

Financial Statements

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Years ended September 30, 2002 and 2001 with Report of Independent Auditors

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Financial Statements

Years ended September 30, 2002 and 2001

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Report of Independent Auditors

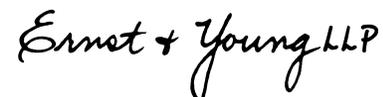
The Board of Commissioners
Hospital Service District No. 1 of
Iberia Parish, State of Louisiana

We have audited the accompanying balance sheets of Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center) as of September 30, 2002 and 2001, and the related statements of revenue, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Medical Center'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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our 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 Hospital Service District No. 1 of Iberia Parish, State of Louisiana as of September 30, 2002 and 2001, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 13, 2002 on our consideration of the Medical Center's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, and contracts. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.



December 13, 2002

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Balance Sheets

	September 30	
	2002	2001
Assets		
Current assets:		
Cash and cash equivalents	\$ 3,411,696	\$ 2,220,444
Patient accounts receivable, less allowance for doubtful accounts of \$4,627,000 and \$5,191,000 in 2002 and 2001, respectively	6,611,297	6,255,818
Other receivables	622,363	466,293
Inventories	1,206,393	1,077,639
Prepaid expenses	165,643	158,921
Current portion of assets limited as to use	717,583	874,848
Total current assets	<u>12,734,975</u>	<u>11,053,963</u>
Assets limited as to use, less current portion	3,628,191	4,666,944
Property and equipment, net	19,033,337	19,592,650
Investments in joint ventures	337,111	351,535
Bond issuance costs, net	110,924	375,033
Total assets	<u>\$ 35,844,538</u>	<u>\$ 36,040,125</u>
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 3,446,406	\$ 3,682,240
Accrued expenses	1,796,926	1,620,242
Due to third-party payers	834,877	854,867
Accrued interest payable	324,513	437,842
Current installments of long-term debt and capital lease obligations	874,803	762,505
Total current liabilities	<u>7,277,525</u>	<u>7,357,696</u>
Amount due to Iberia Parish	-	1,000,000
Long-term debt and capital lease obligations:		
Hospital Service District bonds payable	-	16,208,991
Iberia Parish bonds payable	15,338,000	-
Capital lease obligations	543,992	633,795
Total liabilities	<u>15,881,992</u>	<u>16,842,786</u>
Total liabilities	<u>23,159,517</u>	<u>25,200,482</u>
Net assets	12,685,021	10,839,643
Total liabilities and net assets	<u>\$ 35,844,538</u>	<u>\$ 36,040,125</u>

See accompanying notes.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Statements of Revenue, Expenses, and Changes in Net Assets

	Year ended September 30	
	2002	2001
Patient service revenue	\$ 39,921,250	\$ 36,487,847
Other revenue	522,946	574,017
Total revenue	40,444,196	37,061,864
Operating expenses:		
Salaries, wages, and benefits	17,536,693	16,056,050
Supplies and other expenses	14,328,943	12,949,355
Depreciation and amortization	1,595,861	1,977,850
Interest expense	1,107,675	1,373,674
Provision for doubtful accounts	4,695,418	3,730,201
Debt refinancing costs	368,805	—
Total expenses	39,633,395	36,087,130
Gain from operations	810,801	974,734
Nonoperating gains, net	1,034,577	633,403
Revenue and gains in excess of expenses	1,845,378	1,608,137
Net assets at beginning of year	10,839,643	9,231,506
Net assets at end of year	\$ 12,685,021	\$ 10,839,643

See accompanying notes.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Statements of Cash Flows

