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Slidell Memorial Hospital

*Management's Discussion and Analysis,
Consolidated Financial Statements and
Additional Information as of December 31, 2004
and 2003 and for the Years Then Ended and
Independent Auditors' Reports*

Under provisions of state law, this report is a public document. A copy of the report has been submitted to the entity and other appropriate public officials. The report is available for public inspection at the Baton Rouge office of the Legislative Auditor and, where appropriate, at the office of the parish clerk of court.

Release Date 6/22/05

SLIDELL MEMORIAL HOSPITAL

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MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of St. Tammany Parish Hospital Service District No. 2's (Slidell Memorial Hospital or "the Hospital") annual financial report presents background information and management's analysis of the Hospital's financial performance during the fiscal year that ended on December 31, 2004. This should be read in conjunction with the financial statements in this report.

GOVERNANCE

Fiscal 2004 was the first full year under the revised governance structure of the Hospital. Governance was significantly revised by Act 562 (which amended Act 180) of the 2003 Regular Session of the Louisiana Legislature. Act 562 created a nominating committee to solicit, interview and make nominations for appointment to the Board of Commissioners. The legislation also sets forth an appointing authority of the District, which is a cross-section of representatives of city, parish and state governmental bodies. The appointing authority appoints the Board of Commissioners from the nominations put forth by the nominating committee. Act 562 increased the number of physicians on the Board from one to two. The St. Tammany Parish Hospital Service District No. 2 Board of Commissioners (the Board) is authorized to oversee the assets and govern the operations of the Hospital.

FINANCIAL HIGHLIGHTS

Net patient service revenue increased \$5.9 million or 6% from prior year due primarily to: (1) 4% growth in acute admissions and (2) a 3% across-the-board price increase instituted on July 1, 2004. Operating expenses increased \$4.6 million or 5% from prior year primarily from costs associated with services due to increased patient volumes. In total, the Hospital experienced an increase in the excess of revenues over expenses of \$2,850,000 as compared to the fiscal year 2003. Of the increased bottom line, \$1,535,000 is the net effect of non-operating income related to the general obligation bonds backed by a property tax.

The Hospital's total net assets increased by \$3.7 million or 10%, from the prior year. This results from the recognition of revenue in excess of expenses for the year of \$3.7 million. The assets of the Hospital exceeded liabilities at the close of the 2004 fiscal year by \$39 million. Of this amount, \$21 million (unrestricted net assets) may be used to meet ongoing obligations to the Hospital District's patients and creditors, and \$16 million is invested in capital assets, net of related debt.

The year 2004 was a transition year for the organization. This was the first full year of operation of the new competing 58 bed MedCath physician joint venture facility. The impact on cardiology volumes was evident, but not as dramatic as the most conservative sensitivity analysis prepared by management. As a matter of fact, the actual cardiology impact was within 2% of the sensitivity most likely case scenario.

On October 4th, 2003 the voters of the service district passed a property tax to fund a \$22.45 million general obligation bond issue refinancing all three of the hospital revenue bond issues. The cash flow improvements associated with the general obligation issue did not manifest until the actual sale of the bonds during 2004. On March 31st, 2004 the hospital closed a refinancing of the first \$8.0 million of the 1994 bonds. Due to certain laws governing tax exempt bonds, the remaining general obligation bonds could not be sold until August 2004. By issuing general obligation bonds funded by property tax collections, the hospital's operating cash flow is relieved of bond-related debt service requirements. As a result of the general obligation issues, management anticipates an additional \$5.5 million per year in improved cash flow in 2005 and thereafter. Management anticipates using the improved cash flow to rebuild cash reserves and invest in hospital infrastructure and equipment.

In June 2004, the hospital ended its revenue cycle outsourcing agreement in order to bring the revenue cycle function back in-house. This transition which required six months to complete, improved collections and created 30 new jobs in Slidell. As evidenced in the cash flow statement, accounts receivable were dramatically improved resulting in increased cash reserves and decreased accounts payable given the ability to catch up late payments to vendors.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of four components – the Management’s Discussion and Analysis of Financial Condition and Operating Results (this section), the Independent Auditors’ Report, the Consolidated Financial Statements, and Supplementary Information.

The *Consolidated Financial Statements* of Slidell Memorial Hospital report the consolidated financial position of the Hospital and the consolidated results of its operations and its cash flows. The consolidated financial statements are prepared on the accrual basis of accounting. These statements offer short-term and long-term financial information about the Hospital’s activities.

The *Consolidated Balance Sheet* includes all of the Hospital’s assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to the Hospital’s creditors (liabilities) for both the current year and the prior year. It also provides the basis for evaluating the capital structure of the Hospital, and assessing the liquidity and financial flexibility of the Hospital.

All of the current year’s revenues and expenses are accounted for in the *Consolidated Statement of Revenue, Expenses, and Changes in Net Assets*. This statement measures the performance of the Hospital’s operations over the past two years and can be used to determine whether the Hospital has been able to recover all of its costs through its patient service revenue and other revenue sources.

The primary purpose of the *Consolidated Statement of Cash Flows* is to provide information about the Hospital’s cash from operations, investing, and financing activities. The cash flow statement outlines where the cash comes from, what the cash is used for, and the change in the cash balance during the reporting period.

The annual report also includes *Notes to the Consolidated Financial Statements* that are essential to gain a full understanding of the data provided in the consolidated financial statements. The notes to the consolidated financial statements can be found immediately following the basic financial statements in this report.

Following the notes to the consolidated financial statements is a section containing supplementary information that further explains and supports the information reported in the consolidated financial statements. This section includes optional schedules showing Gross Revenue and Expenses by cost center as well as statistical information.

FINANCIAL ANALYSIS OF THE HOSPITAL

The consolidated balance sheet and the consolidated statement of revenue, expenses, and changes in net assets report information about the Hospital's activities. These two statements report the net assets of the Hospital and changes in them. Increases or improvements, as well as decreases or declines in the net assets, are one indicator of the financial state of the Hospital. Other non-financial factors that should also be considered include changes in economic conditions (including uninsured and working poor) and population growth.

Summary of Balance Sheets

A summary of the Hospital's balance sheets is presented in the following table:

Condensed Consolidated Balance Sheets (In Thousands)

	Fiscal Year 2004	Fiscal Year 2003	Dollar Change	Total % Change
Current and other assets	\$ 41,281	\$ 36,417	\$ 4,864	13 %
Capital assets	<u>41,839</u>	<u>42,180</u>	\$ (341)	<u>(1)%</u>
Total assets	<u>\$ 83,120</u>	<u>\$ 78,597</u>	<u>\$ 4,523</u>	<u>6 %</u>
Long-term debt outstanding	\$ 30,877	\$ 9,893	\$ 20,984	212 %
Other liabilities	<u>13,371</u>	<u>33,523</u>	<u>(20,152)</u>	<u>(60)%</u>
Total liabilities	<u>\$ 44,248</u>	<u>\$ 43,416</u>	<u>\$ 832</u>	<u>2 %</u>
Invested in capital assets, net of related debt	\$ 16,177	\$ 13,110	\$ 3,067	23 %
Restricted	2,100	5,066	(2,966)	(59)%
Unrestricted	<u>20,595</u>	<u>17,005</u>	<u>3,590</u>	<u>21 %</u>
Total net assets	<u>\$ 38,872</u>	<u>\$ 35,181</u>	<u>\$ 3,691</u>	<u>10 %</u>

Long term debt increased 212% primarily due to the refinancing of revenue bonds with general obligation bonds, and the addition of capital leases during FY04 to accelerate strategic replacement of core equipment. Other liabilities decreased 60% as a result of reduction in vendor payables made possible by strong collections of accounts receivable and also due to the classification as a current liability at December 31, 2003 of \$15.8 million of long-term debt which was refinanced in 2004.

Unrestricted net assets increased \$3.59 million or 21%.

Summary of Revenue, Expenses, and Changes in Net Assets

The following table presents a summary of the Hospital's historical revenues and expenses for each of the fiscal years ended December 31, 2004 and 2003:

(In Thousands)

	Fiscal Year 2004	Fiscal Year 2003
Net patient service revenue	\$ 105,800	\$ 99,863
Other operating revenue excluding interest income	<u>2,149</u>	<u>2,197</u>
Total operating revenues	<u>107,949</u>	<u>102,060</u>
Maintenance and operation expenses	86,668	81,743
Bad debt expense	<u>10,267</u>	<u>10,198</u>
Total operating expenses before depreciation/amortization	<u>96,935</u>	<u>91,941</u>
Earnings before interest depreciation and amortization (EBIDA)	<u>11,014</u>	<u>10,119</u>
Depreciation and amortization expense	<u>6,459</u>	<u>6,880</u>
Operating net income	4,555	3,239
Non-operating revenues (expenses):		
Interest income	342	190
Interest expense	(1,987)	(1,960)
Property tax revenue	2,100	
Expenses associated with debt restructuring and tax referendum	<u>(1,319)</u>	<u>(629)</u>
Revenues in excess of expenses	3,691	840
Total net assets - beginning of year	<u>35,181</u>	<u>34,341</u>
Total net assets - end of year	<u>\$ 38,872</u>	<u>\$ 35,181</u>

Operating Revenue

During fiscal year 2004, the Hospital derived approximately 98% of its total revenues from net patient service revenues. Operating revenues include revenues from the Medicare and Medicaid programs, patients, or their third-party carriers who pay for care in the Hospital's facilities.

