

West Allis Memorial Hospital, Inc.

Financial Statements as of and for the Years
Ended December 31, 2011 and 2010, and
Independent Auditors' Report

WEST ALLIS MEMORIAL HOSPITAL, INC.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Aurora Health Care, Inc.:

We have audited the accompanying balance sheets of West Allis Memorial Hospital, Inc. (the "Hospital"), an affiliate of Aurora Health Care, Inc. ("Aurora"), as of December 31, 2011 and 2010, and the related statements of operations and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of West Allis Memorial Hospital, Inc. as of December 31, 2011 and 2010, and the results of its operations, changes in its net assets, and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, the financial statements present the financial position, results of operations, and cash flows of the Hospital and are not necessarily indicative of what the financial position, results of operations, and cash flows would have been if the Hospital had been operated as an unaffiliated corporation during the periods presented. Certain expenses represent allocations from Aurora.

As discussed in Note 2 to the financial statements, the Hospital adopted the presentation and disclosure requirements of Accounting Standards Update No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*, and changed its presentation of the provision for bad debts.

Deloitte & Touche LLP

June 29, 2012

WEST ALLIS MEMORIAL HOSPITAL, INC.

BALANCE SHEETS AS OF DECEMBER 31, 2011 AND 2010 (In thousands)

	2011	2010
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 107	\$ 44
Investments	4	-
Accounts receivable — net of allowance for doubtful accounts of \$14,795 and \$16,570 (Note 2)	30,273	27,561
Inventories and other current assets	4,897	4,409
Due from affiliates	<u>214,732</u>	<u>180,574</u>
Total current assets	250,013	212,588
DUE FROM AFFILIATES	79,659	61,963
PROPERTY, PLANT, AND EQUIPMENT — Net	97,657	101,796
OTHER ASSETS	<u>4,373</u>	<u>3,632</u>
TOTAL	<u>\$431,702</u>	<u>\$379,979</u>
 LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Current installments of long-term debt	\$ 1,072	\$ 2,493
Accounts payable	6,955	10,485
Estimated third-party payor settlements	3,935	3,901
Due to affiliates	7,278	7,278
Accrued salaries and benefits	7,011	6,765
Other accrued expenses	<u>1,221</u>	<u>1,311</u>
Total current liabilities	27,472	32,233
LONG-TERM DEBT — Less current installments	26,460	27,527
OTHER LONG-TERM LIABILITIES	<u>1,457</u>	<u>514</u>
Total liabilities	<u>55,389</u>	<u>60,274</u>
NET ASSETS:		
Unrestricted	375,302	318,516
Temporarily restricted	<u>1,011</u>	<u>1,189</u>
Total net assets	<u>376,313</u>	<u>319,705</u>
TOTAL	<u>\$431,702</u>	<u>\$379,979</u>

See notes to financial statements.

WEST ALLIS MEMORIAL HOSPITAL, INC.

STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010 (In thousands)

	2011	2010
REVENUE:		
Patient service revenue (net of contractual allowances and discounts)	\$255,481	\$253,958
Provision for bad debts	<u>(12,631)</u>	<u>(12,225)</u>
Net patient service revenue less provision for bad debts	242,850	241,733
Other revenue	<u>6,039</u>	<u>5,757</u>
Total revenue	<u>248,889</u>	<u>247,490</u>
EXPENSES:		
Salaries	60,792	63,138
Fringe benefits	22,644	22,799
Professional fees	2,084	2,414
Supplies	35,579	31,240
Depreciation and amortization	9,252	9,148
Interest	1,665	1,841
Maintenance and service contracts	1,614	2,075
Building and equipment rental	2,255	2,300
Hospital tax assessment	9,879	9,342
Utilities	3,307	3,369
Purchased services	3,334	3,890
Management services and operational support	28,864	42,035
Other	<u>11,418</u>	<u>12,322</u>
Total expenses	<u>192,687</u>	<u>205,913</u>
OPERATING INCOME	56,202	41,577
NONOPERATING LOSS — Net	<u>(1)</u>	<u>(2)</u>
EXCESS OF REVENUE OVER EXPENSES	56,201	41,575
TRANSFERS FROM (TO) AFFILIATES — Net	433	(29)
CONTRIBUTIONS	-	(30)
OTHER	<u>152</u>	<u>-</u>
INCREASE IN UNRESTRICTED NET ASSETS	<u>56,786</u>	<u>41,516</u>
TEMPORARILY RESTRICTED NET ASSETS — Change in beneficial interest in net assets of foundation	(206)	227
CONTRIBUTIONS	<u>28</u>	<u>-</u>
(DECREASE) INCREASE IN TEMPORARILY RESTRICTED NET ASSETS	<u>(178)</u>	<u>227</u>
Total increase in net assets	56,608	41,743
NET ASSETS:		
Beginning of year	<u>319,705</u>	<u>277,962</u>
End of year	<u>\$376,313</u>	<u>\$319,705</u>