	Year ended September 30	
	2002	2001
Operating activities		
Gain from operations	\$ 810,801	\$ 974,734
Adjustments to reconcile gain from operations to net cash provided by operating activities:		
Depreciation and amortization	1,595,861	1,977,850
Debt refinancing costs	368,805	-
Amortization of debt reacquisition costs	30,000	-
Provision for doubtful accounts	4,695,418	3,730,201
Interest expense paid, net	1,003,412	1,040,383
Changes in operating assets and liabilities:		
Patient receivables, net	(5,050,897)	(3,324,758)
Other receivables	(156,070)	(233,477)
Prepaid expenses	(6,722)	(27,188)
Inventories	(128,754)	(74,623)
Accounts payable and accrued expenses	(59,125)	(466,976)
Amounts due to third-party payers	(19,990)	(460,615)
Net cash provided by operating activities	<u>3,082,739</u>	<u>3,135,531</u>
Capital and related financing activities		
Purchases of property, plant, and equipment	(947,779)	(363,613)
Proceeds from sales of property, plant, and equipment	-	8,900
Repayment of amount due to Iberia Parish	(1,000,000)	-
Proceeds from the issuance of debt by Iberia Parish	16,910,000	-
Principal payments on Hospital Service District debt	(16,985,487)	(635,126)
Premium paid through debt refunding	(567,250)	-
Principal payments on Iberia Parish debt	(250,000)	-
Principal payments on capital lease obligations	(129,601)	(110,738)
Interest payments on debt and capital lease obligations	(1,173,846)	(1,318,316)
Net cash used in capital and related financing activities	<u>(4,143,963)</u>	<u>(2,418,893)</u>
Investing activities		
Interest received on investments	267,167	389,614
Increase in assets limited as to use	(50,933)	(147,468)
Dividends received from joint ventures, net of contributions	313,944	(103,184)
Other nonoperating income received	475,347	594,052
Net cash provided by investing activities	<u>1,005,525</u>	<u>733,014</u>
Net increase (decrease) in cash and cash equivalents	(55,699)	1,449,652
Cash and cash equivalents at beginning of year	5,717,669	4,268,017
Cash and cash equivalents at end of year	<u>\$ 5,661,970</u>	<u>\$ 5,717,669</u>
Reconciliation of cash and cash equivalents to the balance sheet:		
Cash and cash equivalents in current assets	\$ 3,411,696	\$ 2,220,444
Cash and cash equivalents in assets limited as to use:		
By board for capital improvements	-	1,000,000
Held by trustee under bond indenture	1,702,829	2,003,251
Under self-insurance trust arrangements	547,445	493,974
	<u>\$ 5,661,970</u>	<u>\$ 5,717,669</u>

See accompanying notes.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements

September 30, 2002

1. Organization and Significant Accounting Policies

Organization

Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center) (the Medical Center) is a 130-bed acute-care hospital with related outpatient care facilities principally located in New Iberia, Louisiana. The Medical Center operates under the jurisdiction of the Iberia Parish Council of Iberia Parish, Louisiana (the Parish) as Hospital Service District No. 1 of Iberia Parish, State of Louisiana and is a component unit of the Parish as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*. The Medical Center's component unit relationship to the Parish is principally due to the Medical Center's financial accountability to the Parish as defined in GASB No. 14. The Medical Center is operated by a nine-member Board of Commissioners (the Board), all of whom are appointed by the Parish.

Basis of Accounting

The Medical Center uses the accrual basis of accounting for proprietary funds. Under Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Activities That Use Proprietary Fund Accounting*, the Medical Center has elected to apply the provisions of all relevant Financial Accounting Standards Board (FASB) pronouncements, including those issued after November 30, 1989, except for those that conflict with or contradict GASB pronouncements.

New Accounting Standards

The GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. Statement No. 34 establishes financial reporting standards for state and local governments. It establishes that the basic financial statements and required supplementary information (RSI) for general-purpose governments should consist of Management's Discussion and Analysis, Basic Financial Statements, and RSI. The Statement is effective for the Medical Center in fiscal year 2003. Adoption of this standard is not expected to have any effect on the financial position or results of operations of the Medical Center.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

Reclassifications

Certain reclassifications have been made to prior year balances in order to conform to the current year presentation.

Cash Equivalents

Cash equivalents include investments in highly liquid investments with maturities of three months or less when purchased.

Assets Limited as to Use

Assets limited as to use include:

- assets designated by the Medical Center's Board for future capital improvements, over which the Board retains control and may at its discretion subsequently use for other purposes;
- assets held by bond trustees under related indenture agreements; and
- assets held under self-insurance trust arrangements.

Deposits classified as current assets represent cash and cash equivalents to be used to meet certain debt service amounts classified as current liabilities at September 30.

Investments

All investments are stated at fair value, based on quoted market prices. Changes in the fair value of investments are included in investment income.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

Investments in Joint Ventures

Income earned on investments accounted for on the equity method and dividends received on investments accounted for on the cost basis are included as components of nonoperating gains. Additionally, the Medical Center provides certain personnel and supplies to the joint ventures for a fee and recognizes payment for these services and supplies as other operating income. These amounts increased operating income by \$180,000 in 2002 and \$246,000 in 2001.

Patient Service Revenue and Related Receivables

The Medical Center has entered into agreements with third-party payers, including government programs and insurers, under which the Medical Center is paid based upon established charges, the cost of providing services, predetermined rates per diagnosis, fixed per diem rates, or discounts from established charges.

