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LAKEWOOD MEDICAL CENTER

Financial Statements

December 31, 1996 and 1995

With Independent Auditors' Report Thereon

LAKEWOOD MEDICAL CENTER

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December 31, 1996 and 1995

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KPMG Peat Marwick LLP

Suite 3500 One Shell Square
New Orleans, LA 70139-3599

Independent Auditors' Report

The Board of Commissioners
Hospital Service District No. 2 of
St. Mary Parish, Louisiana
(Lakewood Medical Center):

We have audited the accompanying balance sheets of Hospital Service District No. 2 of St. Mary Parish, Louisiana (Lakewood Medical Center) (the Medical Center) as of December 31, 1996 and 1995, and the related statements of revenues and expenses of unrestricted funds, changes in fund balances, 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 generally accepted auditing standards and *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 Lakewood Medical Center as of December 31, 1996 and 1995, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated March 6, 1997, on our consideration of the Medical Center's internal control structure and a report dated March 6, 1997, on its compliance with laws and regulations.

KPMG Peat Marwick LLP

March 6, 1997

LAKEWOOD MEDICAL CENTER

Balance Sheets

December 31, 1996 and 1995

Assets	1996	1995
Current assets:		
Cash and cash equivalents (notes 2 and 3)	$ 36,141	115,125
Assets limited as to use required for current liabilities (note 4)	516,467	514,177
Patient accounts receivable, less allowances for doubtful accounts of $1,220,000 in 1996 and $1,025,000 in 1995	3,622,771	3,207,827
Ad valorum tax receivable	550,000	440,000
Other receivables	187,002	175,829
Inventories	571,264	745,346
Prepaid expenses and other current assets	147,307	215,534
Total current assets	5,630,952	5,413,838
Assets limited as to use (notes 3 and 4):		
For plant and equipment additions and replacement by board of commissioners	743,661	1,097,303
For maintenance and purchase of capital and technology relating to maintenance taxes received	766,159	147,706
For debt service:		
Revenue bond	1,517	1,577
General obligation bonds	2,333,787	2,729,614
Total assets limited as to use	3,845,124	3,976,200
Less assets limited as to use required for current liabilities	516,467	514,177
Noncurrent assets limited as to use	3,328,657	3,462,023
Property, plant and equipment, net (note 5)	12,401,049	11,223,751
Debt issuance costs, net of accumulated amortization of $61,683 in 1996 and $57,444 in 1995	50,187	54,426
Total assets	$ 21,410,845	20,153,238

Liabilities and Fund Balances	1996	1995
Current liabilities:		
Current portion of:		
Long-term debt (note 6)	$ 815,911	380,911
Capital lease obligations (note 7)	525,009	433,209
Accounts payable	1,214,742	863,653
Accrued salaries, wages and benefits	581,532	649,491
Due to third-party payors	819,558	1,012,639
Accrued interest	88,213	92,530
Total current liabilities	4,044,965	3,432,433
Capital lease obligations, less current portion (note 7)	1,511,153	455,934
Long-term debt, less current portion (note 6)	9,372,664	10,188,575
Total liabilities	14,928,782	14,076,942
Fund balances:		
Restricted for debt service on general obligation bonds	2,218,430	2,606,303
Restricted for plant replacement and other	15,000	15,000
Unrestricted	4,248,633	3,454,993
	6,482,063	6,076,296
Commitments and contingencies (notes 7, 12, 13 and 14)		
Total liabilities and fund balances	$ 21,410,845	20,153,238

See accompanying notes to financial statements.

LAKEWOOD MEDICAL CENTER

Statements of Revenues and Expenses

Years ended December 31, 1996 and 1995

	1996	1995
Net patient service revenue (note 8)	$ 22,681,695	20,796,907
Other revenue	184,115	157,942
Total operating revenues	22,865,810	20,954,849
Expenses:		
Salaries, wages and benefits	10,961,412	10,297,610
Professional fees	1,256,439	1,238,733
Supplies and other	6,438,683	5,900,944
Provision for uncollectible accounts	2,255,036	1,647,744
Depreciation and amortization	1,626,074	1,505,344
Interest	704,512	723,772
Total operating expenses	23,242,156	21,314,147
Loss from operations	(376,346)	(359,298)
Nonoperating gains (losses):		
Ad valorem taxes	841,589	749,611
Donations	86,959	21,537
Interest income	86,804	71,433
Rental income, net	14,034	37,772
Loss on equipment disposal	(224,400)	-
Total nonoperating gains, net	804,986	880,353
Revenues and gains in excess of expenses and losses	$ 428,640	521,055

See accompanying notes to financial statements.