See notes to financial statements.

WEST ALLIS MEMORIAL HOSPITAL, INC.

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010 (In thousands)

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Increase in net assets	\$ 56,608	\$ 41,743
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	9,252	9,148
Provision for bad debts	12,631	12,225
Change in beneficial interest in net assets of foundation	206	(227)
Increase in accounts receivable	(15,343)	(39,786)
Increase in estimated third-party payor settlements	34	2,182
Other — net	<u>(3,874)</u>	<u>281</u>
Net cash provided by operating activities	<u>59,514</u>	<u>25,566</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(5,113)	(6,273)
Transfers and amounts due from affiliates — net	<u>(51,854)</u>	<u>(17,001)</u>
Net cash used in investing activities	<u>(56,967)</u>	<u>(23,274)</u>
CASH USED IN FINANCING ACTIVITIES — Repayment of long-term debt	<u>(2,484)</u>	<u>(2,310)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	63	(18)
CASH AND CASH EQUIVALENTS:		
Beginning of year	<u>44</u>	<u>62</u>
End of year	<u>\$ 107</u>	<u>\$ 44</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION — Cash paid for interest	<u>\$ 1,680</u>	<u>\$ 1,808</u>

See notes to financial statements.

WEST ALLIS MEMORIAL HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

1. DESCRIPTION OF ORGANIZATION

West Allis Memorial Hospital, Inc. (the Hospital) is a Wisconsin nonstock, not-for-profit corporation. The Hospital operates as an acute-care hospital and serves primarily the greater Milwaukee area, providing inpatient, outpatient, and emergency care services.

The Hospital is an affiliate of Aurora Health Care, Inc. (Aurora), a Wisconsin nonstock, not-for-profit corporation, which operates to provide and deliver a variety of health care services and activities in Eastern Wisconsin and the surrounding areas, and to carry on such educational, philanthropic, and medical research activities as may be part of an integrated health care delivery system. The Aurora system comprises 14 acute-care hospital campuses, one psychiatric hospital, a network of 149 physician clinic facilities, home health services, 82 retail pharmacies, and other health care and related services. Aurora Health Care Metro, Inc., is an affiliate of Aurora and is the sole corporate member of the Hospital.

During 2011 and 2010, management and administrative expenses comprised 4.7% and 5.0% of total expenses, respectively. Management and administrative expenses include information technology, finance, purchasing, patient billing, and human resources. The remaining expenses relate to the provision of health care services.

The accompanying financial statements present the financial position, results of operations, and cash flows of the Hospital and are not necessarily indicative of what the financial position, results of operations, and cash flows would have been if the Hospital had been operated as an unaffiliated corporation during the period presented.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses as of the date and period of the financial statements. Actual results could differ from those estimates.

Except as otherwise disclosed, the carrying value of all financial instruments of the Hospital (including cash and cash equivalents, accounts receivable, advances to and amounts due from affiliates, accounts payable, accrued expenses, and estimated third-party settlements) approximates their fair value due to their short-term maturities at December 31, 2011 and 2010. The fair value of the long-term debt is disclosed in Note 4.

