

ARTHUR ANDERSEN LLP

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JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

COMPREHENSIVE ANNUAL REPORT  
AS OF DECEMBER 31, 1997

Under provisions of state law, this report is a public document. A copy of the report has been submitted to the audited, or reviewed, 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 4-22-98

JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

COMPREHENSIVE ANNUAL REPORT

AS OF DECEMBER 31, 1997

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# ARTHUR ANDERSEN LLP

**JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1**

**COMBINED FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 1997 AND 1996  
TOGETHER WITH AUDITORS' REPORT**

# ARTHUR ANDERSEN LLP

## REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Parish Council of  
Jefferson Parish:

We have audited the accompanying combined balance sheets of Jefferson Parish Hospital Service District No. 1 (the Service District - a component unit of Jefferson Parish, Louisiana) as of December 31, 1997 and 1996, and the related combined statements of revenues and expenses and fund balance and cash flows for the years then ended. These combined financial statements are the responsibility of the Service District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and in accordance with the standards for financial audits contained in Government Auditing Standards (1994 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits 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 Jefferson Parish Hospital Service District No. 1 at December 31, 1997 and 1996, 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 on our consideration of the Service District's compliance and internal control over financial reporting dated February 27, 1998.

*Arthur Andersen LLP*

New Orleans, Louisiana,  
February 27, 1998

JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

COMBINED BALANCE SHEETS

DECEMBER 31, 1997 AND 1996

ASSETS

	<u>1997</u>	<u>1996</u>
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 7,937,243	\$ 8,830,967
Patient accounts receivable, less allowance for doubtful accounts of \$15,475,000 in 1997 and \$17,108,000 in 1996	22,823,191	20,672,634
Government health care program receivables	5,241,558	2,108,780
Inventory of drugs and supplies	2,423,259	2,646,458
Prepaid expenses	4,368,064	4,239,023
Assets whose use is limited that are required for current liabilities	<u>5,332,000</u>	<u>4,984,168</u>
Total current assets	<u>48,125,315</u>	<u>43,482,030</u>
<b>ASSETS WHOSE USE IS LIMITED (Note 2):</b>		
By board for specific purposes, at market	183,155,847	170,740,967
Trustee-held assets, at amortized cost	<u>57,923,418</u>	<u>60,138,760</u>
Total assets whose use is limited	241,079,265	230,879,727
Less amounts required for current liabilities	<u>(5,332,000)</u>	<u>(4,984,168)</u>
Noncurrent assets whose use is limited	<u>235,747,265</u>	<u>225,895,559</u>
PROPERTY, PLANT AND EQUIPMENT, net (Note 3)	<u>77,892,534</u>	<u>75,846,351</u>
<b>OTHER ASSETS:</b>		
Unamortized financing costs	4,222,157	4,712,674
Other	<u>4,986,139</u>	<u>5,875,774</u>
Total other assets	<u>9,208,296</u>	<u>10,588,448</u>
<b>Total</b>	<u>\$ 370,973,410</u>	<u>\$ 355,812,388</u>

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

JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

COMBINED BALANCE SHEETS

DECEMBER 31, 1997 AND 1996

LIABILITIES AND FUND BALANCE

	<u>1997</u>	<u>1996</u>
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 4,731,933	\$ 4,841,797
Accrued expenses	9,867,614	10,364,448
Patient deposits and credit balances	4,090,112	1,876,000
Current installments of long-term debt (Note 4)	3,515,000	3,310,000
Bond interest payable	<u>1,816,994</u>	<u>1,674,168</u>
Total current liabilities	24,021,653	22,066,413
RESERVE FOR ESTIMATED MALPRACTICE CLAIMS (Note 5)	2,100,000	1,900,000
LONG-TERM DEBT (Note 4)	159,449,999	162,964,999
CONTINGENCIES (Notes 5 and 6)		
FUND BALANCE	<u>185,401,758</u>	<u>168,880,976</u>
Total	<u>\$ 370,973,410</u>	<u>\$ 355,812,388</u>

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

JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

COMBINED STATEMENTS OF REVENUES AND EXPENSES AND FUND BALANCE

FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996

	<u>1997</u>	<u>1996</u>
OPERATING REVENUES:		
Net patient service revenue	\$ 133,542,554	\$ 126,754,760
Other operating revenues	<u>5,879,826</u>	<u>7,125,410</u>
Total operating revenues	<u>139,422,380</u>	<u>133,880,170</u>
OPERATING EXPENSES:		
Personnel	60,054,546	56,520,769
Professional fees	6,010,515	6,013,715
Medical and general supplies	23,986,460	22,582,241
Purchased services	11,559,930	9,521,951
Other expense	10,173,892	9,966,952
Bad debt expense	9,589,657	7,527,340
Depreciation	8,666,551	8,641,153
Interest expense, net of interest income from bond fund investments of \$4,692,000 in 1997 and \$4,986,000 in 1996	<u>4,719,920</u>	<u>5,048,904</u>
Total operating expenses	<u>134,761,471</u>	<u>125,823,025</u>
INCOME FROM OPERATIONS	4,660,909	8,057,145
INVESTMENT INCOME AND OTHER NONOPERATING REVENUES	<u>10,736,176</u>	<u>10,487,022</u>
EXCESS OF REVENUES OVER EXPENSES	15,397,085	18,544,167
FUND BALANCE AT BEGINNING OF YEAR	168,880,976	152,474,809
ASSESSMENTS BY JEFFERSON PARISH (Note 1)	(641,303)	(514,000)
UNREALIZED GAINS (LOSSES) ON AVAILABLE FOR SALE SECURITIES (Note 2)	<u>1,765,000</u>	<u>(1,624,000)</u>
FUND BALANCE AT END OF YEAR	<u>\$ 185,401,758</u>	<u>\$ 168,880,976</u>