LAKEWOOD MEDICAL CENTER

Statements of Changes in Fund Balances -
Restricted and Unrestricted Funds

Years ended December 31, 1996 and 1995

	Fund Balances		
	Restricted for debt service on general obligation bonds	Restricted for plant replacement and other	Unrestricted
Balance at January 1, 1995	$ 2,540,824	-	2,588,938
Additions (deductions):			
Ad valorem tax receipts	446,252	-	-
Investment earnings	126,227	-	-
Revenues and gains in excess of expenses and losses	-	-	521,055
Debt service on general obligation bonds:			
Principal payments	(345,000)	-	345,000
Interest paid or accrued	(162,000)	-	-
Donations received	-	36,537	-
Transfers to finance property, equipment and other	-	(21,537)	-
Balance at December 31, 1995	2,606,303	15,000	3,454,993
Additions (deductions):			
Investment earnings	117,427	-	-
Revenues and gains in excess of expenses and losses	-	-	428,640
Debt service on general obligation bonds:			
Principal payments	(365,000)	-	365,000
Interest paid or accrued	(140,300)	-	-
Donations received	-	86,959	-
Transfers to finance property, equipment and other	-	(86,959)	-
Balance at December 31, 1996	$ 2,218,430	15,000	4,248,633

See accompanying notes to financial statements.

LAKEWOOD MEDICAL CENTER

Statements of Cash Flows - Restricted and Unrestricted Funds

Years ended December 31, 1996 and 1995

	1996	1995
Cash flows from operating activities:		
Loss from operations	$ (376,346)	(359,298)
Interest expense considered capital financing activity	704,512	723,772
Adjustments to reconcile loss to net cash provided by operating activities:		
Depreciation and amortization	1,626,074	1,505,344
Provision for uncollectible accounts	(2,255,036)	(1,647,744)
Changes in operating assets and liabilities:		
Decrease in patient receivables	1,840,091	2,067,275
Increase in other receivables	(11,973)	(12,816)
Decrease in prepaid expenses and other assets	68,227	23,390
Decrease (increase) in inventories	174,082	(120,445)
Increase (decrease) in accounts payable accrued expenses and current liabilities	351,089	(297,182)
(Decrease) increase in accrued salaries	(106,488)	288,455
Decrease in due to third-party payors	(154,552)	(17,106)
Net cash provided by operating activities	1,859,680	2,153,645
Cash flows from investing activities:		
Net rental receipts	71,289	90,667
Ad valorem taxes received	591,289	593,863
Utilization of (investment in) assets limited as to use	107,882	(1,013,318)
Investment earnings	204,232	197,660
Net cash provided by (used in) investing activities	974,692	(131,128)
Cash flows from capital and related financing activities:		
Acquisitions of property, plant and equipment	(1,394,369)	(930,902)
Principal paid on long-term debt and capital leases	(920,311)	(750,029)
Interest paid on long-term debt and capital leases	(708,829)	(968,750)
Restricted donations received	86,959	36,537
Net cash used in capital and related financing activities	(2,936,550)	(2,613,144)

(Continued)

LAKEWOOD MEDICAL CENTER

Statements of Cash Flows -
Restricted and Unrestricted Funds, Continued

	1996	1995
Net decrease in cash and cash equivalents	$ (102,178)	(590,627)
Cash and cash equivalents at beginning of year	470,869	1,061,495
Cash and cash equivalents at end of year	$ 368,691	470,868
Reconciliation of cash and cash equivalents to the balance sheet:		
Cash and cash equivalents in current assets	36,141	115,125
Cash and cash equivalents in assets limited as to use:		
For plant and equipment additions and replacement by board of commissioners	152,241	202,489
For maintenance and purchase of capital and technology	170,327	147,706
For debt service on revenue bonds	1,517	1,577
For debt service on general bonds	8,465	3,971
	$ 368,691	470,868

The Medical Center entered into capital lease obligations of $1,702,330 for new equipment in 1996.