The following table represents the relative percentage of gross charges billed for patient services by payor for the fiscal years ended December 31, 2004 and 2003:

	Fiscal Year 2004	Fiscal Year 2003
Medicare	38.8 %	39.6 %
Medicaid	9.9 %	9.4 %
Managed care and commercial insurance	45.3 %	45.2 %
Uninsured	<u>6.0 %</u>	<u>5.8 %</u>
Total gross charges	<u>100.0 %</u>	<u>100.0 %</u>

OPERATING AND FINANCIAL PERFORMANCE

The following summarizes the Hospital's Statements of Revenue, Expenses, and Changes in Net Assets between 2004 and 2003:

- During 2004, the Hospital had 8,406 inpatient admissions. This is an increase of 4% from fiscal year 2003.
- Outpatient registrations were 59,434 in 2004. This is an increase of 9% from fiscal year 2003.
- Emergency registrations were 24,835 in 2004. This is a decrease of 4% from fiscal year 2003.
- Net patient service revenue increased \$5.9 million or 6% from prior year due primarily to: (1) growth of acute admissions of 4% and (2) a 3% across-the-board price increase instituted on July 1, 2004.
- Although inpatient admissions increased 4% from fiscal year 2003, cath procedures (which is an indicator of highly profitable cardiology business) decreased 28% from fiscal year 2003 and this resulted in an unfavorable net revenue budget variance.
- Salaries and wages increased \$2.8 million, due to (1) a 3% across the board pay increase, (2) termination of the revenue cycle outsourcing agreement in mid-year returning jobs to payroll from purchased services and (3) increased staff required to service the increased patient volumes.
- Supplies and materials increased approximately 9% compared to 2003 reflecting (1) a 4% increase in admissions and (2) the rising cost of drugs, implantable devices, and chemotherapy.
- Net nonoperating income and expenses of \$781,000 were incurred in 2004 related to the Hospital's debt refinancing efforts. These income and expense items include (1) property tax revenue accrued at year end of \$2.1 million, (2) revenue bond redemption premiums of \$437,000 and (3) accelerated amortization of \$882,000 in unamortized issuance cost of the revenue bonds refinanced with the general obligation bonds during 2004.
- Interest expense of \$568,000 related to the general obligation bonds was recognized during FY04.

PERFORMANCE AGAINST BUDGET

	FY 2004 Budget	FY 2004 Actual	Favorable (Unfavorable) Variance
Revenues:			
Net patient service revenue	\$ 107,373	\$ 105,800	\$ (1,573)
Other operating revenue	<u>2,201</u>	<u>2,149</u>	<u>(52)</u>
Total revenues	<u>109,574</u>	<u>107,949</u>	<u>(1,625)</u>
Operating expenses:			
Salaries, wages and benefits	45,149	44,709	440
Supplies and other	28,990	29,620	(630)
Provision for bad debts	12,485	10,267	2,218
Professional and contractual services	<u>12,553</u>	<u>12,339</u>	<u>214</u>
Total operating expenses before depr/amort	<u>99,177</u>	<u>96,935</u>	<u>2,242</u>
EBIDA	<u>10,397</u>	<u>11,014</u>	<u>617</u>
Interest income	181	342	161
Interest expense	(1,195)	(1,987)	(792)
Depreciation and amortization	(6,798)	(6,459)	339
Non-operating expenses, net	<u>(1,278)</u>	<u>781</u>	<u>2,059</u>
Excess of revenues over expenses	<u>1,307</u>	<u>3,691</u>	<u>2,384</u>
Increase (decrease) in net assets	<u>\$ 1,307</u>	<u>\$ 3,691</u>	<u>\$ 2,384</u>

- The most significant budget variance is the provision for bad debts. This results from improved revenue cycle performance.

CAPITAL ASSETS

	FY 2004	FY 2003	Dollar Change	Percent Change
Land and land improvements	\$ 4,675	\$ 4,675	\$ -	- %
Building and leasehold improvements	62,207	62,172	35	0 %
Equipment	<u>47,966</u>	<u>47,821</u>	<u>145</u>	<u>0 %</u>
Subtotal	114,848	114,668	180	0 %
Less: Accumulated depreciation	<u>(73,009)</u>	<u>(72,488)</u>	<u>(521)</u>	<u>1 %</u>
Net capital assets	<u>\$ 41,839</u>	<u>\$ 42,180</u>	<u>\$ (341)</u>	<u>(1)%</u>

Net capital assets decreased 1% due to continued recognition of depreciation and the Hospital's limited ability to invest in capital projects. As stated earlier, the refinancing of revenue bonds with general obligation bonds created a slight improvement in cash flow available for capital improvements in FY04, but the cash flow improvement matures in FY05 and beyond.

LONG-TERM DEBT

The hospitals revenue bonds were refinanced with property tax backed general obligation bonds during FY04. In addition, capital leases totaling \$9.6 million were entered into in order to accelerate strategic deployment of equipment replacement. More detailed information about the long-term debt is presented in the Notes to the Consolidated Financial Statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Hospital's Board and Management considered many factors when setting the fiscal year 2005 budget. *Of primary importance in setting the 2005 budget is the status of the economy, which takes into account market forces and environmental factors such as:*

- Increased competition in the marketplace in the form of physician investor specialty hospitals
- Medicare reimbursement changes and reductions
- Medicaid reimbursement reductions
- Increased number of uninsured and working poor
- Louisiana charity hospital system uncertainty
- Workforce shortages primarily in nursing and other clinically skilled positions
- Cost of implantable devices
- Cost of drugs
- Access to free cash flow
- Increased compliance costs due to HIPAA regulations

CONTACTING THE HOSPITAL FINANCIAL MANAGER

This Financial report is designed to provide our citizens, customers, and creditors with a general overview of the Hospital's finances. *If you have any questions about this report or need additional financial information, please contact the Chief Financial Officer, Slidell Memorial Hospital, 1001 Gause Blvd. Slidell, LA 70458.*

INDEPENDENT AUDITORS' REPORT

Members of the Board of Commissioners
St. Tammany Parish Hospital Service
District No. 2:

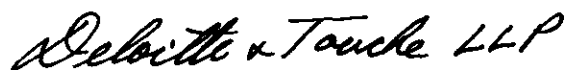
We have audited the accompanying consolidated balance sheets of St. Tammany Parish Hospital Service District No. 2 (d/b/a Slidell Memorial Hospital) (the Hospital) as of December 31, 2004 and 2003, and the related consolidated statements of revenue, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of Slidell Memorial Hospital'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 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 Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, 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 consolidated financial position of Slidell Memorial Hospital at December 31, 2004 and 2003, and the consolidated 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 I through 7 is not a required part of the basic consolidated financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Slidell Memorial Hospital'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 we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 19, 2005 on our consideration of Slidell Memorial Hospital's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.



March 19, 2005

SLIDELL MEMORIAL HOSPITAL

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2004 AND 2003

ASSETS	2004	2003
CURRENT ASSETS:		
Cash and cash equivalents	\$ 10,379,605	\$ 5,537,144
Patient accounts receivable, net of allowance for uncollectible accounts of \$7,908,488 in 2004 and \$8,391,841 in 2003, respectively	15,179,996	17,250,322
Assets whose use is limited - required for current liabilities	939,657	1,167,307
Inventories	1,971,553	2,022,426
Prepaid expenses and other receivables	<u>1,115,242</u>	<u>1,461,012</u>
Total current assets	<u>29,586,053</u>	<u>27,438,211</u>
ASSETS WHOSE USE IS LIMITED OR RESTRICTED:		
By board or under agreements for capital improvements and debt service	11,524,273	7,448,836
By donors	<u>29,185</u>	<u>24,185</u>
Total assets whose use is limited or restricted	<u>11,553,458</u>	<u>7,473,021</u>
CAPITAL ASSETS:		
Land and improvements	4,675,583	4,675,583
Buildings	62,206,609	62,171,994
Equipment	47,965,563	47,820,514
Less accumulated depreciation and amortization	<u>(73,008,586)</u>	<u>(72,488,510)</u>
Total capital assets—net	<u>41,839,169</u>	<u>42,179,581</u>
OTHER ASSETS	<u>141,587</u>	<u>1,505,944</u>
TOTAL	<u>\$ 83,120,267</u>	<u>\$ 78,596,757</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Trade accounts payable	\$ 3,959,286	\$ 7,472,022
Salaries, wages and benefits payable	1,314,382	1,002,161
Accrued vacation payable	1,397,126	1,253,414
Accrued interest and other expenses	2,946,671	2,644,744
Amounts due to third-party payors	1,368,575	953,750
Amounts due within one year on capital lease obligations	1,850,152	406,645
Amounts due within one year on bonds	365,000	19,619,806
Amounts due within one year on notes payable	<u>170,000</u>	<u>170,000</u>
Total current liabilities	<u>13,371,192</u>	<u>33,522,542</u>
CAPITAL LEASE OBLIGATIONS—less amounts due within one year	8,241,879	1,043,262
BONDS—less amounts due within one year	21,955,000	8,000,000
NOTES PAYABLE—less amounts due within one year	680,000	850,000
COMMITMENTS AND CONTINGENCIES (Notes 5 and 8)		
NET ASSETS:		
Invested in capital assets—net of related debt	16,177,138	13,109,868
Restricted for debt service	2,100,038	5,066,053
Unrestricted	<u>20,595,020</u>	<u>17,005,032</u>
Total net assets	<u>38,872,196</u>	<u>35,180,953</u>
TOTAL	<u>\$ 83,120,267</u>	<u>\$ 78,596,757</u>

See notes to consolidated financial statements.

SLIDELL MEMORIAL HOSPITAL

CONSOLIDATED STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
REVENUE:		
Net patient service revenue	\$ 105,800,053	\$ 99,863,289
Other revenue	<u>2,148,585</u>	<u>2,196,958</u>
Total revenue	<u>107,948,638</u>	<u>102,060,247</u>
OPERATING EXPENSES:		
Salaries and wages	35,553,138	32,704,710
Employee benefits	9,155,974	9,757,611
Supplies and materials	19,260,896	17,731,419
Other direct expenses	10,359,244	8,872,850
Professional fees	6,555,819	5,724,410
Purchased services	5,782,524	6,951,904
Provision for bad debts	10,266,975	10,198,468
Depreciation and amortization	<u>6,458,995</u>	<u>6,880,106</u>
Total expenses	<u>103,393,565</u>	<u>98,821,478</u>
OPERATING INCOME	4,555,073	3,238,769
NONOPERATING REVENUES (EXPENSES):		
Interest income	341,620	189,977
Interest expense	(1,986,621)	(1,960,320)
Property tax revenue	2,100,000	
Expenses related to debt restructuring and related referendums	<u>(1,318,829)</u>	<u>(628,705)</u>
Total non-operating expenses—net	<u>(863,830)</u>	<u>(2,399,048)</u>
INCREASE IN NET ASSETS	3,691,243	839,721
NET ASSETS—Beginning of year	<u>35,180,953</u>	<u>34,341,232</u>
NET ASSETS—End of year	<u>\$ 38,872,196</u>	<u>\$ 35,180,953</u>

See notes to consolidated financial statements.