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

JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

COMBINED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996

	<u>1997</u>	<u>1996</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Income from operations	\$ 4,660,909	\$ 8,057,145
Adjustments to reconcile income from operations to net cash provided by operating activities-		
Depreciation	8,666,551	8,641,153
Amortization of bond financing costs	490,517	490,518
Interest expense, net	4,719,920	5,048,904
Loss on sale of assets	136,479	-
Changes in assets and liabilities-		
Accounts receivable	(5,283,335)	(5,384,648)
Inventories and prepaid expenses	94,158	(676,637)
Other assets, net of non-cash items	889,635	717,777
Accounts payable	(109,864)	838,465
Accrued expenses, credit balances and malpractice	<u>1,917,278</u>	<u>1,846,464</u>
Net cash provided by operating activities	<u>16,182,248</u>	<u>19,579,141</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of investment securities	(1,113,095,995)	(41,624,988)
Proceeds from sales and maturities of investments	1,111,446,927	35,374,910
Investment income and other	<u>8,642,332</u>	<u>9,330,537</u>
Net cash provided by investing activities	<u>6,993,264</u>	<u>3,080,459</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Interest payments	(9,268,720)	(10,070,927)
Acquisitions of capital assets	(10,849,213)	(5,523,260)
Principal payments on borrowings	<u>(3,310,000)</u>	<u>(3,120,000)</u>
Net cash used in capital and related financing activities	<u>(23,427,933)</u>	<u>(18,714,187)</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>		
Transfers to other parish funds	<u>(641,303)</u>	<u>(514,000)</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>(893,724)</b>	<b>3,431,413</b>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<u>8,830,967</u>	<u>5,399,554</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<u><u>\$ 7,937,243</u></u>	<u><u>\$ 8,830,967</u></u>

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

JEFFERSON PARISH HOSPITAL SERVICE DISTRICT NO. 1

NOTES TO COMBINED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Organization

West Jefferson Medical Center (the Medical Center) and West Jefferson Service Corporation (the Service Corporation) operate under the jurisdiction of the Parish Council of Jefferson Parish, Louisiana (the Parish) as Jefferson Parish Hospital Service District No. 1 (the Service District) and are exempt from Federal and state income taxes. The Service District reports in accordance with the American Institute of Certified Public Accountants' "Audits of Providers of Health Care Services." As a governmental entity, the Service District also provides certain disclosures required by the Governmental Accounting Standards Board.

The Medical Center operates an acute care hospital, physician clinics, medical office buildings and a health and fitness center. The primary purpose of the Service Corporation is to support the activities of the Medical Center. It operates an outpatient imaging center (d/b/a West Jefferson Imaging Center) and provides management consulting services to its subsidiaries as well as various unrelated healthcare providers. The Service Corporation subsidiaries include Advance Care Center (formerly a subsidiary of the Service Corporation and a long-term inpatient hospital), Omega Claims, Inc. (a claims administration service begun during 1994) and Physicians Center Pharmacy, Inc. (a retail pharmacy). Advance Care Center ceased operations effective November 16, 1995, and the Medical Center entered into a lease with an unrelated entity that pays monthly rent for the space used to operate the long-term care facility. The Medical Center also entered an agreement with the unrelated entity under which a certain number of beds are reserved for use by Medical Center patients requiring long-term acute care. The Service Corporation is also the leasing agent for various medical office buildings owned by the Medical Center.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from these estimates.

The operations of all entities are included in the accompanying combined financial statements. All significant intercompany transactions have been eliminated in combination. Significant accounting policies used by the Service District in preparing and presenting its combined financial statements are summarized below.

### Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with a maturity of three months or less, excluding amounts whose use is limited by board designation or other arrangements under trust agreements or with third-party payors.

### Investments

Investments are stated in accordance with Statement of Financial Accounting Standards No. 115 (SFAS 115), Accounting for Certain Investments in Debt and Equity Securities. Investment income on trustee-held assets limited as to use is recorded within income from operations. All other realized investment income is recorded as non-operating revenue. See Note 2.

In March 1997 the Governmental Accounting Standards Board issued Statement No. 31 (GASB 31) "Accounting and Financial Reporting for Certain Investments and for External Investment Pools," which will be effective for the Service District for the year ended December 31, 1998. GASB 31 requires that investments be reported at fair value in the balance sheet and all investment income including changes in fair value of investments be reported as revenue in the statement of revenues and expenses. Had GASB 31 been applied at December 31, 1997, the carrying value of the Service District's investments would have been increased by approximately \$3,873,000.

### Inventory

Inventory, which consists primarily of drugs and supplies, is stated at the lower of cost (first-in, first-out) or market.

### Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is computed on the straight-line basis over estimated useful lives as follows:

Land improvements	10 years
Buildings	10-40 years
Fixed equipment	10-25 years
Major movable equipment	5-10 years
Minor equipment	3 years

### Costs of Borrowing

Deferred financing costs are amortized over the period the obligation is outstanding using the interest method.

### Other Assets

Other assets consist primarily of the Medical Center's 25% interest in a managed care organization and a 33% interest in a shared laundry co-operative, both of which are carried under the equity method of accounting.

Net Patient Service Revenue

The Service District has agreements with third-party payors that provide for payments to the Service District at amounts different from its established rates. Net patient service revenue is reported at the estimated net amounts realizable from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Government health care program receivables include settlements for 1991 and subsequent years which are subject to audit and retroactive adjustment by the intermediary and the Department of Health and Human Services. Payment arrangements with major third-party payors are summarized below:

- Government Programs - Services rendered to most Medicare and Medicaid program beneficiaries are paid at prospectively determined rates or fee schedules which may vary according to a patient classification system based on clinical, diagnostic and other factors. Certain outpatient services and defined capital costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology under which the Service District is paid at a tentative rate with final settlement determined after submission of annual cost reports by the Service District and audits thereof by the fiscal intermediary.
- Commercial Insurance - The Service District and subsidiaries of the Service Corporation have entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Service District under these agreements includes prospectively determined rates per discharge, discounts from established charges, prospectively determined daily rates and capitated per member per month rates.