Significant accounting policies of the Hospital are as follows:

Cash and Cash Equivalents — Cash and cash equivalents include highly liquid investments purchased with an original maturity or maturity at the date of purchase of three months or less.

Accounts Receivable — The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors is as follows:

- Medicare — Inpatient acute, most hospital outpatient services, and inpatient rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Certain inpatient non-acute and outpatient services, defined capital costs, medical education costs, select drugs, and devices related to Medicare beneficiaries are paid based on cost-reimbursement methodologies. The Hospital is reimbursed for cost-reimbursable items at a tentative rate, with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary.
- Medicaid — Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed primarily based upon prospectively determined rates.
- Other third-party payors — Services rendered to patients insured by other third-party payors are reimbursed based on a discount from customary charges, prospectively determined rates per discharge or negotiated fee schedules.

Accounts receivable are stated at net realizable value. Accounts receivable are reduced by a contractual allowance and by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the Hospital analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate contractual allowance and allowance for doubtful accounts. Management regularly reviews data about these major payor sources in evaluating the sufficiency of the contractual allowance and allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides a contractual allowance, as well as an allowance for doubtful accounts, if necessary. For receivables associated with self-pay patients, the Hospital records a significant provision for bad debt and charity care in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates, if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

The Hospital's allowance for doubtful accounts decreased from 39.9% of gross accounts receivable less contractual allowances at December 31, 2010, to 34.8% of gross accounts receivable less contractual allowances at December 31, 2011. The Hospital's allowance for doubtful accounts decreased \$1,775,000 from \$16,570,000 at December 31, 2010, to \$14,795,000 at December 31, 2011. The decrease in the allowance for doubtful accounts was the result of an increase in bad debt write-offs as compared to the prior year. The decrease in the allowance for doubtful accounts as a percent of gross accounts receivable less contractual allowances was driven by an increase in bad debt write offs during the year ended December 31, 2011. The Hospital did not change its charity care or uninsured discount policies during fiscal year 2011 and 2010. The Hospital does not maintain a material allowance for doubtful accounts from third-party payors and did not have significant write-offs from third-party payors.

At December 31, 2011 and 2010, approximately 15% and 22%, respectively, of the Hospital's net accounts receivable were due from the Medicare and Medicaid programs. At December 31, 2011 and 2010, approximately 43% and 48%, respectively, was due from patients, and 42% and 30%, respectively, was due from managed care and other contracted payors.

Inventories — Medical supplies inventories are stated at the lower of cost (first-in, first-out) or market.

Property, Plant, and Equipment — Property, plant, and equipment acquisitions are recorded at cost. Donated property, plant, and equipment are recorded at fair value at date of donation, which is then treated as cost. Property, plant, and equipment assets are depreciated on the straight-line method over their estimated useful lives, ranging from three to 40 years. Plant and equipment are subject to the lease agreement between the Hospital and the City of West Allis (see Note 7).

The Hospital periodically assesses the impairment of long-lived assets (including property, plant, and equipment) whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. Management considers such factors as current results, trends, and future prospects, in addition to other economic factors, in determining the impairment of an asset. No such impairment adjustments were recorded in 2011 and 2010.

Deferred Financing Costs and Amortization of Bond Discount — Long-term debt issuance costs are deferred and amortized over the term of the debt along with any original issue discount. Long-term debt issuance costs and original issue discounts are amortized using methods that approximate the interest rate method.

Income Taxes — The Hospital is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and has been recognized as tax exempt pursuant to Section 501(a) of the Code.

The Hospital evaluates its uncertain tax positions on an annual basis. A tax benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits. There have been no uncertain tax positions recorded in 2011 or 2010.

Net Assets — Restricted net assets are used to differentiate resources, the use of which is limited by the donor or grantor, from unrestricted net assets that arise as a result of the operations of the Hospital. Temporarily restricted net assets consist of donations restricted to various specific purposes by donors. At December 31, 2011 and 2010, temporarily restricted net assets comprise assets held by an unconsolidated foundation for the benefit of the Hospital (see Note 6).