See accompanying notes to financial statements.

LAKEWOOD MEDICAL CENTER

Notes to Financial Statements

December 31, 1996 and 1995

(1) Organization and Significant Accounting Policies

Lakewood Medical Center (the Medical Center) is a nonprofit public corporation, exempt from federal income taxes under Internal Revenue Code Section 115 (as a governmental entity) and Section 501(a) (as a hospital organization described in Section 501(c)(3)), owned by Hospital Service District No. 2 of St. Mary Parish, Louisiana (the District). The Medical Center is organized under powers granted to Parish Police Juries by the State Legislature under Act 420 of 1950. All corporate powers are vested in a Board of Commissioners (the Board) appointed by the Parish Police Jury of St. Mary Parish, Louisiana. The significant accounting policies used by the Medical Center in preparing and presenting its financial statements are summarized as follows:

(a) Inventories

Inventories consisting primarily of medical supplies and drugs, are stated at the latest invoice price which approximates the lower of cost (first-in, first-out), or market.

(b) Use of Estimates

Management of the Medical Center has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

(c) Proprietary Fund Accounting

The Medical Center utilizes the proprietary fund method of accounting whereby revenue and expenses are recognized on the accrual basis. Substantially all revenues and expenses are subject to accrual.

(d) Accounting Standards

Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Medical Center has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989.

(Continued)

(e) Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less.

(f) Assets Limited as to Use

Assets limited as to use include:

- Assets set aside by the Board of Commissioners for future capital improvements over which the Board retains control and may at its discretion subsequently use for other purposes, and

- Assets set aside under indenture agreements.

Assets limited as to use that will be used for current liabilities are reflected as current assets in the accompanying balance sheets.

(g) Investments

Investments are stated at cost, adjusted for amortization of premiums, accretion of discounts and impairments in value that are deemed other than temporary. Premiums and discounts are amortized using the straight-line method which is not materially different from the interest method.

(h) Property, Plant and Equipment

Property, plant, and equipment are stated at cost less accumulated depreciation. Donated equipment is recorded at fair value at date of donation, which is then treated as cost. Equipment under capital lease is stated at the lower of the present value of minimum lease payments at the beginning of the lease term or fair value at the inception of the lease.

Depreciation on plant and equipment is calculated on the straight-line method over the estimated useful lives of the assets. Equipment held under capital lease obligations is amortized on the straight-line method over the shorter of the lease term or estimated useful life of the asset.

(i) Fund Balance Temporarily Restricted for Debt Service on General Obligation Bonds

Upon receipt of tax revenues levied through December 31, 1994, the Medical Center records the proceeds from ad valorem taxes levied on property within Hospital Service District No. 2 of St. Mary Parish,

(Continued)

Louisiana as additions to the temporarily restricted fund balance for debt service on general obligation bonds. These monies are available only for payment of the debt service on the general obligation bonds. As principal payments are made on the general obligation bonds, a transfer to unrestricted funds is recorded. Interest payments result in a transfer to other revenue in the statement of revenue and expenses of unrestricted funds to offset the interest on the general obligation bonds included in expenses.

Beginning in the year ended December 31, 1995, the proceeds from ad valorem taxes levied on December 31 of each year on property within Hospital Service District No. 2 of St. Mary Parish, Louisiana for the same tax year ended December 31, are recorded as additions to assets limited as to use for plant and equipment additions and replacement by Board of Commissioners. These funds are only available for the maintenance and purchase of capital and technology. Current taxes are received beginning in December of each year and become delinquent after February 28 of the following year.

(j) Statement of Revenues and Expenses

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as revenue and expenses. Peripheral or incidental transactions are reported as gains and losses.

(k) Net Patient Service Revenue

Net patient service is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors.

Retroactively calculated contractual adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted as final settlements are determined.

(l) 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.

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(m) Income Taxes

The Medical Center qualifies as tax-exempt under existing provisions of the Internal Revenue Code, and its income, generally, is not subject to Federal or State income taxes.

(n) Debt Issuance Costs

Expenses related to issuance of bonds are deferred and amortized over the period the bonds will remain outstanding.

(o) Reclassifications

Certain reclassifications have been made in the 1995 financial statements to conform with the 1996 presentation.