The Service District derived a significant amount (approximately 45% in 1997 and 43% in 1996) of its net patient service revenue from patients covered by the Medicare and Medicaid programs and by Medicare health maintenance organization insurance plans. The Service District is unable to predict the future course of Federal, state and local regulation or legislation, including Medicare and Medicaid statutes and regulations. Further changes could have a material adverse effect on the financial results of the Service District.

Community Benefits

Services provided to the indigent and benefits provided to the broader community by the Medical Center for the years ended December 31, 1997 and 1996 are summarized below:

	<u>1997</u>	<u>1996</u>
Benefits for the Indigent (unpaid costs)- Traditional charity care	<u>\$ 1,643,000</u>	<u>\$ 1,440,000</u>
Benefits for the Broader Community-		
Unpaid costs of Medicare programs	3,894,000	3,217,000
Other community benefits	<u>1,021,000</u>	<u>894,000</u>
Total quantifiable benefits for the broader community	<u>4,915,000</u>	<u>4,111,000</u>
Total quantifiable community benefits	<u>\$ 6,558,000</u>	<u>\$ 5,551,000</u>

Benefits for the indigent include services provided to persons who cannot afford healthcare because of inadequate resources or who are uninsured. This includes the estimated costs of services associated with traditional charity care and other services such as emergency room services.

Benefits for the broader community include the unpaid cost of treating Medicare beneficiaries in excess of government payments. These benefits also include services provided to other needy populations that may not qualify as indigent but that need special services and support. Examples include the cost of health promotion and education, an assistance program for the elderly, health clinics and screenings, ground ambulance and air ambulance services, and special assessments by the Parish to fund healthcare for the Parish correctional center, all of which benefit the broader community.

Community benefit expense approximated 5% of total Service District operating expenses in 1997 and 1996.

Reclassifications

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

2. CASH AND INVESTMENTS:

Assets whose use is limited that are required for obligations classified as current liabilities are reported in current assets. The composition of assets whose use is limited at December 31, 1997 and 1996 is set forth below:

	1997 Carrying Value			1996 Total
	Cash Equivalents	U.S. Government Securities	Total	
Board designated	\$ 105,768	\$ 183,050,079	\$ 183,155,847	\$ 170,740,967
1986 Bond Issue	779	-	779	746
1988 Bond Issue	443,424	50,103,020	50,546,444	50,039,209
1985-A borrowings	1,269	-	1,269	1,201
1993 Bond Issue	<u>1,485,631</u>	<u>5,889,295</u>	<u>7,374,926</u>	<u>10,097,604</u>
Total Carrying Value	<u>\$ 2,036,871</u>	<u>\$ 239,042,394</u>	<u>\$ 241,079,265</u>	<u>\$ 230,879,727</u>
Total Market Value	<u>\$ 2,036,871</u>	<u>\$ 242,940,122</u>	<u>\$ 244,952,510</u>	<u>\$ 232,784,796</u>

Louisiana state statutes authorize the Service District to invest in obligations of the U. S. Treasury and other Federal agencies, time deposits with state banks and national banks having their principal offices in the State of Louisiana, guaranteed investment contracts issued by highly rated financial institutions and certain investments with qualifying mutual or trust fund institutions. During the years ended December 31, 1997 and 1996, the Service District invested primarily in securities issued by the U. S. Treasury and other Federal agencies. Louisiana state statutes also require that all of the deposits of the Service District be protected by insurance or collateral. The market value of collateral pledged must equal 100% of the deposits not covered by insurance. The bank balances of deposits at December 31, 1997 and 1996 were entirely covered by insurance or collateral held by financial institutions in the Service District's name.

The Service District's investments are categorized below to give an indication of the level of risk assumed at yearend. Category (a) includes investments that are insured or registered or for which the securities are held by the Service District or its agent in the Service District's name. Category (b) includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the Service District's name. Category (c) includes uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent, but not in the Service District's name. Balances at December 31, 1997 were as follows:

Securities Type	Credit Risk Category			Carrying Amount	Market Value
	(a)	(b)	(c)		
U.S. Government and Federal agencies' securities	\$ -	\$239,042,394	\$ -	\$ 239,042,394	\$ 242,940,122
Money market funds and other cash equivalents	<u>100,000</u>	<u>1,936,871</u>	<u>-</u>	<u>2,036,871</u>	<u>2,036,871</u>
Total investments	<u>\$ 100,000</u>	<u>\$240,979,265</u>	<u>\$ -</u>	<u>\$ 241,079,265</u>	<u>\$ 244,952,510</u>

The majority of the Service District's investments are classified as noncurrent because management does not intend to liquidate them for working capital purposes. The Service District reports investments in accordance with SFAS 115, which requires investments to be classified as either "available for sale," "held to maturity," or "trading." In previous years, all of the Service District's investments were classified as "held to maturity" and, accordingly, were carried on the amortized cost basis. During 1996, at the direction of the Jefferson Parish Council, management of the Board-designated investment portfolio was assigned to an outside investment management firm. As the Board-designated portfolio may be sold and reinvested in the near future, it is classified as "available for sale" and, accordingly, is carried at market value at December 31, 1996. As a result of this classification, unrealized gains of \$1,765,000 and unrealized losses of \$1,624,000 were recorded as a component of fund balance in 1997 and 1996, respectively.