SLIDELL MEMORIAL HOSPITAL

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
OPERATING ACTIVITIES:		
Cash received from patient services	\$ 98,018,229	\$ 86,086,277
Cash paid to or on behalf of employees	(44,253,179)	(42,120,120)
Cash paid for supplies and services	<u>(42,797,384)</u>	<u>(35,886,820)</u>
Net cash provided by operating activities	<u>10,967,666</u>	<u>8,079,337</u>
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of capital assets	(3,210,554)	(1,743,945)
Principal payments on long-term debt and capital lease obligations	(28,426,793)	(4,519,011)
Proceeds from issuance of bonds	22,320,000	
Payment of deferred financing costs	(146,458)	
Premium paid on advance refunding	(436,700)	
Interest payments	(1,778,689)	(1,991,952)
Proceeds from sale of capital assets	336,445	362,204
Other—net	<u>(148,254)</u>	<u> </u>
Net cash used in capital and related financing activities	<u>(11,491,003)</u>	<u>(7,892,704)</u>
INVESTING ACTIVITIES:		
Decrease in assets whose use is limited or restricted	4,997,213	341,504
Interest earned on investments	<u>368,585</u>	<u>196,680</u>
Net cash provided by investing activities	<u>5,365,798</u>	<u>538,184</u>
INCREASE IN CASH AND CASH EQUIVALENTS	4,842,461	724,817
CASH AND CASH EQUIVALENTS—Beginning of year	<u>5,537,144</u>	<u>4,812,327</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 10,379,605</u>	<u>\$ 5,537,144</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ 4,555,073	\$ 3,238,769
Adjustments to reconcile operating income to net cash provided by operating activities:		
Provision for bad debts	10,266,975	10,198,468
Depreciation and amortization	6,458,995	6,880,106
Loss (gain) on sale of capital assets	61,577	(95,772)
Expenses related to restructuring		(628,705)
Changes in operating assets and liabilities:		
Patient accounts receivable	(8,196,649)	(14,246,565)
Inventories and other operating assets	369,678	(35,201)
Accounts payable and accrued expenses	<u>(2,547,983)</u>	<u>2,768,237</u>
Net cash provided by operating activities	<u>\$ 10,967,666</u>	<u>\$ 8,079,337</u>

See notes to consolidated financial statements.

SLIDELL MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2004 AND 2003

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization—St. Tammany Parish Hospital Service District No. 2 (the District), d/b/a Slidell Memorial Hospital (the Hospital), is a nonprofit corporation organized as a political subdivision of the State of Louisiana as established in Act 180 of the 1984 Regular Session of the Legislature and as amended by Act 999 of the 1991 Regular Session of the Legislature, Act 570 of the 1992 Regular Session of the Legislature, Act 440 of the 1997 Regular Session of the Legislature, and Act 562 of the 2003 Regular Session of the Legislature. Act 562 created a nominating committee to solicit, interview and make nominations for appointment to the Board of Commissioners. The legislation sets forth an appointing authority of the District, which is a cross-section of representatives of city, parish and state government bodies. The appointing authority appoints the Board of Commissioners from the nominations put forth by the nominating committee. The St. Tammany Parish Hospital Service District No. 2 Board of Commissioners (the Board) is authorized to oversee the assets and govern the operations of the Hospital.

Principles of Consolidation—The consolidated financial statements include the accounts and transactions of the Hospital and its member organizations, Slidell Memorial Health Foundation, Inc. (SMH Foundation), SMH Physician Practice Services, Inc. (Physician Practice Services) and Slidell Radiation Center, Inc. (SRC). All material intercompany accounts and transactions have been eliminated in consolidation.

Basis of Accounting—The Hospital utilizes the accrual basis of accounting for proprietary funds. Under Governmental Accounting Standards Board Statement (GASBS) No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Activities That Use Proprietary Fund Accounting*, the Hospital has elected not to apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989.

Income Tax Status—The Hospital is exempt from federal income tax under both Section 115 of the Internal Revenue Code as a governmental entity and Section 501(a) as a hospital organization as described in Section 501(c)(3). The exemption from federal income taxes also extends to state income taxes. SMH Foundation has been designated as a not-for-profit organization described in Internal Revenue Code Section 501(c)(3) and is exempt from federal income taxation under Internal Revenue Code Section 501(a). Physician Practice Services and SRC are taxable not-for-profit corporations.

Net Patient Service Revenue and Related Receivables—Net patient service revenue and the related accounts receivable are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. The Hospital provides care to patients even though they may lack adequate insurance or may be covered under contractual arrangements that do not pay full charges. As a result, the Hospital is exposed to certain credit risks. The Hospital manages such risk by regularly reviewing its accounts and contracts, and by providing appropriate allowances.

Medicare and Medicaid Reimbursement Programs—The Hospital is reimbursed under the Medicare Prospective Payment System (PPS) for acute care inpatient services provided to Medicare beneficiaries and is paid a predetermined amount for these services based, for the most part, on the Diagnosis Related Group (DRG) assigned to the patient. In addition, the Hospital is paid prospectively for Medicare inpatient capital costs based on the federal specific rate. The Hospital qualifies as a disproportionate share provider under the Medicare regulations. As such, the Hospital receives an additional payment for Medicare inpatients served. Except for Medicare disproportionate share reimbursement and Medicare bad debts, there is no retroactive settlement for inpatient costs under the Medicare inpatient prospective payment methodology.

The Hospital is paid a prospective per diem rate for Medicaid inpatients. The per diem rate is based on a peer grouping methodology which assigns a per diem rate to each hospital in the peer group.

Medicaid outpatient services (excluding ambulatory surgery and clinical lab), and Medicare bad debts are reimbursed on a cost basis. Outpatient services rendered to Medicare beneficiaries are reimbursed by the Outpatient Prospective Payment System (OPPS) which establishes a number of Ambulatory Payment Classifications (APC) for outpatient procedures in which the Hospital is paid a predetermined amount per procedure. Medicare and Medicaid outpatient clinical lab and Medicaid ambulatory surgery services are reimbursed based upon the respective fee schedules.

Retroactive cost settlements based upon annual cost reports are estimated for those programs subject to retroactive settlement and recorded in the consolidated financial statements. Final determination of retroactive cost settlements to be received under the Medicare and Medicaid regulations is subject to review by program representatives. The difference between a final settlement and an estimated settlement in any year is reported as an adjustment of net patient service revenue in the year the final settlement is made.

Cash and Cash Equivalents—Cash and cash equivalents are recorded at fair value. The Hospital reports short-term, highly liquid investments (that are both readily convertible to known amounts of cash and mature within three months or less from date of purchase) as cash equivalents, excluding amounts classified as assets whose use is limited or restricted on the consolidated balance sheet. As of December 31, 2004 and 2003, the Hospital's cash, cash equivalents and certificates of deposit were entirely insured or collateralized with securities held by its agent in the Hospital's name.

Assets Whose Use is Limited or Restricted—Assets whose use is limited or restricted consists of investments reported at fair value with gains and losses included in the consolidated statements of revenue, expenses and changes in net assets.

Inventories—Inventories are valued at the lower of cost (first-in, first-out method) or market.

Capital Assets—Land, buildings and equipment acquisitions are recorded at cost except for assets donated to the Hospital. Donated assets are recorded at the fair value of the assets at the date of donation. Depreciation of buildings and equipment is computed using the straight-line method in amounts sufficient to amortize the cost of these assets over their estimated useful lives.

Equipment held under capital lease obligations has been recorded at the present value of the minimum lease payments. Amortization of leased assets is included in depreciation and amortization expense.

Other Assets—At December 31, 2004, other assets consists of unamortized bond issuance costs on the 2004 general obligation bonds of \$141,587 (net of accumulated amortization of \$4,180). At December 31, 2003, other assets consisted of the unamortized bond issuance costs on the 1994, 1996 and 1999 revenue bonds of \$941,398 and the unamortized balance of goodwill amounting to \$564,546 related to the 1999 acquisition of the Slidell Radiation Center. The original goodwill recognized on the purchase amounted to \$1,350,000, which amount was being amortized over an eight year period. The balance of goodwill was written off in 2004.

Employee Health and Workers' Compensation Insurance—The Hospital is self-insured for hospitalization and workers' compensation claims. Estimated amounts for claims incurred but not reported are calculated based on claims experience and, together with unpaid claims, are included in accrued interest and other expenses on the consolidated balance sheets.

Statements of Revenue, Expenses and Changes in Net Assets—All revenues and expenses directly related to the delivery of health care services are included in operating revenues and expenses in the statement of revenue, expenses and changes in net assets. Non-operating revenues and expenses consist of those revenues and expenses that are related to financing and investing types of activities and result from non-exchange transactions or investment income.

Property Tax Revenues—As a result of a voter referendum in 2003, the Hospital began receiving dedicated property tax revenues in 2004 in amounts sufficient to fund annual debt maturities of the general obligation bonds and related interest costs (see Note 6). Such revenues are considered nonoperating in the accompanying statement of revenue, expenses and changes in net assets. Unexpended property tax revenues are accumulated in a restricted fund and are used exclusively for debt service.

Use of Estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. The determination of the allowance for uncollectible accounts receivable and amounts estimated to be recovered from third party payors are particularly sensitive estimates subject to change.

Net Assets—In accordance with Governmental Accounting Standards Board Statement (GASBS) No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, net assets are classified into three components – invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- **Invested in capital assets, net of related debt**—This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- **Restricted**—This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- **Unrestricted**—This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

2. ASSETS WHOSE USE IS LIMITED OR RESTRICTED

The terms of the Hospital's bond issues require certain funds to be maintained on deposit with the trustee. The funds on deposit with the trustee and funds designated by the Board for capital improvements as of December 31 were as follows:

	2004	2003
Current assets:		
Under bond indenture:		
Bond debt service account	\$ -	\$ 1,167,307
Dedicated property tax revenue	939,657	
	<u>\$ 939,657</u>	<u>\$ 1,167,307</u>
Noncurrent assets:		
Under bond indenture:		
Debt service reserve account	\$ -	\$ 3,898,746
Dedicated property tax revenue	1,160,381	
Equipment acquisition funds related to municipal leases	6,750,000	
By board:		
Designated for capital improvements	3,613,892	3,550,090
By donors	29,185	24,185
	<u>\$ 11,553,458</u>	<u>\$ 7,473,021</u>

Statutes authorize the Hospital to invest in direct obligations of the U.S. Government, certificates of deposit of state banks and national banks having their principal office in the State of Louisiana, and any other federally insured investments, guaranteed investment contracts issued by a financial institution having one of the two highest rating categories published by Standard & Poor's or Moody's, and mutual or trust fund institutions registered with the Securities and Exchange Commission (provided the underlying investments of these funds meet certain restrictions). The Hospital's funds were invested in certificates of deposit and U.S. Government obligations carried at fair value at December 31, 2004 and 2003.

