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Hospital Service District No. 1 of Iberia Parish, State of Louisiana
(d/b/a Iberia Medical Center)

Management's Discussion and Analysis and Basic Financial Statements

Years ended September 30, 2003 and 2002 with Report of Independent Auditors

Hospital Service District No. 1 of Iberia Parish,
State of Louisiana (d/b/a Iberia Medical Center)

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Years ended September 30, 2003 and 2002

Contents

Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center)

Management's Discussion and Analysis

This section of the annual financial report for Iberia Medical Center (the "Medical Center") presents background information and management's analysis of the Medical Center's financial performance during the fiscal year that ended on September 30, 2003. Please read it in conjunction with the basic financial statements in this report.

Required Financial Statements

The basic financial statements in this report are presented using Governmental Accounting Standards Board ("GASB") accounting principles. These financial statements offer short-term and long-term financial information about the Medical Center's activities.

The balance sheets include all of the Medical Center's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to Medical Center creditors (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of the Medical Center, and assessing the liquidity and financial flexibility of the Medical Center.

All of the current year's revenues and expenses are accounted for in the statements of revenue, expenses, and changes in net assets. This statement measures changes in the Medical Center's operations over the past years and can be used to determine whether the Medical Center has been able to recover all of its costs through its patient service revenue and other revenue sources.

The final required financial statement is the statement of cash flows. The primary purpose of this statement is to provide information about the Medical Center's cash from operating, investing, and financing activities, and to provide answers to such questions as where did cash come from, what was cash used for, and what was the change in cash balance during the reporting period.

Financial Analysis of the Medical Center

The balance sheets and the statements of revenue, expenses, and changes in net assets report information about the Medical Center's activities. Increases or decreases in the Medical Center's net assets are one indicator of whether its financial health is improving or deteriorating. However, other nonfinancial factors such as changes in the health care industry, changes in Medicare and Medicaid regulations, and changes in managed care contracting should also be considered.

Balance Sheets

The Medical Center's condensed balance sheets are presented in Table 1.

TABLE 1

	September 30 2003	September 30 2002	Dollar Change	Percent Change
	(In Thousands)			
Total current assets	**$ 16,634**	$ 12,735	$ 3,899	31%
Property and equipment – net	**18,975**	19,034	(59)	–
Other assets	**4,241**	4,076	165	4
Total assets	**$ 39,850**	$ 35,845	$ 4,005	11%
Current liabilities	**$ 8,316**	$ 7,278	$ 1,038	14%
Long-term debt and capital lease obligations	**17,851**	15,882	1,969	12
Total liabilities	***26,167***	*23,160*	*3,007*	*13*
Net assets	**13,683**	12,685	998	8
Total liabilities and net assets	**$ 39,850**	$ 35,845	$ 4,005	11%

During 2003, the Medical Center's total assets increased by $4,005,000, or 11%, primarily due to the issuance of $3,000,000 of bonds during the year plus the cash flow generated from operations and investment activities exceeding amounts invested in equipment.

Current Assets

Increases in current assets, concentrated in growth in cash and cash equivalents, outpaced increases in current liabilities in 2003 indicating improved liquidity at September 30, 2003 versus September 30, 2002. The Medical Center's current ratio improved from 1.75 at the end of the prior year to 2.0 at September 30, 2003.

Capital Assets

The following table presents the components of property and equipment at September 30, 2003 and 2002.

TABLE 2

	September 30	
	2003	**2002**
	(In Thousands)	
Land and improvements	**$ 1,385**	$ 1,380
Building and improvements	**15,242**	14,937
Medical office building	**8,347**	8,347
Fixed equipment	**4,383**	4,383
Major movable equipment	**18,554**	17,798
	47,911	46,845
Accumulated depreciation and amortization	**(29,199)**	(27,870)
Construction in progress	**263**	58
Net property and equipment	**$ 18,975**	$ 19,033

During fiscal year 2003, the Medical Center invested $1,447,000 in capital assets. The source of the funding for these projects was derived primarily from operations. Assets with a net book value of $176,000 were disposed of during 2003.

In Table 3, the Medical Center's fiscal year 2004 capital budget projects spending up to $4,012,000 for capital projects. These projects are expected to be financed from operations and the proceeds from the 2003 bond offering.

TABLE 3

Equipment purchases	$ 1,032,000
Construction/renovation	2,980,000
Total	$ 4,012,000

Debt

The Medical Center has pledged its revenue and assets as collateral for Hospital Revenue Bonds issued by Iberia Parish. The Medical Center has agreed to fund the interest and principal payments as they become payable. Accordingly, these Bonds have been recognized as obligations of the Medical Center.