### 3. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at December 31, 1997 and 1996 consists of:

	<u>1997</u>	<u>1996</u>
Land and land improvements	\$ 5,806,989	\$ 5,235,439
Buildings	58,139,168	56,380,372
Fixed equipment	38,630,701	38,630,701
Movable and other equipment	<u>83,220,862</u>	<u>76,248,458</u>
Total	185,797,720	176,494,970
Less- accumulated depreciation	<u>(107,905,186)</u>	<u>(100,648,619)</u>
Property, plant and equipment, net	<u>\$ 77,892,534</u>	<u>\$ 75,846,351</u>

The Service District leases certain major movable and other equipment under operating leases with terms predominantly on a month-to-month basis. Rental expenses for leased equipment amounted to approximately \$556,000 for 1997 and \$889,000 for 1996. During 1996, the Medical Center entered into an agreement whereby an outside firm is to manage the Information Systems function. Future commitments under this arrangement total \$2,596,000 at December 31, 1997. Extension of this arrangement is at the Medical Center's discretion beginning in September 1998.

#### 4. LONG-TERM DEBT

Long-term debt consists of:

	<u>1997</u>	<u>1996</u>
Customized Purchase Revenue and Refunding Bonds (Series 1986); variable interest rates (ranging from 3.50% to 4.35% in 1997 and 3.50% to 4.00% during 1996); due in 2026	\$ 48,000,000	\$ 48,000,000
Louisiana Public Facilities Authority Revenue Bonds (Series 1988); 7.9%, due in installments to 2015 (\$48,000,000 of the bond proceeds were placed in escrow to advance refund the Series 1986 bonds)	45,664,999	46,399,999
Louisiana Public Facilities Authority CP Program Hospital Equipment Financing and Refunding Revenue Bonds (Series 1985-A); variable interest rate (ranging from 4.43% to 5.75% in 1997 and 3.80% to 6.40% in 1996); due in varying principal installments from 1997 through 2005	17,000,000	18,550,000
Hospital Revenue Bonds (Series 1993); 3.60% - 5.40%; due in installments to 2019	<u>52,300,000</u>	<u>53,325,000</u>
Total	162,964,999	166,274,999
Less: Current maturities	<u>(3,515,000)</u>	<u>(3,310,000)</u>
Long-term debt, less current maturities	<u>\$ 159,449,999</u>	<u>\$ 162,964,999</u>
Total market value of long-term debt	<u>\$ 164,672,580</u>	<u>\$ 168,246,720</u>

Standard sinking fund payments on the Service District's long-term debt are as follows:

1998 (net of \$61,250 funded at December 31, 1997)	\$ 3,453,750
1999	3,630,000
2000	3,975,000
2001	4,962,916
2002	5,489,167
Thereafter	<u>141,454,166</u>
Total long-term debt	<u>\$162,964,999</u>

In 1985, the Medical Center issued \$52,100,000 of Hospital Revenue Bonds (Series 1985), repayable solely from the revenues of the Medical Center. The proceeds of the issue were used primarily to finance construction of a professional office building and a garage, purchase equipment and advance refund the Series 1979 Hospital Revenue Bond issue. Proceeds in the amount of \$27,580,000 were deposited with an escrow trustee and invested in obligations secured by the U.S. Government. The principal and interest income from these invested funds are used to service the debt of the refunded issue. Neither the escrow fund nor the Series 1979 bonds payable are shown in the accompanying balance sheets. Series 1979 bonds payable outstanding were \$28,415,000 at December 31, 1997 and 1996. The Series 1985 bonds were advance refunded through issuance of the Series 1986 bonds and the Series 1993 bonds as discussed below.

In 1986, the Medical Center issued \$48,000,000 of Hospital Revenue and Refunding Bonds (Series 1986) to be repayable from the revenues of the Medical Center. Additionally, the trustee of the bond issue is entitled to draw up to an amount sufficient to pay the outstanding principal of and up to 58 days of accrued interest on the bonds under a transferable irrevocable letter of credit. Proceeds of the Series 1986 Bonds were used to

provide funding for certain construction and equipment acquisitions at the Medical Center and advance refund certain debt issues. Approximately \$14,807,000 in proceeds from this issue and approximately \$22,599,000 from amounts held in connection with the advance refunded Series 1979 bonds were deposited with an escrow trustee and invested in obligations secured by the U. S. Government for redemption of \$30,710,000 of Series 1985 Hospital Revenue Bonds. The principal and interest from these investments are used to service the advance-refunded bonds payable. Of the Series 1985 issue bonds which were advance-refunded, \$15,000,000 was outstanding at December 31, 1997 and 1996. Neither the escrow fund nor the Series 1985 advance-refunded bonds payable are shown in the accompanying balance sheets.

During 1988, the Medical Center entered into a loan agreement with the Louisiana Public Facilities Authority to obtain financing of \$59,500,000 to refund the Series 1986 bonds and finance the cost of providing improvements and equipment for the Medical Center. Loan proceeds of \$48,000,000 were placed in escrow to provide for the future advance refunding of the Series 1986 bonds and to fund the debt servicing requirements of the related liability prior to the refunding. Amounts in the escrow fund will be used to redeem the Series 1986 bonds on any date directed by the Medical Center on or before December 1, 2001. Prior to redemption of the Series 1986 bonds, the interest on borrowed funds deposited in the escrow fund is payable solely from investments and earnings of the escrow fund. The Series 1988 loan agreement is secured by a lien on a pledge of revenues and requires the Medical Center charge rates sufficient to generate revenues in excess of expenses, exclusive of depreciation and interest expense, at a level that is greater than or equal to 120% of its maximum annual debt service requirement.

During 1991, the Medical Center borrowed \$20,000,000 through the Louisiana Public Facilities Authority CP Program Hospital Equipment Financing and Refunding Bonds (Series 1985-A) Program.

In January 1994, the Medical Center completed the issuance of \$55,265,000 of Hospital Revenue Bonds (Series 1993) to provide funds to (1) advance refund \$13,340,000 of the Series 1985 Hospital Revenue Bonds, (2) advance refund \$9,275,000 of the Series 1988 Bonds (3) finance acquisition, construction improvements, renovations and expansions of the Medical Center and (4) finance the costs incurred in connection with the issuance of the Bonds. The 1993 Bonds have a fixed rate of interest at an average yield of 5.67% and are due in varying installments through 2019.