Patient service revenue is reported at the estimated net realizable amounts due from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. These estimates are subject to inherent variability and actual results can differ materially from recorded estimates. Retroactively calculated contractual adjustments arising under reimbursement agreements with third-party payers are accrued on an estimated basis in the period the related services are rendered and adjusted as final settlements are determined.

Inventories

Inventories, consisting principally of medical supplies and pharmaceuticals, are stated at the lower of cost (first-in, first-out) or replacement value.

Property and Equipment

Property and equipment are recorded at cost, or if donated, at fair value at date of receipt. Depreciation is provided over the useful life of each class of depreciable asset using the straight-line method. Equipment held under capital lease obligations is amortized using the straight-line method over the shorter of the lease term or estimated useful life of the equipment and is included in depreciation and amortization expense.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

Unamortized Bond Issuance Costs

Bond issuance costs have been deferred and are being amortized using the interest method over the life of the related bonds.

Charity Care

The Medical Center 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 Medical Center does not pursue collection of amounts determined to qualify as charity care, such amounts are not reported as revenue.

Income Taxes

As a political subdivision, the Medical Center qualifies as tax-exempt under existing provisions of the Internal Revenue Code and its income is not generally subject to federal or state income taxes.

Operating and Nonoperating Revenue

The Medical Center's primary purpose is to provide diversified health care services to individuals, physicians, and businesses in Iberia Parish and the surrounding communities. As such, activities related to the ongoing operations of the Medical Center are classified as operating revenues. Operating revenues include those generated from direct patient care, related support services, gains or losses from disposition of operating properties and sundry revenues related to the operation of the Medical Center. Investment income from unrestricted and board-designated investments is reported as nonoperating gain. Investment income from trustee investments held under a related bond indenture is reported as other revenue. Additionally, gains and losses not directly related to the ongoing operations of the Medical Center or that occur infrequently, and gifts, grants, and bequests not restricted by donors for specific purposes, are reported as nonoperating income.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

2. Patient Service Revenue

Patient service revenue for 2002 and 2001 was comprised of the following:

	<u>2002</u>	<u>2001</u>
Gross patient service charges	\$ 95,058,516	\$ 85,272,047
Contractual and other allowances:		
Medicaid	9,998,281	8,189,729
Medicare	29,181,797	25,907,329
Insurers	15,216,821	14,069,957
Other	740,367	617,185
Total contractual and other allowances	55,137,266	48,784,200
Patient service revenue	\$ 39,921,250	\$ 36,487,847

The Medical Center participates in the Medicare and Medicaid programs as a provider of medical services to program beneficiaries. During the years ended September 30, 2002 and 2001, approximately 43% and 37%, respectively, of the Medical Center's net patient service revenue was related to services provided to Medicare and Medicaid program beneficiaries.

Revenues derived from government programs are subject to review by program representatives. Settlements for the years ended through September 30, 1998 for the Medicare program and September 30, 1999 for the Medicaid program have been reviewed by program representatives. Adjustments resulting from these reviews decreased net patient service revenue by \$117,000 in 2002 and increased net patient service revenue by \$175,000 in 2001.

3. Charity Care

The Medical Center maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy.

The Medical Center provides four full-time nurses at the Parish Criminal Justice Facility for medical assistance to the individuals in the facility. The Medical Center does not maintain records to identify and monitor the level of charity care it provides under this program; however, the total cost of providing this service approximated \$143,000 in 2002 and \$139,000 in 2001.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

4. Cash and Investments

Governmental accounting standards require that the carrying amounts of cash and investments as of the balance sheet date be categorized according to the level of credit risk associated with the Medical Center's cash and investments at that time. The level of credit risk is defined as follows:

- Category 1 – Insured (including government securities), registered, or collateralized with securities held by the Medical Center or its agent in the Medical Center's name.
- Category 2 – Uninsured and unregistered, collateralized with securities held by the counterparty's trust department or agent in the Medical Center's name.
- Category 3 – Uncollateralized, including balances collateralized with securities held by the pledging financial institution.