During fiscal 2001, the Board granted management discretion to utilize for other operating purposes those funds designated for capital improvements. Management has continued to maintain these funds in a separate trust account and treat them as internally designated funds.

3. THIRD-PARTY PAYOR ARRANGEMENTS

The Hospital participates in the Medicare and Medicaid programs as a provider of medical services to program beneficiaries. During the years ended December 31, 2004 and 2003, approximately 49% of the Hospital's gross patient service charges were derived from services provided to Medicare and Medicaid program beneficiaries. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Revenue derived from the Medicare program is subject to audit and adjustment by the fiscal intermediary and must be accepted by the United States Department of Health and Human Services before settlement amounts become final. Revenue derived from the Medicaid program is subject to audit and adjustment and must be accepted by the State of Louisiana, Department of Health and Hospitals before the settlement amounts become final. The fiscal intermediary has completed its review of estimated Medicare settlements for fiscal years ended through December 31, 2000 and Medicaid settlements for fiscal years ended through December 31, 1998. Annually, management evaluates the recorded estimated settlements and adjusts these balances based upon the results of the intermediary's audit of filed cost reports and additional information becoming available. Although the fiscal intermediary has not completed its audits of the estimated settlements for the years ended December 31, 2001 through December 31, 2004 for Medicare and December 31, 1999 through December 31, 2004 for Medicaid, the Hospital does not anticipate significant adverse adjustments to the recorded settlements for those years.

The Hospital has also entered into payment agreements with certain commercial insurance carriers and *managed care organizations*. The basis for payment to the Hospital under these arrangements includes prospectively determined daily rates and discounts from established charges.

4. COMMUNITY BENEFITS

As a community health care provider, the Hospital's stated mission is to "serve the community through a commitment to excellence in patient care." As such, total revenue includes that revenue generated from direct patient care, rentals from various medical office buildings, and sundry revenue related to the operation of the Hospital and its member organizations.

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care provided during the years ended December 31, 2004 and 2003, measured at established rates, totaled \$9,145,789, net of a \$0 government subsidy, and \$8,297,522, net of a \$722,000 government subsidy, respectively.

In addition, the Hospital sponsors or participates in numerous activities to benefit the community. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. The Hospital has conducted a Community Health Assessment to identify health risks in the community. Through this research, the Hospital has developed wellness and prevention programs that target these high-risk areas for a healthier community.

Annually, the Hospital sponsors several health fairs and programs regarding such issues as diabetes, breast cancer, prostate cancer, smoking cessation, nutrition, exercise, cardiology, women's health, parenting skills, development topics, etc., to provide the community access to health-related information. Also, the Hospital provides health screening at no cost or a reduced cost to the community. Some health screenings include prostate cancer, cholesterol, colorectal, skin cancer, glucose, and thyroid screenings.

The Hospital encourages its employees to volunteer for charitable organizations and to participate in fund-raising activities and, in some cases, pays employees to perform public services such as health screenings. In addition, the Hospital aided various community service organizations through donations and sponsorships.

5. LEASES

The Hospital leases medical and administrative equipment under operating leases with terms that vary from month-to-month to five years. Total rental expense included in other direct expenses on the consolidated statements of revenue, expenses and changes in net assets was \$1,050,576 and \$1,121,435 for the years ended December 31, 2004 and 2003, respectively.

The Hospital also leases medical equipment under lease agreements accounted for as capital lease obligations in accordance with Financial Accounting Standards Board Statement No. 13, *Accounting for Leases*. These capital lease obligations expire at various dates through 2010. The capital asset balances on the consolidated balance sheets include equipment under capital lease obligations of \$4,934,374 and \$2,451,955, less accumulated amortization of \$2,192,139 and \$1,691,191 at December 31, 2004 and 2003, respectively. In addition, equipment acquisition funds have been set aside in assets whose use is limited or restricted amounting to \$6,750,000 related to Louisiana municipal leases negotiated in December, 2004. Such municipal leases are included in the capital leases set forth below. Such amounts are scheduled for expenditure in 2005. During the year ended December 31, 2004, the Hospital entered into new capitalized leases amounting to approximately \$9.45 million for equipment purchases of which \$6.75 million remained unexpended at December 31, 2004.

The future minimum lease payments at December 31, 2004 for noncancelable leases are as follows:

	Operating Leases	Capital Leases
2005	\$ 636,446	\$ 2,209,684
2006	549,889	2,209,684
2007	376,033	1,890,755
2008	32,096	1,712,812
2009	21,397	1,320,673
Thereafter	<u> </u>	<u>1,981,187</u>
	<u>\$1,615,861</u>	11,324,795
Amounts representing imputed interest (interest rates range from 3.9% to 5.67%)		<u>1,232,764</u>
Present value of capital lease obligations (including \$1,850,152 classified as amounts due within one year)		<u>\$10,092,031</u>

The Hospital leases space to physicians through a combination of cancelable and noncancelable lease agreements. Rental income earned under these agreements was \$1,261,300 and \$1,241,335 for the years ended December 31, 2004 and 2003.

The future minimum lease payments to be received from noncancelable lease agreements at December 31, 2004 are as follows:

	Operating Leases
2005	\$1,215,615
2006	1,013,306
2007	659,709
2008	474,662
2009	165,805
Thereafter	<u>230,193</u>
	<u>\$3,759,290</u>

6. LONG-TERM DEBT

The details and balances of long-term debt at December 31 are presented below:

	2004	2003
Hospital Revenue Bonds, Series 1994, described in detail below (refunded October 4, 2004)	\$ -	\$23,400,000
Hospital Revenue Bonds, Series 1996, described in detail below (refunded July 29, 2004)		2,742,239
Hospital Revenue Bonds, Series 1999, described in detail below (refunded July 29, 2004)		1,477,567
General Obligation Bonds, Series 2004A, described in detail below (\$15,000 due in 2005)	8,000,000	
General Obligation Bonds, Series 2004B, described in detail below (\$325,000 due in 2005)	13,115,000	
General Obligation Bonds, Series 2004C, described in detail below (\$25,000 due in 2005)	1,205,000	
Notes payable to physicians, 7% (\$170,000 due in 2005)	<u>850,000</u>	<u>1,020,000</u>
	23,170,000	28,639,806
Less amounts due within one year according to terms of debt instruments	535,000	4,013,873
Additional amounts classified as current due to planned 2004 refinancing		<u>15,775,933</u>
	<u>\$22,635,000</u>	<u>\$ 8,850,000</u>

The following table summarizes the changes in long-term debt for the year ended December 31, 2004:

Balance of long-term debt at December 31, 2003	\$ 28,639,806
Less: Retirement of revenue bonds due to refinancing	(27,619,806)
Repayment of notes payable	(170,000)
Add: Issuance of general obligation bonds	<u>22,320,000</u>
Balance of long-term debt at December 31, 2004	<u>\$ 23,170,000</u>

Refinancing—In October 2003, the voters of St. Tammany Parish approved a referendum authorizing the Hospital to issue up to \$22.45 million of general obligation bonds in 2004 which would be secured by the pledge of dedicated property tax millages set annually at rates sufficient to fund principal maturities and interest on the related bonds. The Hospital issued three series of general obligation bonds in 2004 to refinance the balances of 1994, 1996 and 1999 revenue bonds. In connection with the refinancing, the Hospital incurred a loss of \$1,318,829 consisting of redemption premiums of \$436,700 related to calling the revenue bonds prior to their original maturities and \$882,129 related to writing off the remaining balance of unamortized bond issuance costs which arose from the original issuance of the revenue bonds.

General Obligation Bonds—On March 31, 2004, the Hospital issued \$8 million in General Obligation Bonds with a interest rates ranging from 2% to 5% to advance refund \$9.24 million of outstanding Hospital Revenue Bonds, Series 1994. The net proceeds of \$7.9 million (after payment of underwriting fees, insurance, and other issuance costs) plus an additional \$1.99 million of existing sinking fund and debt service reserve monies were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the portion of the 1994 bonds until the bonds were advance refunded on October 4, 2004.

On July 29, 2004, the Hospital issued \$13.115 million in General Obligation Bonds with interest rates ranging from 4.125% to 6% to advance refund the remaining \$14.16 million of outstanding 1994 Revenue Bonds and all of the \$691,885 outstanding Hospital Revenue Bonds, Series 1996. The net proceeds of \$13 million (after payment of underwriting fees, insurance, and other issuance costs) plus an additional \$2.5 million of existing sinking fund and debt service reserve monies were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1994 bonds until the amount were advance refunded on October 4, 2004. The entire amount of the Series 1996 Bonds were refunded on July 29, 2004.

On July 29, 2004, the Hospital issued \$1.205 million in General Obligation Bonds with interest rates ranging from 5.8% to 8% to advance refund \$2.2 million of outstanding 1999 Revenue Bonds. The net proceeds of \$1.2 million (after payment of underwriting fees, insurance, and other issuance costs) plus an additional \$1 million of existing debt service reserve monies were deposited in an irrevocable trust with an escrow agent to provide for the advance refunding on July 29, 2004.

Interest on the general obligation bonds is payable semi-annually on March 1 and September 1 each year. The bonds mature in annual installments on March 1 each year from 2005-2024. The bonds can be called for early redemption after March 1, 2014.