#### 5. MALPRACTICE INSURANCE:

During 1976, the State of Louisiana enacted legislation that created a statutory limit of \$500,000 for each medical professional liability claim and established the Louisiana Patient Compensation Fund (State Insurance Fund) to provide professional liability insurance to participating health care providers. The constitutionality of the statutory limit has been tested and sustained to date although additional challenges may be made in the future. The Service District participates in the State Insurance Fund, which provides up to \$400,000 coverage for settlement amounts in excess of \$100,000 per claim. The Service District is self-insured with respect to the first \$100,000 of each claim and has excess insurance coverage with an annual aggregate limit of \$11,000,000 in excess of an annual deductible of \$1,500,000. In addition, the Service District is insured for claims under \$100,000 to the extent they exceed an annual aggregate of \$500,000. Malpractice suits involving claims of varying amounts have been filed against the Service District by various claimants. These actions are in various stages of processing and some may ultimately be tried before juries. The Service District believes the ultimate resolution of these claims will not have a material adverse effect on the Service District financial position or results of operations.

#### 6. GOVERNMENTAL REGULATIONS:

The healthcare industry is subject to numerous laws and regulations of Federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, and

Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Service District is in compliance with fraud and abuse as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

Legislation and regulation at all levels of government have affected and are likely to continue to affect the operation of the Service District. Federal healthcare reform legislation proposals debated in Congress in recent years have included the imposition of price controls and/or healthcare spending budgets or targets, significant reductions in Medicare and Medicaid program reimbursement to hospitals and the promotion of a restructured delivery and payment system focusing on competition among providers based on price and quality, managed care, and steep discounting or capitated payment arrangements with many, if not all, of the Service District's principal payors. It is not possible at this time to determine the impact on the Service District of government plans to reduce Medicare and Medicaid spending, government implementation of national and state healthcare reform or market-initiated delivery system and/or payment methodology changes. However, such changes could have an adverse impact on operating results, cash flows and estimated debt service coverage of the Service District in future years.

## 7 EMPLOYEE BENEFITS:

### Retirement Plan Description

The Service District contributes to the Retirement Plan for Employees of West Jefferson Medical Center (the Plan) which is a single-employer, noncontributory defined benefit pension public employee retirement system (PERS) which covers substantially all employees who meet certain length of service requirements. The Service District's total payroll for all employees and the Service District's total covered payroll for the year ended December 31, 1997, amounted to approximately \$49,814,000 and \$40,277,000, respectively, and \$47,154,000 and \$40,277,000, respectively, for the year ended December 31, 1996. Covered payroll refers to all compensation paid by the Service District to active employees covered by the plan on which contributions to the plan are based.

The Service District's PERS provides retirement benefits as well as death and disability benefits. Benefits do not vest until after ten years of service at which time benefits are 100% vested. The normal form of retirement benefit at age 65 is an actuarially equivalent joint and 50% contingent benefit payable for life in an amount approximating the sum of (1) 1.2% of final average monthly compensation multiplied by the number of years of credited service not in excess of thirty and (2) .65% of final average monthly compensation in excess of "covered" compensation multiplied by the number of years of credited service. The Plan issues a publicly available financial report that includes financial statements and required supplemental information.

Employer contributions to the Plan are invested primarily in equity and fixed income funds.

### Funding Status

The amount shown below as pension benefit obligation was determined as part of an actuarial valuation as of January 1, 1998 and represents a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases estimated to be payable in the future as a result of employee service to date. The measure is the actuarial present value of credited projected benefits and is

intended to help users assess the Plan's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due and make comparisons with other plans.

Annual Pension Cost and Net Pension Obligation:

Annual required contribution	\$ 911,398
Adjustment to annual required contribution	<u>-</u>
Annual pension cost	911,398
Contribution made	(911,398)
Increase in net pension obligation	-
Net pension obligation beginning of year	-
Net pension obligation end of year	<u>-</u>
	<u>\$ -</u>

Significant actuarial assumptions used in the valuation include a rate of return on the investment of present and future assets of 8.5% per year, compounded annually, and projected salary increases based on merit of 5% per year.

Contributions

The funding policy of the PERS provides for periodic employer contributions at actuarially determined rates that are sufficient to fund normal costs and amortization of past service costs over 30 years. The actuarially determined contribution requirement accrued in 1997 (to be paid in 1998) was \$911,398 and the contribution actually made in 1997 (accrued in 1996) was \$1,140,375. The actuarial unfunded liability at January 1, 1998 was \$1,723,220.

Significant actuarial assumptions used to compute contribution requirements are the same as those used to compute the standardized measure of the pension benefit obligation.

Trend Information

Historical trend information as of January 1 is presented in order to assess the progress made in accumulating sufficient assets to pay pension benefits as they become payable.

<u>Fiscal Year</u> <u>Ending</u>	<u>Annual</u> <u>Pension</u> <u>Cost (APC)</u>	<u>Percentage</u> <u>of APC</u> <u>Contributed</u>	<u>Net</u> <u>Pension</u> <u>Obligation</u>
12/31/95	\$ 1,419,308	100%	\$ -
12/31/96	1,140,375	100%	-
12/31/97	911,398	100%	-

The 1997 audited financial statements of the Plan include certain required supplementary information related to net actuarial value of assets and accrued liabilities, funded ratio and annual covered payroll.

Executive Benefits

The Service District provides a supplemental executive retirement plan (SERP) as well as a contributory flexible benefit plan to certain key employees. Service District contributions to the plans were \$254,000 in 1997 and \$312,000 in 1996. Assets and liabilities associated with the plans were approximately \$3,183,000 and \$2,882,000 at December 31, 1997 and 1996, respectively, and are included in current assets and liabilities in the accompanying financial statements.