At September 30, 2003, the Medical Center had $18,875,000 in outstanding debt excluding capital leases. The debt amount is presented in the balance sheet net of an unamortized reacquisition premium of $492,000. During fiscal year 2003, Iberia Parish issued $3,000,000 of additional bonds on behalf of the Medical Center. Principal payments of $785,000 were made during this fiscal year. Total debt outstanding represents approximately 46% of the Medical Center's total assets at September 30, 2003.

The Medical Center made principal payments of $90,000 on the obligations under capital leases during the current fiscal year.

Net Assets

The following table presents the components of the Medical Center's net assets at September 30, 2003 and 2002.

TABLE 4

	September 30	
	2003	**2002**
Invested capital assets, net of related debt	**$ 2,948**	$ 2,276
Restricted	**4,526**	4,346
Unrestricted	**6,208**	6,063
	$ 13,682	$ 12,685

Net assets increased $998,000 during 2003, indicating an improvement in financial condition.

During 2003, the Medical Center issued $3,000,000 of debt that is considered related to the capital assets. As substantially all of the proceeds from this offering are still held at September 30, 2003, there was no reduction in the component of net assets invested in capital assets, net of related debt. Principal pay downs, net of amortization, on the capital- related debt and loans approximated $830,000 during 2003. This increases the amount of reported net assets in this component. Additions to property and equipment were approximately $52,000 less than the current year depreciation further reducing this component of net assets.

Changes in the cash and investment balances held by the trustee under the bond indenture and under the self-insurance trust arrangement resulted in the $180,000 increase in the restricted component of net assets.

Statements of Revenue and Expenses

The Medical Center's condensed revenues and expenses for fiscal years 2003 and 2002 are presented in Table 5.

TABLE 5

	Year ended September 30 2003	2002	Dollar Change	Percent Change
	(In Thousands)			
Revenue:				
Net patient service revenue	**$ 37,221**	$ 35,226	$ 1,995	6%
Other revenue	**575**	523	52	10
Total operating revenue	**37,796**	35,749	2,047	6
Expenses:				
Salaries, wages, and benefits	**19,499**	17,537	1,962	11
Supplies and other expenses	**15,885**	14,329	1,556	11
Debt refinancing costs	**–**	369	(369)	(100)
Depreciation and amortization	**1,517**	1,596	(79)	(5)
Interest expense	**1,033**	1,107	(74)	(7)
Total operating expenses	**37,934**	34,938	2,996	9
Operating revenue in excess (deficit) of operating expenses	**(138)**	811	(949)	(117)
Nonoperating gains, net	**1,019**	847	172	20
Revenue and gains in excess of expenses	**$ 881**	$ 1,658	$ (777)	(47)%

During the year, the Medical Center's total operating revenues increased $2,047,000, or 6%, to $37,796,000 while expenses increased $2,996,000, or 9%, to $37,934,000. The Medical Center had a loss from operations of $138,000, which is 0.4% of total operating revenue. This compares to the prior fiscal year's income from operations of $811,000, or 2%, of operating revenue.

Operating Revenue

During fiscal year 2003 and 2002, the Medical Center derived 99% of its total operating revenue from net patient service revenue. Total net patient service revenue increased $1,995,000, or 6%, in 2003. Overall activity at the Medical Center, as measured by patient discharges, increased 10% to 4,761 discharges in 2003 from 4,329 discharges in 2002. Patient days increased 9% over prior year from 14,534 in 2002 to 15,866 in 2003. The average length of stay for all patients was 3.3 days in 2003 and 2002.

Table 6 presents the relative percentages of gross charges billed for patient services by payer type for fiscal years 2003 and 2002.

TABLE 6

	Year ended September 30	
	2003	**2002**
Medicare	**43%**	46%
Managed care	**35**	34
Medicaid	**15**	13
Self-pay and other	**7**	7
	100%	100%

The following table presents the contractual allowances on gross billings by payer and the provision for doubtful accounts for fiscal years 2003 and 2002.

TABLE 7

	Year ended September 30	
	2003	**2002**
	(In Thousands)	
Contractual allowances:		
Medicare	**$ 32,301**	$ 29,182
Managed care and commercial insurers	**20,019**	15,217
Medicaid	**13,698**	9,998
Other adjustments	**1,640**	740
Total contractual allowances	**67,658**	55,137
Provision for doubtful accounts	**5,534**	4,695
	$ 73,192	$ 59,832

Allowances increased over prior year due to realized contract rate increases not keeping pace with charge rate increases.

