding aged over 240 days. Concentration of patient accounts receivable at December 31, 2011 and 2010, were as follows:

	2011	2010
Medicare	44%	44%
Other third-party payors	46%	43%
Medi-Cal and Medi-Cal pending	10%	13%
Total	100%	100%

NOTE 5 – OTHER RECEIVABLES

Other receivables as of December 31, 2011 and 2010 were comprised of the following:

	2011	2010
Advances to physicians, notes and related receivables	$ 632,000	$ 572,000
Deposits	252,000	316,000
Refunds and rebates receivable	137,000	1,000,000
Third-party settlement receivable	139,000	1,935,000
Other	-	232,000
Total other receivables	$ 1,160,000	$ 4,055,000

Advances to physicians are comprised of physician income guarantees and/or business loans to those physicians requiring assistance to begin a local practice. The District has entered into agreements with certain physicians whereby the District guarantees their income for a specified period of time. These agreements are structured so that if a physician maintains a practice in the area for a specified period of time, the income guarantee advances are forgiven.

NOTE 6 – CAPITAL ASSETS

Capital assets as of December 31, 2011, were comprised of the following:

	Balance at December 31, 2010	Additions	Retirements & Adjustments	Balance at December 31, 2011
Capital assets not being depreciated				
Land and land improvements	$ 12,120,000	$ -	$ -	$ 12,120,000
Construction-in-progress	960,000	3,931,000	(246,000)	4,645,000
	13,080,000	3,931,000	(246,000)	16,765,000
Capital assets being depreciated				
Buildings and improvements	16,955,000	-	(97,000)	16,858,000
Equipment	31,988,000	-	(999,000)	30,989,000
	48,943,000	-	(1,096,000)	47,847,000
Totals at historical cost	62,023,000	3,931,000	(1,342,000)	64,612,000
Less accumulated depreciation	(16,616,000)	(4,132,000)	918,000	(19,830,000)
Total capital assets, net	$ 45,407,000	$ (201,000)	$ (424,000)	$ 44,782,000

Capital assets as of December 31, 2010, were comprised of the following:

	Balance at December 31, 2009	Additions	Retirements & Adjustments	Balance at December 31, 2010
Capital assets not being depreciated				
Land and land improvements	$ 12,090,000	$ 30,000	$ -	$ 12,120,000
Construction-in-progress	1,280,000	-	(320,000)	960,000
	13,370,000	30,000	(320,000)	13,080,000
Capital assets being depreciated				
Buildings and improvements	16,931,000	24,000	-	16,955,000
Equipment	31,856,000	4,888,000	(4,756,000)	31,988,000
	48,787,000	4,912,000	(4,756,000)	48,943,000
Totals at historical cost	62,157,000	4,942,000	(5,076,000)	62,023,000
Less accumulated depreciation	(18,124,000)	(3,568,000)	5,076,000	(16,616,000)
Total capital assets, net	$ 44,033,000	$ 1,374,000	$ -	$ 45,407,000

Future construction commitments of approximately $2,099,000 and $4,702,000 exist for the upgrade of the Paragon system and installation of medical equipment at December 31, 2011 and 2010.

NOTE 7 – DEBT BORROWINGS

A schedule of changes in the District's debt borrowings for the year ended December 31, 2011, is as follows:

	December 31, 2010	Additions	Reductions	December 31, 2011
Notes payable:				
American Savings	$ 31,000	$ -	$ (5,000)	$ 26,000
City of San Pablo	1,346,000	-	(479,000)	867,000
Bonds payable:				
Certificates of participation - Series 2004	22,865,000	-	(799,000)	22,066,000
Certificates of participation - Series 2011	-	39,833,000	-	39,833,000
Revenue bonds	1,181,000	-	(1,181,000)	-
Capital leases - equipment	1,205,000	1,809,000	(1,426,000)	1,588,000
	$ 26,628,000	$ 41,642,000	$ (3,890,000)	$ 64,380,000

A schedule of changes in the District's debt borrowings, for the year ended December 31, 2010, is as follows:

	December 31, 2009	Additions	Reductions	December 31, 2010
Notes payable:				
American Savings	$ 36,000	$ -	$ (5,000)	$ 31,000
City of San Pablo	-	1,500,000	(154,000)	1,346,000
Bonds payable:				
Certificates of participation - Series 2004	23,644,000	-	(779,000)	22,865,000
Revenue bonds	2,321,000	-	(1,140,000)	1,181,000
Capital leases - equipment	2,939,000	-	(1,734,000)	1,205,000
	$ 28,940,000	$ 1,500,000	$ (3,812,000)	$ 26,628,000

The terms and due dates of the District's debt borrowings, including capital lease obligations, at December 31, 2011, are as follows:

- American Savings notes payable dated September 1986, interest at 9.5%, maturing November 2015, principal payable in annual amounts ranging from $5,000 in 2012 to $7,000 in 2015, secured by property.