(2) Cash and Cash Equivalents

Cash and cash equivalents include cash on deposit with financial institutions, excluding amounts whose use is limited by Board designation. At December 31, 1996 and 1995, the Medical Center had cash as follows:

	1996	1995
Demand deposits	$ 34,441	113,425
Petty cash	1,700	1,700
	$ 36,141	115,125

(3) Bank Deposits

Under state law, the bank balances of bank deposits and cash balances included in assets limited as to use by board designation, as discussed in note 4, must be secured by Federal deposit insurance or the pledge of securities owned by the fiscal agent. At December 31, 1996 and 1995, the market value of pledged securities plus the federal deposit

(Continued)

insurance exceeded the amount on deposit with the fiscal agent banks. At December 31, 1996 and 1995, the Medical Center had bank deposits as follows:

	1996	1995
Secured by Federal deposit insurance	$ 444,840	452,835
Collateralized by securities held by the pledging financial institution's trust department in the Medical Center's name	1,951,033	2,821,635
Total	$ 2,395,873	3,274,470
Carrying value of bank deposits in the balance sheets	$ 2,163,915	2,902,098

Reconciliation of carrying value of bank deposits to the balance sheets:

	1996	1995
Demand deposits	$ 34,441	113,425
Cash and cash equivalents in assets limited as to use:		
For plant and equipment additions and replacement	152,241	202,489
For maintenance and purchase of capital and technology relating to maintenance taxes	170,327	147,706
For debt service on revenue bonds	1,517	1,577
For debt service on general bonds	8,465	3,971
Certificates of deposit in assets limited as to use:		
For plant and equipment additions and replacement	-	200,000
For debt service on general obligation bonds	1,796,924	2,232,930
	$ 2,163,915	2,902,098

(4) Assets Limited as to Use

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

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Category 1 - Insured (including government securities) or registered, or collateralized with securities held by the Hospital or its agent in the Hospital's name.

Category 2 - Uninsured and unregistered, collateralized with securities held by the counterparty's trust department or agent in the Hospital's name.

Category 3 - Uninsured and unregistered, or uncollateralized, including balances collateralized with securities held by the pledging financial institution, but not in the Hospital's name.

The details of assets limited as to use at December 31, 1996 and 1995 are as follows:

	1996	1995
For plant and equipment additions and replacement by board of commissioners:		
Cash and cash equivalents	$ 152,241	202,489
Certificate of deposit	-	200,000
U.S. Treasury notes	585,221	690,988
Accrued interest receivable	6,199	3,826
	743,661	1,097,303
For maintenance and purchase of capital and technology relating to maintenance taxes received:		
Cash and cash equivalents	170,327	147,706
U.S. Treasury notes	584,853	-
Accrued interest receivable	10,979	-
	766,159	147,706
For debt service on Series 1978 revenue bond - cash and cash equivalents	1,517	1,577
For debt service on Series 1976 general obligation bonds:		
Cash and cash equivalents	8,465	3,971
Certificates of deposit	1,796,924	2,232,930
U.S. Treasury notes	97,595	97,394
Accrued interest receivable	430,803	395,319
	2,333,787	2,729,614

(Continued)

	1996	1995
Total assets limited as to use	$ 3,845,124	3,976,200
Less amounts classified as current	516,467	514,177
Noncurrent assets limited as to use	$ 3,328,657	3,462,023

On December 31, 1996 and 1995, all assets whose use is limited are a Category 1 type investment.

In connection with the 1978 revenue bond, the Medical Center established a sinking fund and reserve fund. The reserve fund is used for the purpose of making payments of principal and interest on the bond if funds available for payment of principal and interest in the sinking fund are insufficient. At December 31, 1996 and 1995, there were no funds on deposit in the reserve fund. The amounts on deposit in the sinking fund were $1,517 and $1,577 at December 31, 1996 and 1995, respectively. The Medical Center has not funded the sinking fund since September 1993 (see Note 6).