Operating Expenses

Employee-related costs increased $1,962,000, or 11%, to $19,499,000 in 2003 from $17,537,000 in 2002. As a percentage of net patient service revenue, these costs were 52% in 2003 and 49% in 2002. This increase is attributed to an increase of $1,167,000 in salaries and wages reflecting patient volume increases of approximately 10%, wage increases and an increase of $795,000 in employee benefits primarily related to health insurance expenses. Supplies and other operating expenses increased $1,556,000, or 11%, from the prior fiscal year. As a percentage of net patient service revenue, these expenses increased to 43% in 2003 from 41% in 2002. The increase in this percentage also reflects patient volume increases of approximately 10%, combined with supplier price increases.

Depreciation and amortization expense decreased $79,000 to $1,517,000 for 2003 from $1,596,000 for 2004. The increase in depreciation expense due the Medical Center's investment in capital assets during 2003 was less than the reduction in depreciation expense due to those assets that became fully depreciated during the current year.

Interest expense decreased $74,000 to $1,033,000 for 2003 from $1,107,000 for 2002. The Medical Center's higher interest rate debt was refinanced during 2002. The lower borrowing costs for all debt outstanding during 2003 more than offset the impact of the additional borrowings made during the current year.

Nonoperating Gains

The following table summarizes nonoperating gains for fiscal years 2003 and 2002.

TABLE 8

	Year ended September 30 2003	2002
	(In Thousands)	
Rental income	**$ 389**	$ 337
Dividends received from joint venture	**450**	314
Equity in undistributed earnings of New Iberia Surgery Center	**137**	(15)
Other	**43**	211
	$ 1,019	$ 847

Contacting the Medical Center's Financial Manager

This financial report is designed to provide our citizens, customers, and creditors with a general overview of the Medical Center's finances and to demonstrate the Medical Center's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Medical Center Administration.

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Report of Independent Auditors

The Board of Commissioners
Hospital Service District No. 1 of Iberia Parish,
State of Louisiana (d/b/a Iberia Medical Center)

We have audited the accompanying balance sheets of Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center) (the "Medical Center") as of September 30, 2003 and 2002, and the related statements of revenue, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Medical Center's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States and in accordance with the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Medical Center at September 30, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

As discussed in Note 1 to the financial statements, effective October 1, 2002, the Medical Center changed its accounting policy related to financial statement presentation in order to comply with the provisions of Statement No. 34 of the Government Accounting Standards Board ("GASB").

Management's discussion and analysis on pages i through viii is not a required part of the basic financial statements but is supplementary information required by the GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report as of and for the period ended September 30, 2003 on our consideration of the Medical Center's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Ernst + Young LLP

January 9, 2004

Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center)

Balance Sheets

	September 30 2003	September 30 2002
Assets		
Current assets:		
Cash and cash equivalents	**$ 6,829,284**	$ 3,411,696
Patient accounts receivable, less allowance for doubtful accounts of $5,777,000 and $4,627,000 in 2003 and 2002, respectively	**6,684,846**	6,611,297
Other receivables	**727,559**	622,363
Inventories	**1,288,609**	1,206,393
Prepaid expenses	**212,492**	165,643
Current portion of assets limited as to use	**890,968**	717,583
Total current assets	**16,633,758**	12,734,975
Assets limited as to use, less current portion	**3,635,428**	3,628,191
Property and equipment, net	**18,974,633**	19,033,337
Investments in joint ventures	**474,605**	337,111
Bond issuance costs, net	**131,262**	110,924
Total assets	**$ 39,849,686**	$ 35,844,538
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 2,886,710**	$ 3,098,402
Employee-related accruals	**2,344,463**	2,144,930
Due to third-party payers	**1,660,653**	834,877
Accrued interest payable	**348,695**	324,513
Current installments of debt and capital lease obligations	**1,076,013**	874,803
Total current liabilities	**8,316,534**	7,277,525
Debt and capital lease obligations, less current portion:		
Iberia Parish bonds payable	**17,402,830**	15,338,000
Capital lease obligations	**447,896**	543,992
	17,850,726	15,881,992
Total liabilities	**26,167,260**	23,159,517
Net assets:		
Invested in capital assets, net of related debt	**2,947,570**	2,276,542
Restricted	**4,526,396**	4,345,774
Unrestricted	**6,208,460**	6,062,705
Total net assets	**13,682,426**	12,685,021
Total liabilities and net assets	**$ 39,849,686**	$ 35,844,538

See accompanying notes.