A summary of cash and investments at September 30, 2002 follows:

	Category			Total
	1	2	3	
Cash and cash equivalents	\$ 200,000	\$ 3,211,696	\$ –	\$ 3,411,696
Held by trustee under bond indenture:				
Cash and cash equivalents	\$ –	\$ –	\$ 1,702,829	\$ 1,702,829
U.S. Treasury Notes	1,904,199	–	191,301	2,095,500
	1,904,199	–	1,894,130	3,798,329
Held under self-insurance trust arrangements:				
Cash and cash equivalents	–	547,445	–	547,445
Total assets limited as to use	\$ 1,904,199	\$ 547,445	\$ 1,894,130	\$ 4,345,774

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

4. Cash and Investments (continued)

A summary of cash and investments at September 30, 2001 follows:

	Category			Total
	1	2	3	
Cash and cash equivalents	\$ 200,000	\$ 2,020,444	\$ –	\$ 2,220,444
Board-designated for capital improvements:				
Cash and cash equivalents	\$ 100,000	\$ 900,000	\$ –	\$ 1,000,000
Held by trustee under bond indenture:				
Cash and cash equivalents	226,909	–	1,776,342	2,003,251
U.S. Treasury Notes	2,044,567	–	–	2,044,567
	2,271,476	–	1,776,342	4,047,818
Held under self-insurance trust arrangements:				
Cash and cash equivalents	–	493,974	–	493,974
Total assets limited as to use	\$ 2,371,476	\$ 1,393,974	\$ 1,776,342	\$ 5,541,792

The Medical Center's U.S. Treasury Notes mature in May 2006.

Trusted bond funds are maintained in accordance with the requirements of the indentures related to the Parish of Iberia, State of Louisiana Hospital Revenue Refunding Boards and Hospital Service District No. 1 of Iberia Parish, Louisiana Hospital Revenue Bonds.

A summary of the trusted funds at September 30 follows:

	2002	2001
Debt service reserve funds	\$ 2,095,500	\$ 2,271,476
Principal and interest project funds	683,625	647,986
Depreciation reserve fund	1,019,204	1,128,356
	3,798,329	4,047,818
Less deposits classified as current assets	717,583	874,848
	\$ 3,080,746	\$ 3,172,970

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

4. Cash and Investments (continued)

The debt service reserve funds are generally equal to the maximum annual principal and interest requirements (as defined) for the bonds. Amounts in the principal and interest funds are used for the annual debt service of the bonds. The depreciation reserve fund is to be used for Medical Center additions and improvements, and equipment replacements.

5. Investments in Joint Ventures

Investments in joint ventures consisted of the following at September 30:

	<u>2002</u>	<u>2001</u>
New Iberia Surgery Center	\$268,111	\$282,535
Acadiana Diagnostic Imaging LLC	69,000	69,000
	<u>\$337,111</u>	<u>\$351,535</u>

The Medical Center holds a 20% interest in the New Iberia Surgery Center, which provides outpatient surgery services to the community. This investment is carried on the equity method of accounting. The Medical Center holds a 15% interest in Acadiana Diagnostic Imaging LLC, which is a provider of radiation services. This investment is accounted for on the cost basis.

6. Business and Credit Concentrations

The Medical Center grants credit to patients, substantially all of whom are local area residents. The Medical Center generally does not require collateral or other security in extending credit to patients; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies (e.g., Medicare, Medicaid, Blue Cross Blue Shield of Louisiana, and commercial insurance policies).

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

6. Business and Credit Concentrations

The mix of gross receivables from patients and third-party payors at September 30 follows:

	<u>2002</u>	<u>2001</u>
Self-pay	41%	45%
Medicare	24	19
Other third-party payers	4	3
Medicaid	7	5
Blue Cross Blue Shield of Louisiana	7	10
Commercial insurers	17	18
	<u>100%</u>	<u>100%</u>

7. Property and Equipment

A summary of property and equipment at September 30 follows:

	<u>2002</u>	<u>2001</u>
Land and improvements	\$ 1,380,089	\$ 1,380,089
Building and improvements	23,283,699	22,627,878
Fixed equipment	4,382,801	4,382,801
Major movable equipment	17,798,724	17,463,257
Construction in progress	58,238	119,512
	<u>46,903,551</u>	<u>45,973,537</u>
Less accumulated depreciation and amortization	27,870,214	26,380,887
	<u>\$ 19,033,337</u>	<u>\$ 19,592,650</u>

Major movable equipment under capital lease obligations totaled \$2,082,000 at September 30, 2002 and 2001. Related accumulated amortization was approximately \$1,693,000 and \$1,524,000 at September 30, 2002 and 2001, respectively.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

8. Long-Term Debt and Capital Lease Obligations

A summary of long-term debt, including capital lease obligations, at September 30 follows:

	<u>2002</u>	<u>2001</u>
Hospital Service District No. 1 of Iberia Parish, Louisiana Hospital Revenue Bonds - Series 1979, payable in semiannual installments, including interest at 6%, through November 2009	\$ —	\$ 2,685,422
Hospital Service District No. 1 of Iberia Parish, Louisiana Hospital Revenue Bonds - Series 1980, payable in semiannual installments, including interest at 6%, through May 2010	—	2,762,000
Hospital Service District No. 1 of Iberia Parish, Louisiana Hospital Revenue Bonds - Series 1996, payable in semiannual installments, including interest at rates from 7.5% to 8%, through May 2016	—	11,440,000
Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds - Series 2001A, payable in semi- annual installments beginning in May 2008, including interest at 5.25%, through May 2016	7,905,000	—
Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds - Series 2001B, payable in semi- annual installments beginning in May 2002, including interest at 7.25%, through May 2008	3,565,000	—
Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds - Series 2002, payable in semi- annual installments beginning in May 2002, including interest at 5%, through May 2016	5,190,000	—
Capital lease obligations, payable in various monthly installments through September 2008, including interest at rates from 6.5% to 7.9%	633,795	717,869
	17,293,795	17,605,291
Less current installments	874,803	762,505
Less reacquisition premium	537,000	—
Long-term debt, less current installments	<u>\$ 15,881,992</u>	<u>\$ 16,842,786</u>

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

8. Long-Term Debt and Capital Lease Obligations (continued)

During 2002, the Medical Center, through an arrangement with the Parish, issued \$16,910,000 of Revenue Refunding bonds (Series 2001A, 2001B, and 2002) in a current refunding of \$16,552,000 of outstanding bonds (Series 1979, 1990, and 1996). The current refunding required a premium payment totaling \$567,000. This reacquisition premium, reported in the accompanying financial statements as a reduction in the carrying amount of the associated debt, will be charged to operations through 2016 using the effective-interest method. Unamortized bond issuance costs of \$369,000 related to the refunded bonds was charged to operations in 2002.

The Medical Center's revenue and assets are pledged as collateral for the Parish's bonds. The Medical Center is directly obligated to the Parish for principal and interest payments on the debt as these amounts come due. The indentures also place limits on additional borrowings. The Medical Center was in compliance with these covenants at September 30, 2002 and 2001.

Future maturities of long-term debt and payments on capital lease obligations at September 30, 2002 are as follows:

	Long-Term Debt	Capital Lease Obligations
2003	\$ 785,000	\$ 129,603
2004	840,000	129,602
2005	890,000	129,603
2006	955,000	129,603
2007	1,020,000	129,603
Thereafter	12,170,000	119,196
	<u>16,660,000</u>	<u>767,210</u>
Less unamortized reacquisition costs	537,000	
Less amounts representing interest on capital lease obligations	-	133,415
	<u>\$16,123,000</u>	<u>\$ 633,795</u>

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

9. Pension Plan

The Medical Center contributes to the Parochial Employees Retirement System of Louisiana (the System), a cost-sharing multiple-employer defined benefit pension plan. The System is comprised of two distinct plans—Plan A and Plan B—with separate assets and benefit provisions. Employees of the Medical Center are members of Plan A. The System provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by state law and may be amended only by the State of Louisiana Legislature. The System issues a publicly available financial report that includes financial statements and required supplementary information.

System members are required to contribute 9.5% of their annual covered salary and the Medical Center is required to contribute at an actuarially determined rate. The current rate is 7.75% of annual covered payroll. The Medical Center's pension cost and contributions to the System were approximately \$952,000 in 2002 and \$889,000 in 2001. These amounts were equal to the required contributions for each year.

10. Contingencies

The Medical Center maintains insurance coverage for medical malpractice claims up to the statutory limit through the Louisiana Hospital Association Trust Fund and the State of Louisiana Patient Compensation Fund. As of September 30, 2002, there was certain litigation pending against the Medical Center and management believes the insurance coverage described previously adequately insures the Medical Center against these claims.

The Medical Center is self-insured for employee health coverage, up to a limit of \$60,000 per individual claim. Excess coverage is maintained with a third-party carrier.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

10. Contingencies (continued)

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. 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. Changes in Medicare and Medicaid programs and reductions in funding could have an adverse impact on the Medical Center. It is the Medical Center's policy to be in compliance with these laws and regulations.