(5) Property and Equipment

Property an equipment, by major category, at December 31, 1996 and 1995 are as follows:

	1996	1995
Land and improvements	$ 118,210	118,210
Building and improvements	22,625,729	22,499,287
Fixed equipment	3,792,436	3,732,729
Major moveable equipment	6,804,534	6,503,116
	33,340,909	32,853,342
Less accumulated depreciation	23,517,844	22,883,189
	9,823,065	9,970,153
Equipment under capital lease obligations	3,878,520	2,176,190
Less accumulated amortization	1,300,536	922,592
	2,577,984	1,253,598
	$ 12,401,049	11,223,751

(Continued)

(6) Long-term Debt

Long-term debt at December 31, 1996 and 1995 are as follows:

	1996	1995
Revenue bond, Series 1978, 6%, due serially to 2011, with remaining installments ranging from $370,000 to $716,000	$ 7,936,000	7,936,000
General obligation bonds, Series 1976, interest ranging from 6% to 6.2%, in varying installments through 2001 with remaining annual installments ranging from $390,000 to $505,000	2,230,000	2,595,000
Note payable to St. Mary Parish, noninterest-bearing	22,575	38,486
	10,188,575	10,569,486
Less current installments of long-term debt	815,911	380,911
	$ 9,372,664	10,188,575

Revenue Bond, Series 1978 - In 1978, the Medical Center issued to the National Oceanic and Atmospheric Administration (NOAA), Office of Coastal Zone Management, its revenue bond in the amount of $10,636,000, secured by a pledge of the Medical Center's future revenue. The bond can be paid prior to maturity without penalty. In connection with the issuance of the 1978 revenue bond, the Medical Center is required to maintain funds in a revenue bond sinking fund, reserve fund, and depreciation fund. The reserve fund and the depreciation fund are to be funded up to certain amounts with excess revenue as defined in the Resolution. During 1994, the reserve fund was exhausted to pay the debt service payments on the revenue bond (see note 4).

The Medical Center is currently not in compliance with the Resolution as it does not have the required funds on deposit in the sinking fund, reserve fund and the depreciation fund. However, the revenue bond payment schedule cannot be changed as a result of the lack of required funds on deposit. The bondholders, after giving proper notice, have the right to appoint a receiver of the Medical Center, however the bondholders have indicated that they currently have no intention to exercise this right.

During 1994, the Medical Center requested a moratorium on interest and principal payments to NOAA. The Medical Center was granted a two year

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moratorium for its principal payments, however all interest payments were required to be paid in full by December 1995. All interest payments were made as required in December 1995.

General Obligation Bonds, Series 1976 - During 1976, the District issued $6,250,000 of general obligation bonds to acquire hospital buildings, machinery and equipment. The bonds are payable from the proceeds of a special ad valorem tax levied by the St. Mary Parish Police Jury over the period the bonds are outstanding. The tax receipts and related interest earned on invested unexpended tax receipts are restricted for the payment of principal and interest on the general obligation bonds (see note 4). The bonds are callable at the option of the District in inverse order of maturities on any interest payment date at the principal amount, plus a premium of up to 1.5%.

Note Payable to St. Mary Parish - In 1979, the Medical Center entered into a loan with the Parish of St. Mary, Louisiana, for $200,000. In 1986, the Hospital leased space to the Sheriff of St. Mary Parish for 15 years in satisfaction of the remaining unpaid principal amount of $166,667. During 1991 and 1993, the lease was amended to include additional office space for use by St. Mary Parish.

The Medical Center paid interest relating to long-term debt of approximately $624,000 and $883,000 during the years ended December 31, 1996 and 1995, respectively.

Aggregate maturities of the Medical Center's long-term debt at December 31, 1996 are as follows:

Year ended December 31	
1997	$ 815,911
1998	871,664
1999	915,000
2000	965,000
2001	1,015,000
Thereafter	5,606,000
	$ 10,188,575

(7) Leases

The Medical Center has entered into lease agreements that have been capitalized in accordance with Financial Accounting Standards Board Statement No. 13, Accounting for Leases. Under the terms of the leasing agreements, the Medical Center is obligated to pay a monthly rental

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payment over the primary term of the lease, which generally is for five years. Depending on the lease agreement, the Medical Center has the option to purchase the leased equipment at the fair market price, renew the lease for an additional lease term at the fair market rental rate, or return the equipment to the lessor. Future minimum lease payments at December 31, 1996 under capital lease obligations are as follows:

Year ending December 31:	
1997	$ 644,834
1998	644,834
1999	394,067
2000	394,067
2001	242,127
	2,319,929
Less imputed interest	(283,767)
Present value of future lease obligations	2,036,162
Less amounts due within one year	(525,009)
Long-term portion of capitalized lease obligations	$ 1,511,153

Leased assets included in equipment totaled $3,878,520 and $2,176,190 at both December 31, 1996 and 1995. Related accumulated amortization was $1,300,536 and $922,592, respectively. The leased equipment collateralizes the capital lease obligations.