Hospital Service District No. 1 of Iberia Parish,
State of Louisiana (d/b/a Iberia Medical Center)

Statements of Revenue, Expenses, and Changes in Net Assets

	Year ended September 30	
	2003	**2002**
Net patient service revenue	**$ 37,220,776**	$ 35,225,832
Other revenue	**575,236**	522,946
Total operating revenue	**37,796,012**	35,748,778
Operating expenses:		
Salaries, wages, and benefits	**19,498,703**	17,536,693
Supplies and other expenses	**15,884,790**	14,328,943
Depreciation and amortization	**1,516,919**	1,595,861
Interest expense	**1,033,483**	1,107,675
Debt refinancing costs	**–**	368,805
Total operating expenses	**37,933,895**	34,937,977
Operating revenue in excess (deficit) of operating expenses	**(137,883)**	810,801
Nonoperating gains, net	**1,019,344**	846,985
Revenue and gains in excess of expenses	**881,461**	1,657,786
Increase in restricted net assets	**115,944**	187,592
Net assets at beginning of year	**12,685,021**	10,839,643
Net assets at end of year	**$ 13,682,426**	$ 12,685,021

See accompanying notes.

Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center)

Statements of Cash Flows

	Year ended September 30 2003	2002
Operating activities		
Operating revenue collected	**$ 38,483,669**	$ 35,293,734
Cash payments to employees and for employee-related costs	**(19,290,170)**	(17,360,158)
Cash payments for operating expenses	**(16,353,433)**	(14,852,061)
Net cash provided by operating activities	**2,840,066**	3,081,515
Capital and related financing activities		
Purchases of property and equipment	**(1,447,419)**	(1,024,841)
Proceeds from sales of property and equipment	**10,000**	–
Repayments of amounts due to Iberia Parish	**–**	(1,000,000)
Proceeds from the issuance of debt by Iberia Parish	**3,000,000**	16,910,000
Principal payments on Hospital Service District debt	**–**	(16,985,487)
Premium paid through debt refunding	**–**	(567,250)
Principal payments on Iberia Parish debt	**(785,000)**	(250,000)
Principal payments on capital lease obligations	**(89,886)**	(129,601)
Costs paid related to bond issuance	**(29,306)**	(116,403)
Interest payments on debt and capital lease obligations	**(964,471)**	(1,047,162)
Net cash used in capital and related financing activities	**(306,082)**	(4,210,744)
Investing activities		
Interest received on cash and investments	**179,245**	265,418
Net decrease (increase) in assets limited as to use	**49,650**	(50,933)
Dividends received from joint ventures	**449,558**	313,944
Other nonoperating income received	**435,423**	545,101
Net cash provided by investing activities	**1,113,876**	1,073,530
Net increase (decrease) in cash and cash equivalents	**3,647,860**	(55,699)
Cash and cash equivalents, beginning of year	**5,661,970**	5,717,669
Cash and cash equivalents, end of year	**$ 9,309,830**	$ 5,661,970
Reconciliation of cash and cash equivalents to the balance sheet:		
Cash and cash equivalents in current assets	**$ 6,829,284**	$ 3,411,696
Cash and cash equivalents in assets limited as to use:		
Held by trustee under bond indenture	**1,942,281**	1,702,829
Under self-insurance trust arrangements	**538,265**	547,445
	$ 9,309,830	$ 5,661,970
Reconciliation of income from operations to net cash provided by operating activities		
Gain (loss) from operations	**$ (137,883)**	$ 810,801
Adjustments to reconcile gain (loss) from operations to net cash provided by operating activities:		
Gain on sale of property and equipment	**(10,000)**	–
Depreciation and amortization	**1,506,123**	1,584,154
Debt refinancing costs	**–**	368,805
Amortization of bond issuance costs	**8,968**	11,707
Amortization of debt reacquisition premium	**44,830**	30,000
Provision for doubtful accounts	**5,533,880**	4,695,418
Interest expense, net	**924,075**	998,100
Changes in operating assets and liabilities:		
Patient receivables, net	**(5,607,429)**	(5,050,897)
Other receivables	**(107,050)**	(151,957)
Prepaid expenses	**(46,849)**	(6,722)
Inventories	**(82,216)**	(128,754)
Accounts payable and accrued expenses	**(12,159)**	(59,150)
Amounts due to third-party payers	**825,776**	(19,990)
Net cash provided by operating activities	**$ 2,840,066**	$ 3,081,515

See accompanying notes.