8. CLASSIFICATION OF EXPENSES:

	<u>Salaries, Wages and Benefits</u>	<u>Supplies</u>	<u>Interest</u>	<u>Other</u>	<u>1997 Total</u>	<u>1996 Total</u>
Patient care	\$ 48,407,008	\$ 17,681,921	\$ -	\$ 4,781,299	\$ 70,870,228	\$ 67,135,320
Support services	<u>11,647,538</u>	<u>6,304,539</u>	<u>4,719,920</u>	<u>41,219,246</u>	<u>63,891,243</u>	<u>58,687,705</u>
Total expenses	<u>\$ 60,054,546</u>	<u>\$ 23,986,460</u>	<u>\$ 4,719,920</u>	<u>\$ 46,000,545</u>	<u>\$ 134,761,471</u>	<u>\$ 125,823,025</u>

9. CONCENTRATIONS OF CREDIT RISK:

The Service District 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 at December 31, 1997 and 1996, was as follows:

Medicare	24%	26%
Medicaid	14%	14%
Managed Care	34%	32%
Other third-party payors	17%	14%
Patients	<u>11%</u>	<u>14%</u>
	<u>100%</u>	<u>100%</u>



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## INDEPENDENT AUDITORS' REPORT

### REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Parish Council of Jefferson Parish:

We have audited the financial statements of Jefferson Parish Hospital Service District No. 1 (the Service District - a component unit of Jefferson Parish, Louisiana) as of and for the year ended December 31, 1997, and have issued our report thereon dated February 27, 1998. We conducted our audit in accordance with generally accepted auditing standards 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 Service District's financial statements are free of material misstatement, we performed tests of its compliance with certain provision of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

#### Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Service District'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.

This report is intended for the information of the audit committee and management, however, this report is a matter of public record and its distribution is not limited.

*Arthur Andersen LLP*

New Orleans, Louisiana,  
February 27, 1998



# ARTHUR ANDERSEN LLP

**RETIREMENT PLAN FOR EMPLOYEES OF  
WEST JEFFERSON MEDICAL CENTER**

**FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 1997 AND 1996  
TOGETHER WITH AUDITORS' REPORT**

# ARTHUR ANDERSEN

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Arthur Andersen LLP

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Suite 4500  
201 St Charles Avenue  
New Orleans LA 70170-4500  
504 581 5454

## REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

Retirement Plan for Employees of  
West Jefferson Medical Center:

We have audited the accompanying financial statements and supporting schedules of the Retirement Plan for Employees of West Jefferson Medical Center (the Plan) as of and for the years ended December 31, 1997 and 1996. These financial statements and supporting schedules are the responsibility of the Plan'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 in accordance with the standards for financial audits contained in Government Auditing Standards (1994 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits 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 and supporting schedules referred to above present fairly, in all material respects, the financial position of the Plan at December 31, 1997 and 1996 and the changes in its financial position for the years then ended in conformity with generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued a report on our consideration of the Service District's compliance and internal control other financial reporting dated February 27, 1998.

*Arthur Andersen LLP*

New Orleans, Louisiana,  
February 27, 1998

RETIREMENT PLAN FOR EMPLOYEES OF

WEST JEFFERSON MEDICAL CENTER

STATEMENTS OF PLAN NET ASSETS

DECEMBER 31, 1997 AND 1996

	<u>1997</u>	<u>1996</u>
ASSETS:		
Fixed income funds	\$10,294,968	\$ 9,715,199
Equity funds	15,985,068	11,854,776
Cash equivalents	5,722,567	4,926,640
Employer contributions receivable	911,398	1,140,375
Accrued income receivable	<u>124,830</u>	<u>148,255</u>
	33,038,831	27,785,245
LIABILITIES:		
Payable to employer for administrative expenses	<u>24,006</u>	<u>24,006</u>
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS	<u>\$33,014,825</u>	<u>\$27,761,239</u>

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

RETIREMENT PLAN FOR EMPLOYEES OF

WEST JEFFERSON MEDICAL CENTER

STATEMENTS OF CHANGES IN PLAN NET ASSETS

FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996

	<u>1997</u>	<u>1996</u>
ADDITIONS:		
Employer contributions	\$ 911,398	\$ 1,140,375
Investment income	<u>5,022,941</u>	<u>2,818,491</u>
Total additions	<u>5,934,339</u>	<u>3,958,866</u>
DEDUCTIONS:		
Benefits paid to participants and beneficiaries	642,992	543,145
Administrative expenses	<u>37,761</u>	<u>36,323</u>
Total deductions	<u>680,753</u>	<u>579,468</u>
NET INCREASE	5,253,586	3,379,398
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS, beginning of year	<u>27,761,239</u>	<u>24,381,841</u>
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS, end of year	<u>\$33,014,825</u>	<u>\$27,761,239</u>

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

RETIREMENT PLAN FOR EMPLOYEES OF

WEST JEFFERSON MEDICAL CENTER

NOTES TO FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996

1. PLAN DESCRIPTION:

General

West Jefferson Medical Center operates under the jurisdiction of the Parish Council of Jefferson Parish, Louisiana (the Parish) as Jefferson Parish Hospital Service District No. 1. A Louisiana Attorney General opinion empowers hospital service districts to create pension plans for officers and employees and to completely fund the plan with district funds. The Retirement Plan for Employees of West Jefferson Medical Center (the Plan) is a single-employer, non-contributory, defined benefit public employee retirement system (PERS). The Plan covers substantially all employees of West Jefferson Medical Center (the Employer) who meet certain length of service requirements and is funded through employer contributions and investment earnings. As a governmental entity, the Plan provides disclosures required by the Governmental Accounting Standards Board.