Hospital Revenue Bonds—On May 5, 1994, the Hospital issued \$35 million of Hospital Revenue Bonds, Series 1994 (the 1994 Revenue Bonds) to finance the cost of constructing improvements to the Hospital and to defease or liquidate outstanding debt. The bonds were collateralized by a pledge of the Hospital's revenue. The bonds carried interest rates ranging from 5.5% to 6.25% and matured at various dates through 2014. The bonds were subject to redemption prior to maturity, at the option of the Hospital, on or after October 1, 2004, in whole or in part with premiums of up to 2% of the principal balance.

On October 7, 1996, the Hospital issued \$8 million of Hospital Revenue Bonds, Series 1996 (the 1996 Revenue Bonds) to finance the cost of constructing improvements to the Hospital. The 1996 Revenue Bonds bore interest at 5.7% and were payable monthly in equal installments of principal and interest totaling \$87,533. The 1996 Revenue Bonds were subject to the 1994 Trust Indenture and were issued on a parity with the outstanding 1994 Revenue Bonds. The 1996 Revenue Bonds were subject to redemption prior to maturity, at the option of the Hospital, at any time, in whole or in part with a defined prepayment penalty.

On December 27, 1999, the Hospital issued \$6.2 million of Hospital Revenue Bonds, Series 1999 (the 1999 Revenue Bonds) to finance the acquisition and construction of improvements, renovations and extensions to the Hospital, including, but not limited to, routine capital expenditures for information technology upgrades, radiation oncology vault and other capital equipment. The 1999 Revenue Bonds bore interest at 5% and were payable monthly in equal installments of principal and interest totaling \$117,002 through January 1, 2005. The 1999 Bonds are subject to the 1994 Trust Indenture and were issued in parity with the outstanding 1994 Revenue Bonds. The 1999 Revenue Bonds were subject to redemption prior to maturity, at the option of the Hospital, at any time, in whole or in part with a defined prepayment penalty.

As a result of the issuance of the general obligation bonds in 2004, all revenue bonds were redeemed as described above.

Bond Covenant Violations—In connection with the 1994 Revenue Bonds, the Hospital purchased a bond insurance policy issued by Ambac Assurance Corporation (Ambac) (formerly Connie Lee Insurance Company) which guaranteed the scheduled payment of principal and interest on the 1994 Revenue Bonds. Also, the Hospital entered into a Trust Indenture with First National Bank of Commerce (now J.P. Morgan Trust) which stipulated certain terms and covenants, for example, maintenance of certain financial ratios with which the Hospital must comply. The Hospital was not in compliance with the covenants related to debt service coverage and days of cash on hand as of December 31, 2000. The Hospital maintained compliance in 2001 and thereafter and believes that such actions remedied the covenant violations in 2000. All required payments of principal maturities and interest were paid timely by the Hospital. The Hospital entered into negotiations with Ambac during 2001 to waive the covenant violations as of December 31, 2000 and modify the defined bond covenants applicable to future years. Such negotiations extended from 2001 through 2003 but the parties were unable to negotiate a mutually satisfactory settlement. As a result of the redemption of the revenue bonds in 2004, the issue of the bond covenant violation and the Hospital's position that such violation had been remedied became moot.

Notes Payable to Physicians—On March 1, 1999, the Hospital acquired all the membership rights of Slidell Radiation Center, a non-profit membership corporation. The Hospital issued \$1,700,000 in notes payable which bear an annual interest rate of 7% and are payable in annual installments of principal and interest of approximately \$170,000 over a period of ten years.

Combined Debt Service Commitments—Principal and interest payments due on general obligation bonds and notes payable are as follows:

Year Ended December 31	Principal	Interest
2005	\$ 535,000	\$ 1,381,480
2006	920,000	1,122,170
2007	950,000	1,078,608
2008	990,000	1,034,705
2009	1,030,000	991,785
2010-2014	4,995,000	3,698,220
2015-2019	6,340,000	2,497,889
2020-2024	<u>7,410,000</u>	<u>878,478</u>
	<u>\$23,170,000</u>	<u>\$12,683,335</u>

7. EMPLOYEE BENEFITS

The Hospital and its member organizations maintained a qualified noncontributory defined contribution pension plan which provided pension benefits for eligible employees through March of 2002. Beginning in April of 2002, the Hospital began a combination deferred compensation and contributory employee savings plan for full-time employees. Each employee's interest in the existing plan is fully vested and was transferred over to the new plan. The new pension plan provides an employer match of employee contributions (up to 8%) rather than contributions based on salaries. Employees are eligible to participate at their date of hire.

Participants are immediately vested in their contributions plus actual earnings thereon. Vesting in the Hospital's contribution is based on years of service. The following vesting schedule is in effect:

Years of Vesting Service	Percent Vested
1	20%
2	40%
3	60%
4	80%
5	100%

The total payroll for the years ended December 31, 2004 and 2003 was \$35,553,138 and \$32,704,710, respectively. During the years ended December 31, 2004 and 2003, the Hospital and member organizations made required contributions to the Plan of \$919,775 and \$796,862, respectively.

8. RISK MANAGEMENT

The Hospital is involved in litigation arising in the ordinary course of business. Claims alleging malpractice have been asserted against the Hospital and are currently in various stages of litigation. The Hospital participates in the Louisiana Hospital Association Trust Fund ("LHA Trust Fund") and the Louisiana Patients' Compensation Fund ("Compensation Fund") for insurance coverage on medical malpractice claims. As a participant, the Hospital has a statutory limitation of liability which provides that no award can be rendered against it in excess of \$500,000, plus interest and costs. The LHA Trust Fund provides malpractice coverage for claims up to \$100,000 and the Compensation Fund provides an

additional \$400,000 of coverage. These funds provide the Hospital with malpractice coverage on an occurrence basis up to the \$500,000 statutory limitation. Hospital management has no reason to believe that the Hospital will be prevented from continuing its participation in the Fund. LHA Trust Fund insures general liability up to \$1,000,000 per claim. LHA Trust Fund insures excess general liability claims in excess of \$1,000,000 but limited to \$9,000,000 per claim. At December 31, 2004, there were no malpractice accruals, and the Hospital is fully insured based on the statutory limits. Additional claims may be asserted against the Hospital arising from services provided to patients through December 31, 2004 exceeding these coverage limits. The Hospital is unable to determine the ultimate cost of the resolution of such potential claims and, accordingly, no accrual has been made for them.

The Hospital is self-insured for workers' compensation up to \$300,000 per claim, and employee health up to \$120,000 per claim. A liability is recorded when it is probable that a loss has been incurred and the amount of that loss can be reasonably estimated. Liabilities for claims incurred are reevaluated periodically to take into consideration recently settled claims, frequency of claims and other economic and social factors. The Hospital carries commercial insurance which provides coverages for workers' compensation and employee health claims in excess of the self-insured limits.

Changes in the Hospital's aggregate claims liability for workers' compensation and employee health for the years ended December 31, 2004 and 2003 were as follows:

Year Ended December 31	Beginning of year Liability	Current Year Claims and Changes in Estimates	Claim Payments	Balance at Year End
2004	\$ 926,979	\$ 7,478,743	\$ 7,658,403	\$ 747,049
2003	\$ 720,258	\$ 6,200,673	\$ 5,993,952	\$ 926,979

9. CONCENTRATIONS OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third party payor agreements. The mix of receivables from patients and third party payors net of contractual allowances at December 31 was as follows:

	2004	2003
Medicare	12 %	14 %
Medicaid	2	9
Insurance/managed care	31	35
Patients	54	38
Other	1	4
	<u>100 %</u>	<u>100 %</u>

10. CHANGES IN CAPITAL ASSETS

Capital asset activity for the fiscal year ended December 31, 2004, was as follows:

	Balance December 31, 2003	Additions	Deletions	Balance December 31, 2004
Capital assets not being depreciated:				
Land	\$ 3,597,713	\$ -	\$ -	\$ 3,597,713
Capital assets being depreciated:				
Land improvements	1,077,870			1,077,870
Buildings	62,171,994	282,044	247,429	62,206,609
Equipment	47,820,514	5,634,136	5,489,087	47,965,563
Total capital assets being depreciated	111,070,378	5,916,180	5,736,516	111,250,042
Less accumulated depreciation for:				
Land improvements	831,467	28,090		859,557
Buildings	30,968,761	2,696,577	247,429	33,417,909
Equipment	40,688,282	3,133,903	5,091,065	38,731,120
Total accumulated depreciation	72,488,510	5,858,570	5,338,494	73,008,586
Total capital assets being depreciated—net	38,581,868	57,610	398,022	38,241,456
Total capital assets—net	\$ 42,179,581	\$ 57,610	\$ 398,022	\$ 41,839,169

* * * * *

ADDITIONAL INFORMATION

INDEPENDENT AUDITORS' REPORT ON ADDITIONAL INFORMATION

Members of the Board of Commissioners
St. Tammany Parish Hospital Service District No. 2:

Our audits were conducted for the purpose of forming an opinion on the basic consolidated 2004 and 2003 financial statements taken as a whole. The following additional information, as listed on the table of contents, is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. This information is the responsibility of St. Tammany Parish Hospital Service District No. 2's management. Such information, except for the page marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

Deloitte & Touche LLP

March 19, 2005

SLIDELL MEMORIAL HOSPITAL

CONSOLIDATING SCHEDULE—BALANCE SHEET INFORMATION DECEMBER 31, 2004

ASSETS	Consolidated	Eliminations	Slidell Memorial Hospital	Slidell Memorial Health Foundation, Inc.	SMH Physician Practice Services, Inc.	Slidell Radiation Center, Inc.
CURRENT ASSETS:						
Cash and cash equivalents	\$ 10,379,605		\$ 10,317,909	\$ 1,726	\$ 21,020	\$ 38,950
Patient accounts receivable—net	15,179,996		15,150,233		29,763	
Assets whose use is limited—required for current liabilities	939,657		939,657			
Inventories	1,971,553		1,958,741	506	12,306	
Intercompany receivables		\$ (6,580,266)	6,580,266			
Prepaid expenses and other receivables	1,115,242		1,068,508	44,379	2,355	
Total current assets	29,586,053	(6,580,266)	36,015,314	46,611	65,444	38,950
ASSETS WHOSE USE IS LIMITED OR RESTRICTED:						
By board or under agreements for capital improvements and debt service and by donors	11,553,458		11,524,273	29,185		
CAPITAL ASSETS:						
Land and improvements	4,675,583		4,675,583			
Buildings	62,206,609		62,206,609			
Equipment	47,965,563		47,726,853		45,710	193,000
Less accumulated depreciation and amortization	(73,008,586)		(72,840,066)		(37,306)	(131,214)
Total capital assets—net	41,839,169		41,768,979		8,404	61,786
OTHER ASSETS:						
Investment in affiliated organizations		(100,736)	100,736			
Bond issuance costs—net	141,587		141,587			
Total other assets	141,587	(100,736)	242,323			
TOTAL	\$ 83,120,267	\$ (6,681,002)	\$ 89,550,889	\$ 75,796	\$ 73,848	\$ 100,736