Hospital Service District No. 1 of Iberia Parish,
State of Louisiana (d/b/a Iberia Medical Center)

Notes to Basic Financial Statements

September 30, 2003

1. Organization and Significant Accounting Policies

Organization

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

Basis of Accounting

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

New Accounting Standards

GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments,* Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments Omnibus,* and Statement No. 38, *Certain Financial Statement Note Disclosures,* (the "Statements") which establish financial reporting standards for state and local governments. These statements establish that the financial statements and required supplementary information ("RSI") for general-purpose governments should consist of Management's Discussion and Analysis ("MD&A") to provide an analytical overview of the entity's financial activities, Basic Financial Statements, and RSI. The

1. Organization and Significant Accounting Policies (continued)

Statements are effective for the Medical Center in fiscal year 2003. Adoption of these standards did not have any effect on the financial position or results of operations of the Medical Center.

Statement No. 34 established standards for external financial reporting for all state and local governmental entities, which include a balance sheet; a statement of revenue, expenses, and changes in net assets; and a direct method statement of cash flows. It requires the classification of net assets into three components – invested in capital assets, net of related debt, restricted, and unrestricted. These components are defined as follows:

- Invested in capital assets, net of related debt – This component reports capital assets, including restricted capital assets, net of accumulated depreciation, and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds should not be included in this component of net assets. Rather, that portion of debt should be included in the same net assets component as the unspent proceeds. At December 31, 2003, $2,900,000 of unspent bond proceeds were included in unrestricted net assets.

- Restricted – This component reports those net assets with externally imposed constraints placed on their use by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

- Unrestricted – This component reports net assets that do not meet the definition of either of the other two components.

The adoption of the Statements resulted in the previously reported unrestricted fund balance amount being classified to conform to the above net asset components. Additionally, the Medical Center restated the 2002 statement of cash flows to conform to the direct method of reporting cash receipts and disbursements.

The Statements also require that the Medical Center recognize the provision for doubtful accounts as a component of net patient service revenue.

1. Organization and Significant Accounting Policies (continued)

Use of Estimates

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

Operating and Nonoperating Revenue

The Medical Center's primary purpose is to provide diversified health care services to individuals, physicians, and businesses in Iberia Parish and the surrounding communities. As such, activities related to the ongoing operations of the Medical Center are classified as operating revenues. Operating revenues include those generated from direct patient care, related support services, gains or losses from disposition of operating properties, and sundry revenues related to the operation of the Medical Center.

Investment income from unrestricted and board-designated investments is reported as other operating revenue. Investment income from trusteed investments held under a related bond indenture is reported in nonoperating gains. Additionally, rental income, gains and losses not directly related to the ongoing operations of the Medical Center or that occur infrequently, and gifts, grants, and bequests not restricted by donors for specific purposes are reported as nonoperating gains.

Cash Equivalents

Cash equivalents include investments in highly liquid investments with maturities of three months or less when purchased, excluding amounts whose use is limited by board designation or under trust agreements.

Investments

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

1. Organization and Significant Accounting Policies (continued)

Assets Limited as to Use

Assets limited as to use include cash, cash equivalents, and investments. These assets are designated as such in the accompanying balance sheet as they are held by bond trustees under related indenture agreements, or held under self-insurance trust arrangements.

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

Investments in Joint Ventures

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

Income earned on investments accounted for on the equity method and dividends received on investments accounted for on the cost basis are included as components of nonoperating gains.

Net Patient Service Revenue

The Medical Center provides medical services to government program beneficiaries and has agreements with other third-party payers that provide for payments at amounts different from established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts billed to patients, third-party payers, and others for services rendered. The percentage of total net patient service revenue derived from services furnished to Medicare and Medicaid program beneficiaries combined was approximately 41% in 2003 and 43% in 2002.

1. Organization and Significant Accounting Policies (continued)

Retroactive settlements are provided for in some of the governmental payment programs outlined above, based on annual cost reports. Such settlements are estimated and recorded as amounts due to or from third-party payers in the financial statements. The differences between these estimates and final determination of amounts to be received or paid are based on audits by fiscal intermediaries and are reported as adjustments to net patient service revenue when such determinations are made. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. These adjustments resulted in decreases to net patient service revenue of $684,000 in 2003 and $117,000 in 2002. Estimated settlements through September 30, 1999 for the Medicaid program, and September 30, 2000 for the Medicare program, have been reviewed by program representatives, and adjustments have been recorded to reflect any revisions to the recorded estimates required. The effect of any adjustments that may be made to cost reports still subject to review at September 30, 2003 will be reported in the Medical Center's financial position or results of operations as such determinations are made.