- City of San Pablo notes payable dated August 2010, interest at 6.0%, maturing July 2013, principal payable amount ranging from $509,000 in 2012 to $357,000 in 2013, unsecured.

- Series 2004 Certificates of Participation dated July 2004, plus unamortized bond premium of $422,000, principal payable in annual installments ranging from $800,000 in 2012 to $1,795,000 in 2029, interest at stated coupon rates ranging from 2.0% to 5.5%, payable annually and collateralized by a pledge of the District's parcel tax revenues. Management believes the District is in compliance with the financial covenants and financial reporting requirements as specified in the Indenture Trust Agreement.

- Series 2011 Certificates of Participation dated December 2011, plus unamortized bond discount of $167,000, principal payable in annual installments ranging from $70,000 in 2013 to $4,100,000 in 2042, interest ranging from 3% to 6.25%, payable semi annually and collateralized by a pledge of the District's parcel tax revenues. Management believes the District is in compliance with the financial covenants and financial reporting requirements as specified in the Indenture Trust Agreement.

- Equipment under capital leases dated March 2011, maturing at March 2016, with interest at 9.45%.

The District executed a credit agreement with Gemino Healthcare Finance, LLC dated November 2011, for a maximum amount of $8 million, expiring November 3, 2014. The agreement is defined as a revolving loan that is collateralized by the District's accounts receivable collections. During 2011, the District was advanced $17.3 million and repaid $13.9 million for an ending outstanding balance of $3.4 million on this line of credit. The line of credit bears interest on the outstanding principal amount at a rate per annum equal to the LIBOR rate plus 4.95%.

Aggregate principal maturities on debt borrowings, based on scheduled maturities are as follows:

	Debt Borrowings		Capital Lease Obligations	
Year Ending December 31:	Principal	Interest	Principal	Interest
2012	$ 4,679,000	$ 2,341,000	$ 300,000	$ 137,000
2013	1,282,000	3,463,000	350,000	106,000
2014	960,000	3,422,000	385,000	71,000
2015	995,000	3,387,000	423,000	33,000
2016-2020	5,582,000	16,281,000	132,000	2,000
2021-2025	7,142,000	14,714,000	-	-
2026-2030	9,248,000	12,577,000	-	-
2031-2035	12,152,000	9,590,000	-	-
2036-2040	16,147,000	5,592,000	-	-
2041-2045	7,949,000	753,000	-	-
	$ 66,136,000	$ 72,120,000	$ 1,590,000	$ 349,000

NOTE 8 – OTHER LONG TERM LIABILITIES

The District entered into an agreement with the County of Contra Costa (the "County") in April 2011, receiving a cash advance of $10 million. The County Auditor shall allocate and transfer to the County pursuant to this agreement the entirety of the general ad valorem property tax revenues that otherwise would be collected and allocated to the District commencing July 1, 2011 and continuing from year to year thereafter until a total up to $11.5 million of transfers are made. The current and long term outstanding advance balance is included in other liabilities in the balance sheet.

NOTE 9 – RETIREMENT PLANS

The District offers two defined contribution savings plans intended to qualify under section 457(b) of the Internal Revenue Code ("IRC"). The plans are destined to provide participants with a means to defer a portion of their compensation for retirement and to provide benefits in the event of death, disability, or financial hardship. The plans cover both former and current employees of the District who meet certain eligibility requirements. The District is the administrator of the plans and has delegated certain responsibilities for the operation and administration of the plans to outside third-party trustees. Under the plans employer contributions are discretionary. The District has not contributed to the plans since 2007.

The District also offers two Employer Contributory Tax Deferred Annuity Plans intended to qualify under section 403(b) and 457 of the IRC. The plans are designed to provide participants with a means to defer a portion of their compensation for retirement and to provide benefits in the event of death, disability, or financial hardship. The plan covers employees of the District, who meet certain eligibility requirements. Under the plan, the District may make matching contributions up to 5.0% of the participant's annual compensation to the plan. The District contributed $3,723,000 and $3,568,000 to the plans in 2011 and 2010, respectively.