Plan Membership

At December 31, the Plan's membership consisted of:

	<u>1997</u>	<u>1996</u>
Active employees	1,377	1,314
Retirees and beneficiaries currently receiving benefits	163	141
Terminated employees entitled to, but not yet receiving, benefits	<u>203</u>	<u>190</u>
Total plan participants	<u>1,743</u>	<u>1,645</u>

Eligibility Requirements

An employee is eligible to participate in the Plan as of the date he or she has completed one year of service and attained the age of 21.

## Benefits

### Retirement

The Plan provides retirement benefits as well as death and disability benefits. All benefits are fully vested after 10 years of credited service. The basic annual retirement benefit at age 65 is a benefit payable for life in an amount equal to the number of years of credited service up to 30 years, multiplied by the sum of (1) 1.2% of final average monthly compensation and (2) .65% of final average monthly compensation in excess of "covered compensation," which is defined as the average of the Social Security Taxable Wage Base for the 35-year period ending the year in which social security normal retirement age is attained. Final average monthly compensation is defined as the monthly compensation of a participant averaged over the 5 consecutive calendar years which produces the highest monthly average within the last 10 calendar years preceding the earlier of retirement or termination of employment. Employees with 10 years of credited service may elect to receive a reduced benefit beginning at age 55.

### Deferred and Disability Benefits

A Plan member leaving employment after 10 years of credited service but before attaining retirement age or who ceases active employment because of total and permanent disability after 10 years of credited service but before attaining retirement age is eligible for deferred benefits or may elect to receive reduced benefits beginning on the early retirement date.

### Survivor Benefits

The survivor benefit provided under the Plan is a death benefit for a vested participant payable in the form of a survivor annuity. Such annuity payments are generally equal to 50% of the amount which would be payable to the participant if he had survived and elected to commence receiving a retirement income at the earliest date allowed under the plan.

## Contributions

The Employer is required to contribute amounts necessary to provide the benefits under the Plan determined by the application of accepted actuarial methods and assumptions.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING AND FINANCIAL REPORTING POLICIES.

### Basis of Accounting

The Plan's financial statements are prepared using the accrual basis of accounting.

### Employer Contributions

Employer contributions are recognized as revenues in the period in which employee services are performed.

### Investments

The assets of the Plan are invested in various fixed income, equity and short-term money market funds managed by a Trustee. Investments are carried at fair value as reported by the Trustee

### Administrative Expenses

All administrative expenses of the Plan are paid by the Employer and are to be reimbursed by the Plan.

### 3. CONTRIBUTIONS REQUIRED AND CONTRIBUTIONS MADE:

The funding policy of the Plan provides for periodic employer contributions at actuarially determined rates that are sufficient to pay benefits when due. The actuarial funding method used to determine the normal cost and the unfunded actuarial accrued liability, amortized over 30 years, for purposes of determining contribution requirements is the entry age normal cost method. The significant actuarial assumptions underlying the actuarial method used to compute the contribution requirements are the same as those used to compute the pension benefit obligation.

The actuarially determined contribution requirement for 1997, accrued by the employer and to be received by the Plan in 1998, was \$911,398. The actual contribution paid by the Employer during 1997 relating to the 1996 contribution requirement was \$1,140,375. The 1997 contribution requirement consisted of (a) \$728,137 normal cost, (b) \$111.861 amortization of the unfunded actuarial accrued liability and (c) \$71,400 net interest cost.

### 4. INVESTMENTS

The Plan has adopted certain investment policies, objectives, rules and guidelines which are intended to protect and preserve the Plan's assets while providing an appropriate return. The targeted overall mix of plan investments to meet these objectives are outlined below:

<u>Investment Class</u>	<u>Target</u>
Long-term bonds	15%
Intermediate bonds	20%
High-cap equity	45%
Growth equities	15%
Money market	5%

The fair value of individual investments that represent 5% or more of the Plan's total net assets as of December 31, 1997 is as follows:

Federated U. S. Government Trust Institutional Fund	\$ 6,551,116
Vanguard Fixed Income Securities Fund	3,743,852
Federated Growth Strategies Fund	2,031,060
SEI S&P500 Index Fund	13,954,008
Marquis Treasury Securities Money Market Fund	5,722,567

### 5. HISTORICAL TREND INFORMATION:

Historical trend information designed to provide information about the Plan's progress made in accumulating sufficient assets to pay benefits when due is presented as Schedules 1 and 2.

RETIREMENT PLAN FOR EMPLOYEES OF  
WEST JEFFERSON MEDICAL CENTER

REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF FUNDING PROGRESS

DECEMBER 31, 1997

(1) Actuarial Valuation Date	(2) Actuarial Value of Assets (AVA)	(3) Actuarial Accrued Liability (AAL)	(4) Unfunded Actuarial Accrued Liability (UAAL) (3) - (2)	(5) Funded Ratio (2)/(3)	(6) Annual Covered Payroll	(7) UAAL as Percent of Payroll (4)/(6)
01/01/93	\$16,915,000	\$19,973,478	\$3,058,478	84.7%	\$29,810,785	10.3%
01/01/94	19,000,000	22,683,471	3,683,471	83.8%	32,015,331	11.5%
01/01/95	19,588,000	25,934,315	6,346,315	75.5%	36,983,844	17.2%
01/01/96	23,743,000	27,596,935	3,853,935	86.0%	38,038,967	10.1%
01/01/97	26,228,000	29,532,330	1,304,330	95.6%	37,269,213	3.5%
01/01/98	32,500,000	34,223,220	1,723,220	95.0%	40,276,838	4.3%

RETIREMENT PLAN FOR EMPLOYEES OF  
WEST JEFFERSON MEDICAL CENTER

REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF EMPLOYER CONTRIBUTIONS

DECEMBER 31, 1997

<u>Fiscal Year</u>	<u>Annual Required Contribution</u>	<u>Percentage Contributed</u>
1992	\$ 998,714	100%
1993	967,683	100%
1994	1,047,919	100%
1995	1,419,308	100%
1996	1,140,375	100%
1997	911,398	100%