Inventories

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

Property and Equipment

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

Unamortized Bond Issuance Costs

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

1. Organization and Significant Accounting Policies (continued)

Income Taxes

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

Reclassifications

The prior year financial statements have been reclassified to conform to their current year presentation.

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

The Medical Center provides four full-time nurses at the Parish Criminal Justice Facility for medical assistance to the individuals in the facility. The Medical Center does not maintain records to identify and monitor the level of charity care it provides under this program; however, the total cost of providing this service approximated $140,000 in 2003 and $143,000 in 2002.

3. Cash and Investments

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

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

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

Category 3 – Uncollateralized, including balances collateralized with securities held by the pledging financial institution.

A summary of cash and investments at September 30, 2003 follows:

	Category 1	Category 2	Category 3	Total
Cash and cash equivalents	$ 200,000	$ 6,629,284	$ –	$ 6,829,284
Held by trustee under bond indenture:				
Cash and cash equivalents	$ –	$ –	$ 1,942,281	$ 1,942,281
U.S. Treasury Notes	1,859,864	–	185,986	2,045,850
	1,859,864	–	2,128,267	3,988,131
Held under self-insurance trust arrangements:				
Cash and cash equivalents	–	538,265	–	538,265
Total assets limited as to use	$ 1,859,864	$ 538,265	$ 2,128,267	$ 4,526,396

3. Cash and Investments (continued)

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

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

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

Trusteed bond funds are maintained in accordance with the requirements of the indentures related to the Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds and Parish of Iberia, State of Louisiana Hospital Revenue Bonds.

A summary of the trusteed funds at September 30 follows:

	2003	2002
Debt service reserve funds	**$ 2,146,992**	$ 2,095,500
Principal and interest project funds	**796,161**	683,625
Depreciation reserve fund	**1,044,978**	1,019,204
	3,988,131	3,798,329
Less amounts classified as current assets	**890,968**	717,583
	$ 3,097,163	$ 3,080,746

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

4. Investments in Joint Ventures

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

	2003	2002
New Iberia Surgery Center	**$405,605**	$268,111
Acadiana Diagnostic Imaging LLC	**69,000**	69,000
	$474,605	$337,111

The Medical Center received $450,000 of dividends from these joint ventures in 2003 and $314,000 in 2002. Additionally, the Medical Center provides certain personnel and supplies to the joint ventures for a fee and recognizes payment for these services and supplies as other operating income. These amounts were $186,000 in 2003 and $180,000 in 2002.

5. Business and Credit Concentrations

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

The mix of accounts receivable due from patients or third-party payers at September 30 follows:

	2003	2002
Self-pay	**40%**	41%
Medicare	**20**	24
Commercial insurers	**19**	17
Medicaid	**10**	7
Blue Cross Blue Shield of Louisiana	**6**	7
Other third-party payers	**5**	4
	100%	100%

6. Property and Equipment

Property and equipment at September 30, 2003 and 2002 consisted of:

	Beginning Balance	Additions	Retirements	Ending Balance
Land and improvements	**$ 1,380,089**	$ 5,010	$ –	$ 1,385,099
Building and improvements	**14,936,779**	305,330	–	15,242,109
Medical office building	**8,346,920**	–	–	8,346,920
Fixed equipment	**4,382,801**	–	–	4,382,801
Major movable equipment	**17,798,724**	932,265	(176,838)	18,554,151
Construction in progress	**58,238**	204,814	–	263,052
	46,903,551	1,447,419	(176,838)	48,174,132
Less accumulated depreciation and amortization	**(27,870,214)**	(1,506,123)	176,838	(29,199,499)
	$ 19,033,337	$ (58,704)	$ –	$ 18,974,633

Major movable equipment under capital lease obligations totaled $2,082,000 at September 30, 2003 and 2002. Related accumulated amortization was approximately $1,848,000 and $1,693,000 at September 30, 2003 and 2002, respectively.

7. Debt and Capital Lease Obligations

A summary of debt and capital lease obligations, at September 30 follows:

	2003	2002
Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds - Series 2001A, payable in semi-annual installments beginning in May 2008, through May 2016, including interest at 5.25%	**$ 7,905,000**	$ 7,905,000
Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds - Series 2001B, payable in semi-annual installments through May 2008, including interest at 7.25%	**3,025,000**	3,565,000

7. Debt and Capital Lease Obligations (continued)

	2003	2002
Parish of Iberia, State of Louisiana Hospital Revenue Refunding Bonds - Series 2002, payable in semi-annual installments through May 2016, including interest at 5%	**$ 4,945,000**	$ 5,190,000
Parish of Iberia, State of Louisiana Hospital Revenue Bonds – Series 2003, payable in semiannual installments, beginning in November 2003 through May 2018, including interest at 4.35%	**3,000,000**	–
	18,875,000	16,660,000
Capital lease obligations, payable in various monthly installments through September 2008, including interest at rates from 6.5% to 7.9%	**543,909**	633,795
	19,418,909	17,293,795
Less current installments	**1,076,013**	874,803
Less unamortized reacquisition premium	**492,170**	537,000
Debt, less current installments	**$ 17,850,726**	$ 15,881,992

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

During 2003, the Medical Center, through an arrangement with the Parish, issued $3,000,000 of Hospital Revenue Bonds (Series 2003).