Patient Service Revenue — Patient service revenue includes amounts from patients, third-party payors, and others for services rendered. The Hospital recognizes patient service revenue associated with services provided to patients who have third-party coverage on the basis of contractual rates for the services provided. In addition, patient service revenue includes estimated retroactive adjustments under reimbursement agreements with third-party payors. 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. Laws and regulations governing government and other payment programs are complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimated third-party payor settlements could change by a material amount. Changes in estimates relating to prior years increased patient service revenue by approximately \$500,000 in 2011 and \$1,250,000 in 2010.

The Hospital has filed formal appeals relating to the settlement of certain prior year Medicare cost reports. The ultimate outcome of such appeals cannot be determined at this time. Any resulting gains will be recognized in the statements of operations and changes in net assets when realized.

At both December 31, 2011 and 2010, approximately 32% of the Hospital's patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), was recognized for services provided to Medicare and Medicaid patients. At December 31, 2011 and 2010, approximately 3% and 13%, respectively, was recognized for services provided to uninsured or self-insured patients, and approximately 65% and 55%, respectively, was recognized for services provided to patients of managed care and other contracted payors. Due to the nature of the Hospital's patient base, the majority of patients who do not have commercial insurance qualify for Medicare or Medicaid programs, resulting in a very limited amount of self-pay revenue.

In February 2009, the Wisconsin legislature enacted senate Bill 62, which assessed a fee or tax on the gross patient revenues of all Wisconsin hospitals. The revenues from this assessment are used to increase payments made to hospitals for services provided to Medicaid and other medically-indigent patients. The Hospital's net patient service revenues reflect this increase in payment for services to Medicaid and other medically-indigent patients, and other expenses reflect the fee assessed by the State. Net patient service revenue during 2011 and 2010 includes \$12,240,000 and \$10,177,000, respectively, related to this program, and expenses include \$9,879,000 and \$9,342,000, respectively, of tax assessment fees.

Provision for Bad Debt — For uninsured patients that do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). On the basis of its historical experience, a significant portion of the Hospital's uninsured will be unwilling or unable to pay for the services provided. In addition, a portion of the Hospital's insured patients will be unwilling or unable to pay the portion of their bill for which they are financially responsible in the period services were provided. The Hospital records a provision for bad debts related to uninsured patients, and related to insured patients for the portion of their bill for which they are financially responsible, in the period services were provided.

Other Revenue/Expense — Other revenue primarily comprises revenues from cafeteria sales, rental of hospital space, certain interest income, and other miscellaneous services. Other expense primarily consists of taxes, insurance, and other administrative costs.

Investment income on temporarily restricted net assets is recorded in the applicable category of restricted net assets, if such income is also donor restricted.

Nonoperating Income (Losses) — Net — Revenues and expenses from delivering health care services and other activities that arise from the Hospital's ongoing major or central operations are reported in operations. Income and losses that arise from transactions that are peripheral or incidental to the Hospital's main activities, such as income and losses attributable to sales of property, plant, and equipment, are included in nonoperating income (loss), net.

Charity Care and Uninsured Care — The Hospital provides care to patients who meet certain criteria under its Helping Hands program without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts determined to qualify under this program, they are not reported as revenue. The cost of charity care, estimated based on the Hospital's specific cost-to-charge ratios, was \$1,772,000 in 2011 and \$1,671,000 in 2010.

Excess of Revenue over Expenses — The statements of operations and changes in net assets includes excess of revenue over expenses. Changes in unrestricted net assets that are excluded from excess of revenue over expenses, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services.