RETIREMENT PLAN FOR EMPLOYEES OF

WEST JEFFERSON MEDICAL CENTER

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

DECEMBER 31, 1997

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	January 1, 1998
Actuarial cost method	Entry Age Normal
Amortization method	Level payments closed
Remaining amortization period	30 years
Asset valuation method	Market value
Actuarial assumptions:	
Investment rate of return	8.50%
Projected salary increases	5.00%
Cost-of-living adjustments	None

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Arthur Andersen LLP

February 27, 1998

Suite 4500  
201 St Charles Avenue  
New Orleans LA 70170-4500  
504 581 5454

Mr. Mark McGinnis  
Senior Vice President/Finance  
West Jefferson Medical Center  
1101 Medical Center Boulevard  
Marrero, Louisiana 70072

Dear Mr. McGinnis:

As part of our audit of the financial statements for West Jefferson Medical Center (the Medical Center) for the year ended December 31, 1997, we considered the Medical Center's internal control structure in determining the scope of our audit procedures for the purpose of rendering an opinion on the financial statements. While our primary purpose in this engagement was not to provide assurances on the internal control structure, we noted certain matters that we want to bring to your attention.

Electronic Data Processing (EDP)

*Year 2000* - The primary issue surrounding the year 2000 pertains to computer systems that store dates in the format of Month - Day - Year ("MM-DD-YY") with only two characters allocated for the century identifier. For example, November 13, 2000 would be stored in the format 11-13-00. Computer hardware and software applications that use dates in this fashion will potentially interpret the date as November 13, 1900. All computer hardware and software is potentially at risk of producing unpredictable results or complete failure. It is important to note that resources are expected to become scarce and more expensive as the year approaches.

Eclipsys is currently conducting a formal analysis to determine hardware (computers, security systems, telecommunication systems, etc.) and other software (application software, system software, etc.) at risk. Management is also reviewing other equipment, such as medical devices/equipment and telephone systems, to determine any other risk related to Year 2000. Vendors should be contacted in writing as soon as possible to determine if their products are Year 2000 compliant, and if they are not compliant, vendors should be requested to provide their plans for becoming compliant.

Since the Year 2000 represents an immovable deadline, the Medical Center should complete the inventory analysis of hardware, software, and equipment as quickly as possible and consider its impact in the budgeting process. Additional resources may be required to

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manage and perform the process of replacing or upgrading noncompliant systems in order to ensure the deadline will be met. External resources should be contacted to determine availability and to obtain required commitments.

Management Response: Management agrees with Arthur Andersen regarding its observations regarding Year 2000 preparations. All purchases henceforth will require Year 2000 compliance. Management is also preparing a hospital-wide survey to identify additional Year 2000 problems and issues.

*Internal Controls* – During our discussions regarding the EDP systems used by the Medical Center, several areas were noted in which additional internal controls would improve the security and integrity of the systems.

- Information Systems Access Controls

Information Systems (IS) staff members have the ability to read, copy, and modify clinical, operational, and financial information on the computer system. Also, IS personnel currently perform security administration functions for selected financial and operational computer applications. The ability to bypass normal application security increases the risk that operational and financially significant information may be compromised, either through deliberate or unintentional actions. While it is not unusual for IS staff to have unrestricted access to data contained on the computer systems, minimal procedures should be considered to detect unusual access, such as:

- Establish system logging features for all updates to extremely sensitive data/applications, such as payroll and patient records
- Analyze end-user access rights to determine if current access rights match current employee job functions

Management Response: Management has instructed Eclipsys to establish system logging features and to analyze end-user access rights in accordance with Arthur Andersen's recommendation.

- Disaster Recovery

A comprehensive disaster recovery plan has been developed for the Medical Center which includes a section related to information systems; however, this plan has not been tested by Eclipsys or updated to reflect the changes made to the infrastructure.

The current disaster recovery plan should be reviewed and tested to ensure it adequately addresses disaster recovery risk for information systems and should be modified to include any procedures deemed necessary.

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Management Response: During 1998, management will review its current disaster recovery plan and modify it as deemed necessary.

- Physical Security

The help desk, print shop and operations manager's offices are located in the data center. Print jobs are placed outside the data center to be picked up by the requestor. Information security could be compromised due to non-operations personnel in the data center with access to high-powered consoles, which give the operator access to any operating system or application and by non-authorized access to the data center. The data center should be restricted to only data processing equipment, networking equipment, and operators.

Also, the keypad access to the data center can be bypassed by anyone with a key to the door, so that there is no means of tracking entry into the data center. To provide increased security, the keypad should be used to restrict access to the data center and to track activity in the data center.

Management Response: Access to the data center is limited to those individuals who work in that area. Management will reinforce the policy of utilizing the keypad security system.

## Modification of Bad Debt Template Calculation

The Medical Center captures reserves for bad debt and contractual allowances in several general ledger accounts and uses a template calculation to determine the bad debt allowance required on accounts receivable. Given the changes in the reimbursement generated by the growth in managed care, capitation, and the changes in Medicare and Medicaid payment structures, the reserve methodology and mechanics of booking entries to capture write off's, contractual adjustments, and reserves for such items should be reviewed to ensure that current procedures and calculations are consistent with current reimbursement and provide a mechanism for management to easily monitor reserves.

Management Response. Management agrees with Arthur Andersen's recommendation and will revise its template during 1998.

This letter is intended solely for the use of management and the Board of Directors and is not intended for any other purpose.

We appreciate the courtesies and cooperation extended to our representatives during the course of their work. We would be pleased to discuss the recommendations in greater detail or otherwise assist in their implementation at your convenience.

Very truly yours,

Arthur Andersen LLP