7. Debt and Capital Lease Obligations (continued)

The Medical Center's revenue and assets are pledged as collateral for the Parish's bonds. The Medical Center is directly obligated to the Parish for principal and interest payments on the debt as these amounts come due. The indentures also place limits on additional borrowings.

Future maturities of debt and payments on capital lease obligations at September 30, 2003 were as follows:

	Long-Term Debt	Interest on Long-Term Debt	Capital Lease Obligations
2004	$ 980,000	$ 995,000	$ 129,602
2005	1,040,000	935,000	129,603
2006	1,110,000	869,000	129,603
2007	1,185,000	799,000	129,603
2008	1,250,000	724,000	122,290
2009 - 2013	7,365,000	2,569,000	–
2014 - 2018	5,945,000	588,000	–
	18,875,000	7,479,000	640,701
Less unamortized reacquisition premium	492,170	–	–
Less amounts representing interest on capital lease obligations	–	–	96,792
	$18,382,830	$7,479,000	$ 543,909

8. Pension Plan

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

8. Pension Plan (continued)

System members are required to contribute 9.5% of their annual covered salary and the Medical Center is required to contribute at an actuarially determined rate. The current rate is 7.75% of annual covered payroll. The Medical Center's pension cost and contributions to the System were approximately $993,000 in 2003 and $952,000 in 2002. These amounts were equal to the required contributions for each year.

9. Contingencies

The Medical Center maintains insurance coverage for medical malpractice claims up to the statutory limit through the Louisiana Hospital Association Trust Fund and the State of Louisiana Patient Compensation Fund. As of September 30, 2003, there was certain litigation pending against the Medical Center and management believes the insurance coverage described previously adequately insures the Medical Center against these claims.

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

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. Changes in Medicare and Medicaid programs and reductions in funding could have an adverse impact on the Medical Center.

In July 2000, the Medical Center entered into a Corporate Integrity Agreement (CIA) with the Office of the Inspector General (OIG) of the U.S. Department of Health and Human Services to promote compliance by its employees with the statutes, regulations, and written directives of Medicare, Medicaid, and all other federal health care programs. The agreement is a product of a settlement between the Medical Center and the OIG related to errors in Medicare reimbursements received during the period from 1992 through 1995. The three-year agreement contained provisions specifying the components of the compliance program that the Medical Center implemented. On September 30, 2003, the CIA expired and management has been notified by the OIG that the CIA provisions were fulfilled.

10. Operating Leases

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

2004	$ 268,288
2005	191,763
2006	171,186
2007	128,284
2008	33,264
	$ 792,785

The cost of assets held for lease totaled $8,347,000 at September 30, 2003. Related accumulated depreciation was approximately $1,134,000 at September 30, 2003.

The Medical Center leases various equipment and facilities under operating leases expiring at various dates through May 2008. The following is a schedule by year of future minimum lease payments under operating leases that have initial or remaining lease terms in excess of one year.

2004	$ 836,034
2005	766,438
2006	680,712
2007	141,411
2008	6,425
	$ 2,431,020

Rental expense for operating leases was approximately $896,000 in 2003 and $834,000 in 2002.

11. Governmental Regulations

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers in recent years. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Medical Center is in compliance with fraud and abuse as well as other applicable government laws and regulations. While no material regulatory inquiries have been made, 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.

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

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

We have audited the financial statements of Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center) as of and for the year ended September 30, 2003, and have issued our report thereon dated January 9, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Compliance

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

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Medical Center's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to the board of commissioners and management of the Medical Center in a separate report dated January 9, 2004.

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

Ernst + Young LLP

January 9, 2004

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

In planning and performing our audit of the financial statements of Hospital Service District No. 1 of Iberia Parish, State of Louisiana (d/b/a Iberia Medical Center), for the year ended September 30, 2003, we considered its internal control to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving internal control and its operation that we consider to be material weaknesses as defined above.