(Continued)

SLIDELL MEMORIAL HOSPITAL

CONSOLIDATING SCHEDULE—BALANCE SHEET INFORMATION DECEMBER 31, 2004

	Consolidated	Eliminations	Slidell Memorial Hospital	Slidell Memorial Health Foundation, Inc.	SMH Physician Services, Inc.	Slidell Radiation Center, Inc.
LIABILITIES AND NET ASSETS						
CURRENT LIABILITIES:						
Trade accounts payable	\$ 3,959,286	\$ (6,580,266)	\$ 3,959,286	\$ 700,701	\$ 5,879,565	
Intercompany payables	1,314,382		1,314,382			
Salaries, wages and benefits payable	1,397,126		1,397,126			
Accrued vacation payable	2,946,671		2,942,918		3,753	
Accrued interest and other expenses	1,368,575		1,368,575			
Amounts due to third-party payors						
Amounts due within one year on capital lease obligations and long-term debt	<u>2,385,152</u>		<u>2,385,152</u>			
Total current liabilities	<u>13,371,192</u>	<u>(6,580,266)</u>	<u>13,367,439</u>	<u>700,701</u>	<u>5,883,318</u>	
CAPITAL LEASE OBLIGATIONS—less amounts due within one year	8,241,879		8,241,879			
LONG-TERM DEBT—less amounts due within one year	22,635,000		22,635,000			
NET ASSETS:						
Invested in capital assets—net of related debt	16,177,138	(61,786)	16,168,734		8,404	\$ 61,786
Restricted for debt service	2,100,038		2,100,038			
Unrestricted (deficit)	<u>20,595,020</u>	<u>(38,950)</u>	<u>27,037,799</u>	<u>(624,905)</u>	<u>(5,817,874)</u>	<u>38,950</u>
Total net assets	<u>38,872,196</u>	<u>(100,736)</u>	<u>45,306,571</u>	<u>(624,905)</u>	<u>(5,809,470)</u>	<u>100,736</u>
TOTAL	<u>\$83,120,267</u>	<u>\$(6,681,002)</u>	<u>\$89,550,889</u>	<u>\$ 75,796</u>	<u>\$ 73,848</u>	<u>\$ 100,736</u>

(Concluded)

SLIDELL MEMORIAL HOSPITAL

CONSOLIDATING SCHEDULE—REVENUE, EXPENSES AND CHANGES IN NET ASSETS INFORMATION YEAR ENDED DECEMBER 31, 2004

	Consolidated	Eliminations	Slidell Memorial Hospital	Slidell Memorial Health Foundation, Inc.	SMH Physician Practice Services, Inc.	Slidell Radiation Center, Inc.
REVENUE:						
Net patient service revenue	\$ 105,800,053	\$ -	\$ 105,187,466	\$ 170,031	\$ 442,556	\$ -
Other revenue	<u>2,148,585</u>		<u>2,143,567</u>	<u>5,018</u>		
Total revenue	<u>107,948,638</u>		<u>107,331,033</u>	<u>175,049</u>	<u>442,556</u>	
OPERATING EXPENSES:						
Salaries and wages	35,553,138		35,169,670	122,400	261,068	
Employee benefits	9,155,974		9,130,989	8,697	16,288	
Supplies and materials	19,260,896		19,247,003	2,628	11,265	
Other direct expenses	10,359,244		10,296,685	13,106	49,453	
Professional fees	6,555,819		6,537,119		18,700	
Purchased services	5,782,524		5,732,727		49,797	
Provision for bad debts	10,266,975	202	10,267,247		(272)	(202)
Depreciation and amortization	<u>6,458,995</u>	<u>(27,571)</u>	<u>6,456,344</u>		<u>2,651</u>	<u>27,571</u>
Total expenses	<u>103,393,565</u>	<u>(27,369)</u>	<u>102,837,784</u>	<u>146,831</u>	<u>408,950</u>	<u>27,369</u>
OPERATING INCOME	4,555,073	27,369	4,493,249	28,218	33,606	(27,369)
NONOPERATING REVENUES (EXPENSES):						
Interest income	341,620		339,066			
Interest expense	(1,986,621)		(1,986,621)	1,661	893	
Property tax revenue	2,100,000		2,100,000			
Expenses related to debt restructuring and related referendums	<u>(1,318,829)</u>		<u>(1,318,829)</u>			
Total non-operating expenses	<u>(863,830)</u>		<u>(866,384)</u>	<u>1,661</u>	<u>893</u>	
INCREASE (DECREASE) IN NET ASSETS	3,691,243	27,369	3,626,865	29,879	34,499	(27,369)
NET ASSETS (DEFICIT)—Beginning of year	<u>35,180,953</u>	<u>(128,105)</u>	<u>41,679,706</u>	<u>(654,784)</u>	<u>(5,843,969)</u>	<u>128,105</u>
NET ASSETS (DEFICIT)—End of year	<u>\$ 38,872,196</u>	<u>\$ (100,736)</u>	<u>\$ 45,306,571</u>	<u>\$ (624,905)</u>	<u>\$ (5,809,470)</u>	<u>\$ 100,736</u>

Notes

1. The operations of Slidell Radiation Center, Inc. are included in the operating revenues and expenses of the Hospital.

SLIDELL MEMORIAL HOSPITAL

ADDITIONAL INFORMATION—SCHEDULE OF HOSPITAL DEPARTMENTAL GROSS MARGIN YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004				2003			
	Charges	Direct Operating Expenses	Charges Over Direct Expenses	Gross Margin	Charges	Direct Operating Expenses	Charges Over Direct Expenses	Gross Margin
ROUTINE SERVICES:								
Medical and surgical Intensive and intermediate care	\$ 23,749,390	\$ 6,975,358	\$ 16,774,032	70.6 %	\$ 22,140,436	\$ 6,803,873	\$ 15,336,563	69.3 %
Nursery and NICU	9,715,343	2,518,322	7,197,021	74.1	10,165,923	2,712,309	7,453,614	73.3
Long-term care	3,064,489	1,588,881	1,475,608	48.2	2,020,701	1,428,780	591,921	29.3
	<u>2,304,852</u>	<u>873,916</u>	<u>1,430,936</u>	62.1	<u>2,123,544</u>	<u>846,457</u>	<u>1,277,087</u>	60.1
	<u>38,834,074</u>	<u>11,956,477</u>	<u>26,877,597</u>	69.2	<u>36,450,604</u>	<u>11,791,419</u>	<u>24,659,185</u>	67.7
ANCILLARY SERVICES:								
Anesthesiology	14,672,925	4,270,262	10,402,663	70.9	13,324,496	3,925,547	9,398,949	71.3
Cardiac catheterization	25,996,776	3,430,269	22,566,507	86.8	28,191,869	3,610,661	24,581,208	87.2
Cardiology	7,347,091	545,173	6,801,918	92.6	5,941,967	522,294	5,419,673	91.2
CT Scan/MRI	24,673,533	1,375,153	23,298,380	94.4	18,833,676	1,355,602	17,478,074	92.8
Central services	30,894		30,894	100.0	49,021		49,021	100.0
Delivery room	4,513,758	1,172,730	3,341,028	74.0	3,214,899	1,063,128	2,151,771	66.9
Emergency room	23,191,241	4,645,289	18,545,952	80.0	21,348,994	4,482,538	16,866,456	79.0
Endoscopy	9,102,301	1,957,342	7,144,959	78.5	7,703,084	1,823,378	5,879,706	76.3
Home care services						(435)	435	
Hyperbaric oxygen	692,277	137,112	555,165	80.2	367,940	56,882	311,058	84.5
Laboratory	41,155,080	3,739,222	37,415,858	90.9	36,648,373	3,584,977	33,063,396	90.2
Nuclear medicine	6,389,071	609,114	5,779,957	90.5	4,507,532	483,795	4,023,737	89.3
Operating and recovery	58,316,905	8,801,034	49,515,871	84.9	53,992,356	8,041,987	45,950,369	85.1
Pharmacy	43,987,544	6,020,193	37,967,351	86.3	42,078,234	5,473,759	36,604,475	87.0
Physical therapy	8,740,720	1,709,470	7,031,250	80.4	7,806,633	1,461,680	6,344,953	81.3
Radiation oncology	6,459,637	1,512,407	4,947,230	76.6	6,265,911	1,448,145	4,817,766	76.9
Radiology	10,264,598	2,151,063	8,113,535	79.0	9,764,676	2,011,601	7,753,075	79.4
Respiratory therapy	18,283,705	1,840,812	16,442,893	89.9	18,236,587	1,807,796	16,428,791	90.1
Ultrasound	3,341,307	358,519	2,982,788	89.3	2,813,580	378,672	2,434,908	86.5
	<u>307,159,363</u>	<u>44,275,164</u>	<u>262,884,199</u>		<u>281,089,828</u>	<u>41,532,007</u>	<u>239,557,821</u>	
	<u>345,993,437</u>	<u>\$56,231,641</u>	<u>289,761,796</u>		<u>317,540,432</u>	<u>\$53,323,426</u>	<u>264,217,006</u>	
Provision for charity and contractual allowances	(240,805,971)		(240,805,971)		(218,323,137)		(218,323,137)	
Net patient service revenue	<u>\$ 105,187,466</u>				<u>\$ 99,217,295</u>			
Other revenue			2,482,633				2,404,431	
			<u>51,438,458</u>				<u>48,298,300</u>	
EXPENSES:								
General services			(6,187,795)				(5,261,053)	
Fiscal and administrative services			(23,694,757)				(22,619,434)	
Provision for bad debts			(10,267,247)				(10,206,480)	
Depreciation and amortization			(6,456,344)				(6,876,602)	
Interest expense			(1,986,621)				(1,960,320)	
Nonoperating expenses			781,171				(628,705)	
Excess of revenues over expenses			<u>\$ 3,626,865</u>				<u>\$ 745,706</u>	