The Medical Center is obligated under non-cancelable operating leases for equipment. Future lease payments for one of the leases is based upon patient usage. Amounts paid under this lease totaled $69,751 and $17,397 during 1996 and 1995, respectively. Other future minimum lease payments for operating leases having initial or remaining noncancelable lease terms in excess of one year as of December 31, 1996 are summarized as follows:

Year ending December 31:	
1997	$ 69,751
1998	64,851

(Continued)

Total rental expense incurred for all operating leases was $124,368 and $82,630 for the years ended December 31, 1996 and 1995, respectively.

The Medical Center leases office space to members of its medical staff under operating leases whose terms are generally for 5 years. Assets held for lease at December 31, 1996 consist of buildings and improvements with an original cost of $1,092,895. Accumulated depreciation of the leased assets totaled $429,031 at December 31, 1996. The future minimum lease rentals at December 31, 1996 to be received from these leases are as follows:

Year ending December 31	
1997	$ 74,643
1998	72,018
1999	72,018
2000	3,466
2001	3,177

(8) Net Patient Service Revenue

The Medical Center has agreements with governmental and other third-party payors that provide for reimbursement to the Medical Center at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Medical Center's billings at established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursement with major third-party payors follows:

- Medicare - Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates-per-discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

  Certain types of exempt inpatient and outpatient services related to Medicare beneficiaries are paid based upon a cost reimbursement methodology. The Medical Center is paid for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Medical Center and audits by the Medicare fiscal intermediary.

- Medicaid - Inpatient services rendered to Medicaid program beneficiaries are generally paid at an all-inclusive per diem rate. Outpatient services rendered to Medicaid program beneficiaries are reimbursed based upon a cost reimbursement methodology. The Medical

(Continued)

Center is paid at a tentative rate with final settlement determined after submission of annual cost reports by the Medical Center and audits by the Medicaid fiscal intermediary.

Presented below is a summary of net patient service revenue for the years ended December 31, 1996 and 1995:

	1996	1995
Gross patient service revenue	$ 36,261,259	33,072,864
Less provision for contractual adjustments	13,579,564	12,275,957
	$ 22,681,695	20,796,907

(9) Major Sources of Revenue

The Medical Center participates in the Medicare and Medicaid programs as a provider of medical services to program beneficiaries. The Medical Center derived 65% and 68% of its gross patient revenue in 1996 and 1995, respectively, from patients covered by the Medicare and Medicaid programs.

(10) 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. The Medical Center provided charity care of approximately $105,000 and $99,000 in 1996 and 1995, respectively, based upon foregone charges using established rates.

(11) Accrued Vacation

At December 31, 1996 and 1995, employees of the Medical Center have accumulated and vested $197,470 and $312,597, respectively, of employee leave benefits. This is recorded as an obligation of the Medical Center.

(12) Pension Plan

Effective January 1, 1996, the Medical Center adopted a defined contribution plan. Employees who have completed one year of service and are age 21 or older, are eligible to participate in the Plan. Plan participants are fully vested after 5 years of service or upon participant death or disability.

The amount contributed to the plan by the Medical Center is determined by the management of the Medical Center. Management approved a funding

(Continued)

level of 3% of each eligible participant's compensation as of July 7, 1996. No contributions were made prior to July 7, 1996. Compensation is defined as base pay up to a maximum of 80 hours for each pay period including regular hours worked, vacation and holidays. Total salaries for all employees for the period July 7, 1996 to December 31, 1996 were $4,707,153. Total covered compensation for eligible plan participants for the period July 7, 1996 to December 31, 1996 was $2,680,133. Plan contributions for the same period were $80,404. Loans to participants are not allowed and plan participants are allowed to direct the investment of their plan assets to those investment options designated by the plan administrator. The plan does not allow for investment in insurance policies or qualifying employer securities or employer real property.