In July 2000, the Medical Center entered into a Corporate Integrity Agreement (CIA) with the Office of the Inspector General (OIG) of the U.S. Department of Health and Human Services to promote compliance by its employees with the statutes, regulations, and written directives of Medicare, Medicaid, and all other federal health care programs. The agreement is a product of a settlement between the Medical Center and the OIG related to errors in Medicare reimbursements received during the period from 1992 through 1995. The three-year agreement contains provisions specifying the components of the compliance program that the Medical Center is implementing. Failure of the Medical Center to comply with certain obligations set forth in the CIA may lead to the imposition of certain monetary penalties. Management believes that the Medical Center is in compliance with these obligations.

11. Operating Leases

The Medical Center leases office space and clinical facilities, generally to members of its medical staff, under operating leases with terms ranging from month-to-month up to five years. The future minimum lease payments to be received from these leases follow:

2003	\$ 235,557
2004	141,546
2005	79,262
2006	69,174
2007	33,425
	<u>\$ 558,964</u>

Hospital Service District No. 1 of Iberia Parish, State of Louisiana

Notes to Financial Statements (continued)

11. Operating Leases (continued)

The Medical Center leases various equipment and facilities under operating leases expiring at various dates through May 2007. The following is a schedule by year of future minimum lease payments under operating leases that have initial or remaining lease terms in excess of one year.

2003	\$ 830,569
2004	725,138
2005	678,513
2006	601,872
2007	87,276
	<u>\$ 2,923,368</u>

Rental expense for operating leases was approximately \$834,000 in 2002 and \$419,000 in 2001.

Report of Independent Auditors on
Compliance and on Internal Control
Over Financial Reporting Based on an
Audit of Financial Statements Performed in
Accordance *With Government Auditing Standards*

The Board of Commissioners
Hospital Service District No. 1 of
Iberia Parish, State of Louisiana

We have audited the financial statements of Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center) as of and for the year ended September 30, 2002, and have issued our report thereon dated December 13, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

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

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Medical Center's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements

in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to the board of commissioners and management of the Medical Center in a separate report dated December 13, 2002.

This report is intended for the information and use of the board of commissioners, management, and the Office of Legislative Auditor, State of Louisiana, and is not intended to be and should not be used by anyone other than these specified parties.

Ernst + Young LLP

December 13, 2002

The Board of Commissioners
Hospital Service District No. 1 of Iberia Parish, State of Louisiana

In planning and performing our audit of the financial statements of Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center) for the year ended September 30, 2002, we considered its internal control to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that errors 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. However, we noted no matters involving internal control and its operation that we consider to be material weaknesses as defined above.

During our audit, the following matters came to our attention that we believe merit your consideration.

Significant Estimation Processes

Allowance for Contractual Adjustments

In connection with the financial statement close process, management estimates an allowance for contractual adjustments to the amounts billed and accrued for services rendered. This estimate is material and highly sensitive to changes in historical collection rates. We suggest management establish a documented process to assess the adequacy of prior period contractual allowance estimates through a retrospective analysis similar to the hindsight review of the allowance for uncollectible accounts. This process could aid management in their assessment of the reserving methodology and highlight needed changes in approach.

Management's Response

Management will document the process used to develop the estimates for contractual adjustments. This process includes the hindsight review of payments and adjustments which are detailed in source documents such as third-party remittance advices, the

summarization of this data in trending schedules, and the comparison of this information to the estimates utilized in completing the contractual adjustments reported in the financial statements.

Monitoring Third-Party Settlement Estimates

As part of the current year third-party estimation process, management provided for uncertainties that exist in preparing the cost report due to the potential that there are differing interpretations of government regulations. While management's reserve estimates are based on historical events and current industry issues, management does not have a formal policy for establishing and evaluating the need to provide for the identified uncertainties.

We recommend that management develop a formal process to address this matter that utilizes, among other things, historical data, current year data, and current cost report variables. Additionally, we recommend that management include an analysis of the development of prior years' estimates.

Management's Response

Management will formulate a policy to guide the establishment and evaluation of the need to provide for the uncertainties inherent in the cost reporting process. This policy will include the review of potential impact of intermediary audit adjustments to prior year filed cost reports, the monitoring of cost reimbursement interpretations by intermediaries, and analysis of the accuracy of remittance advices and PS&R's.

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This report is intended solely for the information and use of the board of commissioners, management, and the Office of the Legislative Auditor, State of Louisiana, and is not intended to be and should not be used by anyone other than these specified parties.

We would be pleased to discuss the above matters or to respond to any questions, at your convenience.

Ernst + Young LLP

December 13, 2002