SLIDELL MEMORIAL HOSPITAL

ADDITIONAL INFORMATION - SCHEDULE OF HOSPITAL PATIENT SERVICE CHARGES YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004		2003		Total	Percentage of Charges to Total Department Charges	
	Inpatient	Outpatient	Inpatient	Outpatient		2004	2003
ROUTINE SERVICES:							
Medical and surgical	\$ 22,910,271	\$ 839,119	\$ 21,341,970	\$ 798,466	\$ 22,140,436	61.2 %	60.7 %
Intensive and intermediate care	9,682,707	32,636	10,144,754	21,169	10,165,923	25.0	27.9
Nursery and NICU	3,064,489		2,020,701		2,020,701	7.9	5.5
Long-term care	2,304,852		2,123,544		2,123,544	5.9	5.8
	<u>37,962,319</u>	<u>871,755</u>	<u>35,630,969</u>	<u>819,635</u>	<u>36,450,604</u>	<u>100.0 %</u>	<u>100.0 %</u>
ANCILLARY SERVICES:							
Anesthesiology	10,419,084	4,253,841	9,499,331	3,825,165	13,324,496	4.8 %	4.7 %
Cardiac catheterization	21,587,851	4,408,925	22,496,303	5,695,566	28,191,869	8.5	10.0
Cardiology	3,241,597	4,105,494	2,696,603	3,245,364	5,941,967	2.4	2.1
CT Scan/MRI	6,895,613	17,777,920	5,198,122	13,635,554	18,833,676	8.0	6.7
Central services	30,894	30,894	48,231	790	49,021		
Delivery room	3,729,569	784,189	2,525,605	689,294	3,214,899	1.5	1.1
Emergency room	5,185,066	18,006,175	4,221,637	17,127,357	21,348,994	7.6	7.6
Endoscopy	1,781,549	7,320,752	1,485,618	6,217,466	7,703,084	3.0	2.7
Hyperbaric oxygen	132,914	559,363	79,124	288,816	367,940		
Laboratory	23,201,967	17,953,113	21,055,874	15,592,499	36,648,373	13.4	13.0
Nuclear medicine	2,667,467	3,721,604	1,798,217	2,709,315	4,507,532	2.1	1.6
Operating and recovery	35,382,818	22,934,087	32,576,993	21,415,363	53,992,356	19.0	19.2
Pharmacy	33,394,475	10,593,069	33,339,025	8,739,209	42,078,234	14.3	15.0
Physical therapy	4,560,450	4,180,270	4,187,347	3,619,286	7,806,633	2.8	2.8
Radiation oncology		6,459,637		6,265,911	6,265,911	3.3	3.5
Radiology	3,631,866	6,632,732	3,464,408	6,300,268	9,764,676	2.1	2.2
Respiratory therapy	15,522,046	2,761,659	15,688,262	2,548,325	18,236,587	6.0	6.5
Ultrasound	1,022,034	2,319,273	901,705	1,911,875	2,813,580	1.0	1.0
	<u>172,387,260</u>	<u>134,772,103</u>	<u>161,262,405</u>	<u>119,827,423</u>	<u>281,089,828</u>	<u>100.0 %</u>	<u>100.0 %</u>
	<u>\$210,349,579</u>	<u>\$135,643,858</u>	<u>\$196,893,374</u>	<u>\$120,647,058</u>	<u>\$317,540,432</u>		

SLIDELL MEMORIAL HOSPITAL

**ADDITIONAL INFORMATION—SCHEDULE OF HOSPITAL OPERATING EXPENSES
YEARS ENDED DECEMBER 31, 2004 AND 2003**

	2004				2003				Percentage of	
	Salaries, Wages and Benefits	Supplies and Materials	Other Direct Expenses	Total	Salaries, Wages and Benefits	Supplies and Materials	Other Direct Expenses	Total	2004	2003
ROUTINE SERVICES:										
Medical and surgical Intensive and intermediate care	\$ 6,487,370	\$ 420,187	\$ 67,801	\$ 6,975,358	\$ 6,296,653	\$ 449,568	\$ 57,652	\$ 6,803,873	58.3 %	57.7 %
Nursery and NICU	2,336,540	161,301	20,481	2,518,322	2,525,565	170,445	16,299	2,712,309	21.1	23.0
Long-term care	1,289,422	71,462	227,997	1,588,881	1,172,503	45,384	210,893	1,428,780	13.3	12.1
	716,344	23,441	134,131	873,916	691,273	23,033	132,151	846,457	7.3	7.2
	<u>\$ 10,829,676</u>	<u>\$ 676,391</u>	<u>\$ 450,410</u>	<u>\$ 11,956,477</u>	<u>\$ 10,685,994</u>	<u>\$ 688,430</u>	<u>\$ 416,995</u>	<u>\$ 11,791,419</u>	<u>100.0 %</u>	<u>100.0 %</u>
ANCILLARY SERVICES:										
Anesthesiology	\$ 1,857,347	\$ 245,699	\$ 2,167,216	\$ 4,270,262	\$ 1,696,184	\$ 208,910	\$ 2,020,453	\$ 3,925,547	9.6 %	9.5 %
Cardiac catheterization	480,224	2,799,420	150,625	3,430,269	456,244	2,957,553	196,864	3,610,661	7.7	8.7
Cardiology	485,324	26,402	33,447	545,173	471,266	23,557	27,471	522,294	1.2	1.3
CT Scan/MRI	712,399	341,833	320,921	1,375,153	609,013	269,566	477,023	1,355,602	3.1	3.3
Delivery room	992,154	134,184	46,392	1,172,730	916,450	106,419	40,259	1,063,128	2.6	2.6
Emergency room	2,063,422	271,563	2,310,304	4,645,289	1,908,564	204,277	2,369,697	4,482,538	10.5	10.8
Endoscopy	1,451,581	217,544	288,217	1,957,342	1,316,087	262,811	244,480	1,823,378	4.4	4.4
Home care services						(723)	288	(435)		
Hyperbaric oxygen		4,643	132,469	137,112		288	56,594	56,882	0.3	0.1
Laboratory	1,495,403	1,527,067	716,752	3,739,222	1,386,844	1,537,353	660,780	3,584,977	8.4	8.6
Nuclear medicine	173,994	369,988	65,132	609,114	170,965	244,742	68,088	483,795	1.4	1.2
Operating and recovery	1,918,678	6,063,034	819,322	8,801,034	1,966,682	5,275,849	799,456	8,041,987	19.9	19.4
Pharmacy	784,687	4,953,465	282,041	6,020,193	761,195	4,451,826	260,738	5,473,759	13.6	13.2
Physical therapy	1,556,052	98,417	55,001	1,709,470	1,329,247	88,360	44,073	1,461,680	3.9	3.5
Radiation oncology	356,921	10,926	1,144,560	1,512,407	328,124	5,682	1,114,339	1,448,145	4.9	3.5
Radiology	1,510,160	357,888	283,015	2,151,063	1,399,922	371,083	240,596	2,011,601	3.4	4.8
Respiratory therapy	1,352,281	228,632	259,899	1,840,812	1,344,312	260,633	202,851	1,807,796	4.2	4.4
Ultrasound	304,076	9,798	44,645	358,519	301,069	7,628	69,975	378,672	0.8	0.9
	<u>\$ 17,494,703</u>	<u>\$ 17,660,303</u>	<u>\$ 9,119,958</u>	<u>\$ 44,275,164</u>	<u>\$ 16,362,168</u>	<u>\$ 16,275,814</u>	<u>\$ 8,894,025</u>	<u>\$ 41,532,007</u>	<u>100.0 %</u>	<u>100.0 %</u>

SLIDELL MEMORIAL HOSPITAL

ADDITIONAL INFORMATION—SCHEDULE OF HOSPITAL OPERATING EXPENSES YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004				2003				Percentage of	
	Salaries, Wages and Benefits	Supplies and Materials	Other Direct Expenses	Total	Salaries, Wages and Benefits	Supplies and Materials	Other Direct Expenses	Total	2004	2003
GENERAL SERVICES:										
Dietary	\$ 671,595	\$ 795,437	\$ 168,133	\$ 1,635,165	\$ 616,388	\$ 725,637	\$ 175,148	\$ 1,517,173	26.4 %	28.8 %
Housekeeping	773,304	107,811	783,198	1,664,313	701,112	105,224	750,573	1,556,909	26.9	29.6
Maintenance	484,620	117,789	1,057,976	1,660,385	497,288	83,459	492,547	1,073,294	26.8	20.4
Security	133,799	187	11,278	145,264	103,380	5	12,410	115,795	2.4	2.2
Utilities			1,082,668	1,082,668			997,882	997,882	17.5	19.0
	<u>\$ 2,063,318</u>	<u>\$ 1,021,224</u>	<u>\$ 3,103,253</u>	<u>\$ 6,187,795</u>	<u>\$ 1,918,168</u>	<u>\$ 914,325</u>	<u>\$ 2,428,560</u>	<u>\$ 5,261,053</u>	<u>100.0 %</u>	<u>100.0 %</u>
FISCAL AND ADMINI- STRATIVE SERVICES:										
Accounting	\$ 436,847	\$ 3,335	\$ 11,741	\$ 451,923	\$ 329,583	\$ 4,091	\$ 10,898	\$ 344,572	1.9 %	1.5 %
Administration	1,196,724	11,055	361,681	1,569,460	1,028,805	4,603	251,536	1,284,944	6.6	5.7
Admitting	532,279	21,851	233,790	787,920		6,745	787,716	794,461	3.3	3.5
Business office	396,896	18,219	2,146,346	2,561,461	80	687	2,901,069	2,901,836	10.8	12.8
Case management	477,164	1,077	2,896	481,137	390,045	1,002	1,014	392,061	2.0	1.7
Central Services	309,011	(250,538)	198,510	256,983	261,803	(239,174)	234,031	256,660	1.1	1.1
Fitness Center	277,152	534	8,045	285,731	265,300	771	3,773	269,844	1.2	1.2
Human resources	184,954	5,530	246,503	436,987	148,387	3,052	234,288	385,727	1.9	1.7
Information systems	729,400	9,175	1,424,719	2,163,294	647,194	8,612	1,207,159	1,862,965	9.1	8.2
Medical records	839,677	25,310	104,627	969,614	787,615	21,735	101,620	910,970	4.1	4.0
Medical review services	151,841	2,291	7,088	161,220	134,768	2,075	3,764	140,607	0.7	0.6
Patient care services	842,895	6,676	19,545	869,116	787,501	3,800	15,188	806,489	3.7	3.6
Physician recruitment and staff relations	74,968	1,304	78,665	154,937	71,081	1,451	26,531	99,063	0.7	0.4
Property management	205,557	11,161	598,858	815,576	138,393	6,104	506,936	651,433	3.4	2.9
Public relations	269,283	7,498	544,929	821,710	316,425	10,859	295,269	622,553	3.5	2.8
Purchasing	220,433	1,972	139,114	361,519	203,471	5,855	90,803	300,129	1.5	1.3
Training and development	73,969	12,435	41,734	128,138	56,480	5,397	33,535	95,412	0.5	0.4
Collection agency fees			193,399	193,399			214,710	214,710	0.8	0.9
Directors' expenses			19,344	19,344			9,055	9,055	0.1	
Insurance expenses	5,774,135		1,942,315	7,716,450	6,730,415		1,616,748	8,347,163	32.6	36.9
Pension and retirement	919,777			919,777	796,863			796,863	3.9	3.5
Postage			238,845	238,845			234,914	234,914	1.0	1.0
Professional fees			1,115,901	1,115,901			575,632	575,632	4.7	2.5
Telephone			214,315	214,315			321,371	321,371	0.9	1.4
	<u>\$ 13,912,962</u>	<u>\$ (111,115)</u>	<u>\$ 9,892,910</u>	<u>\$ 23,694,757</u>	<u>\$ 13,094,209</u>	<u>\$ (152,335)</u>	<u>\$ 9,677,560</u>	<u>\$ 22,619,434</u>	<u>100.0 %</u>	<u>100.0 %</u>