We would like to provide you with an update on the prior year observations provided to you in our letter dated December 13, 2002.

Significant Estimation Processes

Allowance for Contractual Adjustments

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

Management's Response

Management will document the process used to develop the estimates for contractual adjustments. This process includes the hindsight review of payments and adjustments, which are detailed in source documents such as third-party remittance advices, the summarization of this data in trending schedules, and the comparison of this information to the estimates utilized in completing the contractual adjustments reported in the financial statements.

Current Year Update

Management has developed a process to retrospectively review the prior year contractual allowance estimate and monitor the payment rates by payer throughout the year.

Monitoring Third-Party Settlement Estimates

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

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

Management's Response

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

Current Year Update

Management has improved the process to estimate reserves for uncertainties that exist in the preparation of cost reports by developing a policy that includes reviewing the potential impact of intermediary audit adjustments to prior year filed cost reports. We believe the process can continue to be improved through the inclusion of an analysis of the development of prior years' reserve estimates.

* * * * *

Additionally, during our current year audit, the following matters came to our attention that we believe merit your consideration.

Financial Statement Presentation

Classification of Revenue and Expenses

Currently, the Medical Center reports earnings from joint ventures as a component of nonoperating income in the Medical Center's financial statements. These joint ventures are with medical service provider companies operating in the Medical Center's primary service area. Joint ventures similar to those of the Medical Center are becoming more and more common in the acute care provider industry. Other acute care hospitals consider joint ventures similar to those of the Medical Center as direct extensions of their missions to provide service to the community. Accordingly, the earnings from these ventures are reported as other operating revenue.

We believe management should review the intent of these joint ventures and determine if their purpose extends the Medical Center's primary mission of providing care to the community. If this is the case, we suggest that the earnings be reported as other operating revenue.

Also, the Medical Center provides medical services and supplies to these joint ventures for a fee. The joint ventures reimburse the Medical Center for time worked by Medical Center employees and for supplies provided to the joint ventures out of the Medical Center's inventory. The amounts earned in these arrangements are reported as other operating revenue in the Medical Center's financial statements. However, before reimbursement from the joint ventures, the payroll and supplies are recognized as operating expenses in the Medical Center's financial statements.

We recommend that the Medical Center recognize the reimbursement from the joint ventures as a reduction to payroll expense and supplies expense and not as other operating revenue, as the amounts have previously been recognized as expense in the Medical Center's financial statements.

Management's Response

Management will evaluate the possibility of classifying joint venture earnings as other operating revenue in accordance with this letter's recommendation. As suggested, this classification merits consideration given the relationship of the Medical Center's mission and the medial services provided by these community-based joint ventures.

Management has considered the recommendation to classify the reimbursement from the joint ventures as a reduction to payroll expense and supplies expense and not as other operating revenue. Management is in concurrence and will incorporate this change in its monthly financial reporting.

Significant Estimation Process

Adequacy of the Allowance for Doubtful Accounts

The Medical Center's historical estimate of the allowance for doubtful accounts is primarily based on the age and payer mix of the outstanding accounts receivable. In the current year, management modified the reserving percentages to develop a larger allowance due to hindsight analysis that indicated the prior reserving percentages were generating an insufficient allowance.

We recommend management more frequently update the reserving percentages used to estimate the allowance for doubtful accounts. Further, we suggest management formally reassess the results of the estimation process through periodic updates of hindsight analyses, historical collection results by financial class, write-offs and recoveries by financial class and year of revenue, and other trend analyses. Continued refinement and proper interpretation of these analytics could aid management in identifying billing and collecting process changes and their impacts on the trends in collectibility and estimating the net realizable value of accounts receivable.

Additionally, self-pay accounts as a percentage of total accounts receivable continue to be significant. These accounts by their nature are more difficult to collect. We recommend management continue to review all processes in place to capture, bill, monitor, and collect these accounts and to assess the collectibility of self-pay accounts using similar analytics as described above.

Management's Response

Management recognizes and concurs with the importance of frequently analyzing the reserving percentages used to estimate the allowance for doubtful accounts. It is management's intent to continue to refine hindsight analysis and to monitor trend development in order to increase the timeliness of necessary adjustments to the estimation process.

Self-pay accounts will receive additional emphasis in the revenue cycle and collection process in order to maximize collectibility and to minimize associated write-off expense. This effort will include the patient registration, charging, and collection functions.

* * * * *

This report is intended solely for the information and use of the board of commissioners, management, and the office of the legislative auditor and is not intended to be and should not be used by anyone other than these specified parties.

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

Ernst + Young LLP

January 9, 2004