The District also provides a non-contributory single employer defined benefit pension plan. The plan covers all eligible employees of the previous Brookside Hospital. Brookside Hospital was the previous name of Doctors Medical Center prior to the Tenet purchase. The plan provides retirement and death benefits to plan members and beneficiaries based on each employee's years of service and annual compensation. No new employees have been enrolled in the plan since 1996. There are no current District employees participating in the plan.

Annual pension cost and net pension obligation – The plan's annual pension cost and net pension obligation for the current and prior year were as follows:

	2011	2010
Annual required contribution	$ 431,000	$ 444,000
Interest on net pension obligation	61,000	26,000
Adjustment to annual required contribution	(86,000)	(37,000)
Annual pension cost	406,000	433,000
Net increase in pension obligation	$ 406,000	$ 433,000
Net pension obligation (prepaid pension asset), beginning of year	$ 764,000	$ 331,000
Net increase in pension obligation	407,000	433,000
Actuarial loss	-	-
Net pension obligation, end of year	$ 1,171,000	$ 764,000

The annual required contribution for the current year was determined as part of the January 1, 2011 and January 1, 2010, actuarial valuations using the entry age actuarial cost method. The actuarial assumptions include (a) 7.5% and 8.0% in 2011 and 2010, respectively, of investment rate of return (net of administrative expenses) and (b) post-retirement benefit increases of 2.0% per year. Both assumptions included an inflation component of 2.0%. The actuarial value of assets for both valuations was determined using market value adjusted to recognize market value gains and losses over five years. The unfunded actuarial accrued liability is amortized using the level dollar method on a closed basis. The remaining equivalent single amortization period at December 31, 2011, was 15 years.

The following table summarizes the net pension obligation ("NPO") for the District's pension plan:

Fiscal Year Ending December 31,	Beginning of Year NPO (a)	Annual Pension Cost (b)	Actual Contribution (c)	Increase (Decrease) in NPO (b-c)	End of Year NPO (Prepaid Pension Cost) ((a)+(b-c))
2009	$ (134,000)	$ 465,000	$ -	$ 465,000	$ 331,000
2010	$ 331,000	$ 433,000	$ -	$ 433,000	$ 764,000
2011	$ 764,000	$ 407,000	$ -	$ 407,000	$ 1,171,000

Funding policy – The District is required to contribute the actuarially determined amounts necessary to fund the benefits for its participants. Active plan participants are not required to contribute. The actuarial methods and assumptions used are those adopted by the District.

NOTE 10 – COMMITMENTS AND CONTINGENCIES

Litigation – The District may from time-to-time be involved in litigation and regulatory investigations, which arise in the normal course of doing business. After consultation with legal counsel, management estimates that matters existing as of December 31, 2011, will be resolved without material adverse effect on the District's future financial position, results from operations or cash flows.

Lease commitments – The District is obligated for land and office rentals under the terms of various noncancelable operating lease agreements. These expire in various years through 2014. The District also entered into various noncancelable operating sublease agreements for office space. These expire in various years through 2014. Following is a schedule by year of future minimum lease payments and future minimum rental revenues under operating leases as of December 31, 2011:

	Operating Lease Commitments	Lease Income	Net Lease Expense
2012	$ 1,662,000	$ 392,000	$ 1,270,000
2013	909,000	398,000	511,000
2014	854,000	404,000	450,000
2015	-	-	-
	$ 3,425,000	$ 1,194,000	$ 2,231,000

Total rental expense in 2011 and 2010 for all operating leases was approximately $3,995,000 and $2,848,000, respectively. Total rental income in 2011 and 2010 for all operating subleases was approximately $588,000 and $620,000, respectively.

Regulatory environment – The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. The District is subject to routine surveys and reviews by federal, state and local regulatory authorities. The District has also received inquiries from health care regulatory authorities regarding its compliance with laws and regulations. Although the District management is not aware of any violations of laws and regulations, it has received corrective action requests as a result of completed and on going surveys from applicable regulatory authorities. Management continually works in a timely manner to implement operational changes and procedures to address all corrective action requests from regulatory authorities. Breaches of these laws and regulations and non-compliance with survey corrective action requests could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

REQUIRED SUPPLEMENTARY INFORMATION - PENSION

Analysis of funding progress - pension plan – The following table summarizes the funding status of the District's pension plan:

Actuarial Valuation Date December 31,	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2009	$ 6,626,000	$ 10,726,000	$ 4,100,000	62%	N/A	N/A
2010	$ 6,470,000	$ 10,458,000	$ 3,988,000	62%	N/A	N/A
2011	$ 5,460,000	$ 10,436,000	$ 4,976,000	52%	N/A	N/A