Pension Plan — The Hospital participates in the Aurora Health Care, Inc. Pension Plan (the Aurora Pension Plan). The Aurora Pension Plan is a noncontributory defined benefit pension plan that is sponsored and administered by Aurora. The Aurora Pension Plan covers substantially all employees of Aurora and its participating affiliates. Periodic pension expense and the related liability for the unfunded status of the Aurora Pension Plan are reported in Aurora's financial statements. The Hospital's portion of the pension liability for the unfunded status of the Aurora Pension Plan has not been recorded in the Hospital's financial statements.

Pension expense reported by the Hospital represented a portion of the total periodic pension costs and was allocated to the Hospital based on guidelines established by the plan administrator. The Hospital's expense for the Aurora Pension Plan was \$5,189,000 and \$7,278,000 in 2011 and 2010, respectively, representing 7.6% and 7.9%, respectively, of the total recorded pension expense for the Aurora Pension Plan. At December 31, 2011, the Hospital's portion of the periodic pension cost is included in due to affiliates on the accompanying balance sheet. At December 31, 2011, the projected benefit obligation of the Aurora Pension Plan totaled \$1,300,402,000 and the fair value of the related plan assets totaled \$803,911,000.

Incentive Savings Plan — The Hospital participates in the Aurora Health Care, Inc. Incentive Savings Plan (the Aurora Savings Plan). The Aurora Savings Plan is a defined contribution plan sponsored and administered by Aurora, whereby the Hospital contributes a percentage of participants' qualifying compensation up to certain limits as outlined in the Aurora Savings Plans. The Aurora Savings Plan covers regular full- or part-time employees of Aurora and its participating affiliates. The Hospital's expense for the Aurora Savings Plan was \$1,301,000 in 2011. For 2010, contributions were not made to the Aurora Savings Plan.

Subsequent Events — For the year ended December 31, 2010, the Hospital has evaluated subsequent events for potential recognition and disclosure through June 29, 2012, the date of financial statement issuance.

New Accounting Pronouncements — In August 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-23, *Health Care Entities (Topic 954): Measuring Charity Care for Disclosure*, which requires that cost be used as the measurement basis for charity care disclosure and the disclosure should include the direct and indirect cost of providing charity care. The guidance also requires disclosure of the method used to identify such costs. The Hospital adopted the provisions of the standard effective January 1, 2011, and the provisions were applied retrospectively to all periods presented. Adoption of this guidance had no impact on the Hospital's financial statements, however, resulted in additional disclosures, as presented above.

In August 2010, the FASB issued ASU No. 2010-24, *Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries*, which clarifies that a healthcare entity should not net insurance recoveries against a related claim liability. Additionally, the amount of the claim liability should be determined without consideration of insurance recoveries. The Hospital adopted the provisions of the standard effective December 31, 2011, and the provisions were applied retrospectively to all periods presented. The incremental effect of retrospectively applying the provisions of ASU No. 2010-24 to the balance sheet as of December 31, 2010, was an increase to other noncurrent assets and other noncurrent liabilities of \$314,000.

In May 2011, the FASB issued ASU No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and IFRSs*, which expands existing disclosure requirements for fair value measurements and makes other amendments in order to develop a single, converged fair value framework. This update is effective for the fiscal year ending December 31, 2012, and is not expected to have a material impact on the financial statements.

In July 2011, the FASB issued ASU No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*, which requires certain health care entities to change the presentation of the statements of operations by reclassifying the provision for bad debts associated with patient service revenue from operating expenses to a deduction from patient service revenue (net of contractual allowances and discounts). The Hospital has elected to adopt the provisions of ASU No. 2011-07 effective January 1, 2011. The provisions of the standard were applied retrospectively to all periods presented. The adoption did not have a material effect on the financial statements, however, resulted in a change in the presentation of the provision for bad debts in the statements of operations and changes in net assets as well as additional disclosures, as presented above.

Reclassification — The Hospital expanded the categories of expenses on the statements of operations and changes in net assets to separately identify maintenance and service contracts, building and equipment rental, and utilities from other expenses. The 2010 amounts were reclassified from other expenses to conform to the 2011 presentation.