(13) Business and Credit Concentration

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

At December 31, 1996, the Medical Center had net receivables from the Federal government (Medicare) of approximately $130,000 and the State of Louisiana (Medicaid) of approximately $173,000. Amounts included in due to third party payors represent estimated settlements to be paid to Medicare and Medicaid for all cost reports for which final settlements have not been made. Final settlement has been made by the intermediary for all years through December 31, 1993 for Medicare and Medicaid.

(14) Contingencies

The Medical Center participates in the Louisiana Hospital Association Trust Fund and the Louisiana Patients' Compensation Fund for medical malpractice claims. As a participant, the Medical Center 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 Trust Fund provides malpractice coverage for claims up to $100,000 and the Compensation Fund provides additional coverage on a claims-made basis for claims over $100,000 and up to $500,000.

The Medical Center provides health insurance benefits to its employees under a self-insured plan. The plan requires that the Medical Center pay the first $50,000 of covered benefits per employee. The Medical Center has reflected its estimate of the ultimate liability for known and incurred but not reported claims in the accompanying consolidated financial statements.

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Independent Auditors' Report

The Board of Commissioners
Hospital Service District No. 2 of
St. Mary Parish, Louisiana
(Lakewood Medical Center):

We have audited the financial statements of Hospital Service District No. 2 of St. Mary Parish, Louisiana (Lakewood Medical Center) as of and for the year ended December 31, 1996, and have issued our report thereon dated March 6, 1997.

We conducted our audit in accordance with generally accepted auditing standards, and *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 general purpose financial statements are free of material misstatement.

The management of Lakewood Medical Center is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure 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 accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of Lakewood Medical Center for the year ended December 31, 1996, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

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Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure 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 the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the general purpose 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 structure and its operation that we consider to be material weaknesses as defined above.

However, we noted certain matters involving the internal control structure and its operation that we have provided to the management of Lakewood Medical Center, in a separate letter dated March 6, 1997.

This report is intended for the information of the Board of Commissioners, management, and the Legislative Auditor. However, this report is a matter of public record and its distribution is not limited.

KPMG Peat Marwick LLP

March 6, 1997

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New Orleans, LA 70139-3599

Independent Auditors' Report

The Board of Commissioners
Hospital Service District No. 2 of
St. Mary Parish, Louisiana
(Lakewood Medical Center):

We have audited the financial statements of Hospital Service District No. 2 of St. Mary Parish, Louisiana (Lakewood Medical Center) as of and for the year ended December 31, 1996, and have issued our report thereon dated March 6, 1997.

We conducted our audit in accordance with generally accepted auditing standards, and *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 general purpose financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Lakewood Medical Center is the responsibility of Lakewood Medical Center's management. As part of obtaining reasonable assurance about whether the general purpose financial statements are free of material misstatement, we performed tests of Lakewood Medical Center's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of the audit of financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards*.

This report is intended for the information of the Board of Commissioners, management, and the Legislative Auditor. However, this report is a matter of public record and its distribution is not limited.

KPMG Peat Marwick LLP

March 6, 1997

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March 6, 1997

CONFIDENTIAL

The Board of Commissioners
Hospital Service District No. 2 of
St. Mary Parish, Louisiana
(Lakewood Medical Center)

Dear Members:

We have audited the financial statements of Hospital Service District No. 2 of St. Mary Parish, Louisiana (Lakewood Medical Center) for the year ended December 31, 1996, and have issued our report thereon dated March 6, 1997. In planning and performing our audit of the consolidated financial statements of Lakewood Medical Center, we considered internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control. A material weakness is a condition in which the design or operation of internal control components does not reduce to a relatively low level the risk that errors or irregularities 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. 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. However, we noted no matters involving internal control and its operation that we consider to be material weaknesses as defined above.

Status of Our Observations Dated March 14, 1996

Presented as appendix A is a summary of the current status of matters contained in our letter, dated March 14, 1996.

* * * * *

This report is intended solely for the information and use of the Board of Commissioners, management and others within Lakewood Medical Center.

We wish to acknowledge the cooperation and courtesy extended to us by the management and others of Lakewood Medical Center throughout the audit. Should you have any questions concerning the matters presented in this letter, we will be pleased to discuss them with you at your convenience.

Very truly yours,

KPMG Peat Marwick LLP

Summary of Status of Our Observations Dated March 14, 1996

Description of Comment	Fully implemented	In progress
Information Systems		X
Segregation of Duties		X
Observation of Bed Billings	X	