SLIDELL MEMORIAL HOSPITAL

ADDITIONAL INFORMATION—SCHEDULE OF HOSPITAL OTHER REVENUE YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
Rental income	\$1,261,300	\$1,241,335
Cafeteria sales	294,927	309,429
Vendor discounts	47,318	15,890
Fitness center revenue	240,271	227,620
Other revenue	388,697	333,677
Loss of subsidiary	(27,369)	(26,833)
Gain (loss) on sale of assets	<u>(61,577)</u>	<u>114,958</u>
	<u>\$2,143,567</u>	<u>\$2,216,076</u>

SLIDELL MEMORIAL HOSPITAL

**ADDITIONAL INFORMATION—SCHEDULE OF HOSPITAL CAPITAL ASSETS
YEAR ENDED DECEMBER 31, 2004**

	Assets			Accumulated Depreciation				
	January 1, 2004	Additions	Transfers and Deductions	December 31, 2004	January 1, 2004	Additions	Transfers and Deductions	December 31, 2004
Land	\$ 3,597,713	\$	\$	\$ 3,597,713	\$ -	\$	\$	\$
Land improvements	1,077,870			1,077,870	831,467	28,090		859,557
Buildings	62,171,994	282,044	247,429	62,206,609	30,968,761	2,696,577	247,429	33,417,909
Equipment	47,581,804	5,634,136	5,489,087	47,726,853	40,549,984	3,103,681	5,091,065	38,562,600
	<u>\$114,429,381</u>	<u>\$5,916,180</u>	<u>\$5,736,516</u>	<u>\$114,609,045</u>	<u>\$72,350,212</u>	<u>\$5,828,348</u>	<u>\$5,338,494</u>	<u>\$72,840,066</u>

SLIDELL MEMORIAL HOSPITAL

ADDITIONAL INFORMATION—SCHEDULE OF HOSPITAL STATISTICS (UNAUDITED) YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
Average census (patients)	106	107
Percentage of occupancy (based on 173 beds)	61.3 %	62.0 %
Average length of stay (acute care patients)	4.4	4.6
Patient days:		
Routine	30,314	30,485
ICU	4,247	4,710
NICU	941	609
Rehabilitation	<u>3,281</u>	<u>3,350</u>
	<u>38,783</u>	<u>39,154</u>
Adjusted patient admissions (*)	13,872	13,045
Adjusted patient days (*)	63,918	63,282
Total number of admissions	8,406	8,071
Total number of admissions (acute care only)	8,116	7,778
Total number of discharges	8,494	8,125
Patient mix based on charges:		
Medicare	38.8 %	39.6 %
Medicaid	9.9 %	9.4 %
Commercial insurance	2.3 %	2.1 %
Managed care	43.0 %	43.1 %
Private pay and other	6.0 %	5.8 %
Total surgical procedures:		
Inpatient	1,760	1,774
Outpatient	<u>2,661</u>	<u>2,682</u>
	<u>4,421</u>	<u>4,456</u>
Emergency visits	24,835	25,794
Full-time equivalents at year end	764.4	697.2

(*) Inpatient days increased for equivalent outpatient volume.



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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Members of the Board of Commissioners
St. Tammany Parish Hospital Service District No. 2
Slidell, Louisiana

We have audited the financial statements of St. Tammany Parish Hospital Service District No. 2 (d/b/a Slidell Memorial Hospital) (the "Hospital"), as of and for the year ended December 31, 2004, and have issued our report thereon dated March 19, 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Hospital'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 reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud 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. However, we noted other matters involving the internal control over financial reporting that we have reported to the management of Slidell Memorial Hospital in a separate letter dated March 19, 2005.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hospital's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Commissioners, management, and the State of Louisiana Legislative Auditor and is not intended to be and should not be used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this report is distributed by the Legislative Auditor as a public document.

Deloitte + Touche LLP

March 19, 2005

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March 19, 2005

Members of the Board of Commissioners
St. Tammany Parish Hospital Service
District No. 2
Slidell, Louisiana

Dear Members of the Board of Commissioners:

In planning and performing our audit of the financial statements of St. Tammany Parish Hospital Service District No. 2 (d/b/a Slidell Memorial Hospital) (the "Hospital") for the year ended December 31, 2004 (on which we have issued our report dated March 19, 2005), we developed the following recommendations concerning certain matters related to the Hospital's internal control and certain observations and recommendations on other accounting, administrative, and operating matters. A description of the responsibility of management for establishing and maintaining internal control, and the objectives and inherent limitations of internal control, is set forth in the attached Appendix, and should be read in conjunction with this letter. Our comments are presented in Exhibit I and are listed in the table of contents thereto.

This report is intended solely for the information and use of the Board of Commissioners, management, others within the organization, and the State of Louisiana Legislative Auditor and is not intended to be and should not be used by anyone other than these specified parties.

We will be pleased to discuss these comments with you and, if desired, to assist you in implementing any of the suggestions.

Yours truly,

Deloitte & Touche LLP

SLIDELL MEMORIAL HOSPITAL AND MEDICAL CENTER

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APPENDIX

EXHIBIT I

INTERNAL CONTROL AND ADMINISTRATIVE AND OTHER MATTERS

BUSINESS CONTINUITY

Observation

Though a Business Continuity and Recovery Plan is in development, procedures linking recovery of systems to recovery of business operations have not been identified. During our review it was noted that Slidell Memorial Hospital (SMH) has not completed a full Business Impact Analysis to ensure that the Business Continuity Plan encompasses all operational and financial procedures and systems. While agreements with Siemens are in place, these agreements have a limited scope and have not been recently tested. Other procedures are being developed; however, these plans are not based on a formal business impact study.

Business Insight

There remains a significant risk that although key information system processes can be restored, key corporate business processes may not be restored.

Recommendation

We recommend SMH develop recovery plans to ensure that, in the event of a disaster, both data processing and business functions can be recovered with minimal lost time and information. A Business Continuity/Disaster Recovery Plan should be developed from an overall business perspective, and should address all critical areas of the business. The plan should include:

- The identification of key manual and automated processes and systems required to continue when a disaster is declared,
- Interim manual processing procedures,
- The specific arrangements to recover those key manual and automated processes and systems, including personnel, facilities, telecommunications, applications, manual procedures, supplies and equipment,
- A process to identify changes within the organization and make updates to help ensure the plan remains current,
- Periodic testing, where feasible and cost-effective, to help ensure the plan is operational
- Offsite storage and periodic testing of data backups for key financial systems.

APPLICATION CHANGE MANAGEMENT

Observation

The following were noted during our review of application change management procedures:

- Documented policies do not reflect the actual application development process. Some changes do not appear to be documented using a "Service Request Form," nor input to the Helpdesk Database as indicated in the Section A.1-2 of the Policy. Although some changes that do not appear in the help desk database are recorded with third-party software support providers, no centralized change management repository for all applications and system changes exists.
- *Evidence of user acceptance testing and final approvals from the business/user departments are not consistently retained to validate appropriate and comprehensive testing was performed on all system changes.*

Business Insight

Program changes that are not subjected to proper approvals, testing and deployment increase the likelihood that improper or unintended changes will be introduced into the company's environment, which could adversely impact normal business activities or underlying financial data.

Recommendation

We recommend that SMH consider:

- Implementation of a repository either within a change management system or manually through procedure, and require that all stages of all application and system changes be logged and approved within the repository.
- Developing and utilizing standardized test plans for all major components of all key financial and operational systems that include all key application functions (e.g. rates are automatically pulled from CDM tables based on the charge description) within the systems. Such standardized tests should be executed in a manner that validates the functionality of critical system functions and recorded in a change management repository.

APPENDIX

MANAGEMENT'S RESPONSIBILITY FOR, AND THE OBJECTIVES AND LIMITATIONS OF, INTERNAL CONTROL

The following comments concerning management's responsibility for internal control and the objectives and inherent limitations of internal control are adapted from the Statements on Auditing Standards of the American Institute of Certified Public Accountants.

Management's Responsibility

Management is responsible for establishing and maintaining internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of controls.

Objectives

The objectives of internal control are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in conformity with accounting principles generally accepted in the United States of America.

Limitations

Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.