3. PROPERTY, PLANT, AND EQUIPMENT

The summary of the components of property, plant, and equipment (see Note 7) at December 31, 2011 and 2010, is as follows (in thousands):

	2011	2010
Land and improvements	\$ 2,073	\$ 2,073
Buildings and fixed equipment	193,450	189,854
Movable equipment	47,562	57,481
Construction in progress	<u>894</u>	<u>1,344</u>
Total property, plant, and equipment	243,979	250,752
Accumulated depreciation	<u>(146,322)</u>	<u>(148,956)</u>
Property, plant, and equipment — net	<u>\$ 97,657</u>	<u>\$ 101,796</u>

At December 31, 2011, construction in progress consisted of various improvement projects. There was no capitalized interest recorded in 2011 or 2010.

4. LONG-TERM DEBT

Long-term debt at December 31, 2011 and 2010, is summarized as follows (in thousands):

	2011	2010
Allocated Wisconsin Health and Educational Facilities Authority bonds	\$ 26,031	\$ 26,093
City of West Allis (City) general obligation bonds and promissory notes — net of unamortized discount of \$4 and \$8, respectively (see Note 7)	1,001	1,642
Notes payable	<u>500</u>	<u>2,285</u>
Total long-term debt	27,532	30,020
Less current installments	<u>(1,072)</u>	<u>(2,493)</u>
Long-term debt — less current installments	<u>\$ 26,460</u>	<u>\$ 27,527</u>

Aurora has issued revenue bonds through the Wisconsin Health and Educational Facilities Authority (WHEFA). Such bonds are subject to a Master Trust Indenture (the Aurora Indenture). All outstanding debt under the Aurora Indenture is the general, joint, and several obligations of the members of the Aurora Obligated Group, which comprises various affiliates of the Aurora system. The Hospital is not a member of the Obligated Group; however, it is the intent of Aurora and the Hospital that each system affiliate with allocated WHEFA debt be responsible for its respective share of principal and interest as reflected in its financial statements.

Under terms of its borrowing agreements with Aurora, the Hospital's allocated WHEFA debt is due annually in varying amounts commencing in 2012 and extending through 2039, and bears interest at a rate of 6%.

The City general obligation bonds and promissory notes represent obligations for which repayment has been assigned to the Hospital for the financing of Hospital facilities and equipment. The bonds and notes are due in varying installments through 2013. Fixed interest rates on the two series of general obligation bonds were 3.625% and 4.5% at December 31, 2011, and 3.5% and 4.5% at December 31, 2010 (see Note 7). During 2010, in conjunction with a refinancing of the City general obligation bonds initiated by the City, the City and the Hospital entered into a Loan Agreement to restructure a portion of the Hospital's obligations with respect to the City general obligation bonds. Pursuant to the Loan Agreement, the City loaned \$2,285,000 at a rate of 4.0% to the Hospital. The Loan Agreement calls for principal payments in 2011 and 2012 such that the obligation will be repaid in full upon maturity of the Loan Agreement in 2012. These obligations are included with the Hospital's long-term debt as they relate to a lease agreement between the City and the Hospital (see Note 7).

Scheduled maturities on long-term debt (excluding amortization of unamortized bond discounts of \$4) at December 31, 2011, are as follows (in thousands):

2012	\$ 1,072
2013	629
2014	127
2015	131
2016	235
Thereafter	<u>25,342</u>
Total	<u>\$27,536</u>

The estimated fair value of long-term debt, based on discounted cash flows at estimated current borrowing rates, approximated \$27,652,000 and \$29,856,000 at December 31, 2011 and 2010, respectively.

5. SELF-FUNDED HEALTH, DENTAL, AND OTHER BENEFITS

Substantially all of the Hospital's employees and their eligible dependents participate in a self-funded health and dental insurance plan sponsored and administered by Aurora. The Hospital's allocated costs under the plan, which totaled \$9,097,000 and \$8,801,000 in 2011 and 2010, respectively, are based upon actual claims paid, administration fees, and provisions for unpaid and unreported claims at year-end. Such costs are included with fringe benefits in the accompanying financial statements.

The Hospital also provides salary continuation payments to current and inactive employees who are eligible to receive long-term disability and workers' compensation under self-funded arrangements. The Hospital costs under the Plan, which totaled \$1,235,000 and \$1,263,000 in 2011 and 2010, respectively, were based on actual claims paid. Such costs are included with fringe benefits in the accompanying financial statements. Aurora measures the cost of its unfunded obligations under such programs based upon actuarial calculations, however, does not allocate any of the unfunded liabilities to the Hospital.

6. ADVANCES TO AND TRANSACTIONS WITH AFFILIATES

Aurora has a centralized cash depository and disbursement arrangement as a means of improving investment returns and facilitating the settlement of intercompany balances. Beginning January 1, 2010, affiliates no longer earn interest on advances to Aurora or incur expense on borrowings from Aurora; rather, the interest on advances to Aurora or expenses on borrowings from Aurora are recorded as an adjustment to the expenses for management services and operational support provided by Aurora to the Hospital. At December 31, 2011 and 2010, the Hospital's portion of Aurora's cash concentration accounts totaled \$294,391,000 and \$242,537,000, respectively. Such amounts are classified as current and noncurrent due from affiliates in the accompanying financial statements in the same proportion as Aurora's consolidated current and noncurrent cash and investments. Amounts advanced by the Hospital to Aurora have been primarily used to fund advances to or investments in the various operating members of the Aurora system. Management of the Hospital believes Aurora and its affiliates have the ability and intent to repay these advances. Should some or all of these advances not be repaid by Aurora, the Hospital's net assets would be reduced and its debt to equity ratio would be increased. The fair value of the Hospital's advances to affiliates is estimated to approximate their carrying value.

Transactions with affiliates are recorded at amounts which approximate cost and are allocated based upon volume, usage, and budgeted financial operations. Aurora provides certain administrative and support services to the Hospital. Additionally, the Hospital provides operational support to certain

affiliated clinics closely associated with the Hospital. Expenses for management services totaled \$28,864,000 and \$42,035,000 (including operational support of \$0 and \$6,985,000) in 2011 and 2010, respectively. The decrease in management expenses from 2010 to 2011 represents the elimination of operational support and a reduction in expenses allocated from Aurora.

The Hospital, along with certain other Aurora affiliates, participates in the Aurora Consolidated Laboratories Co-Tenancy (the Co-Tenancy). The primary purpose of the Co-Tenancy is to operate an integrated, full-service diagnostic laboratory. Other expenses include \$6,793,000 and \$7,082,000 in 2011 and 2010, respectively, related to laboratory services provided by the Co-Tenancy.

Permanent transfers of assets and liabilities to and from affiliates for other than goods and services are reported as changes in unrestricted net assets. Net transfers of assets and liabilities from affiliates amounted to an increase in unrestricted net assets of \$433,000 in 2011 and a decrease in unrestricted net assets of \$29,000 in 2010.

The Aurora Foundation, Inc. (the Foundation) holds unrestricted assets of \$983,000 and \$1,189,000 at December 31, 2011 and 2010, respectively, that are expected to be used for the benefit and support of the Hospital and its activities, and are included in other assets in the accompanying balance sheet. Amounts received from the Foundation for educational and operating purposes were not significant in 2011 and 2010.

7. COMMITMENTS AND CONTINGENCIES

Lease Agreement — The Hospital has a noncancelable lease agreement with the City for the right to operate the Hospital. The City has title to all assets and any subsequent additions, with the exception of certain equipment with a net book value of \$2,148,000 used by the Hospital for laboratory services. The Hospital has exclusive right to the use of the assets and the obligation to maintain and replace them over the term of the lease agreement. The historical cost of the leased facilities is included with the Hospital's property, plant, and equipment (see Note 3) and the general obligation bonds related to the leased facilities are included with the Hospital's long-term debt (see Note 4). The agreement provides for annual payments of \$350,000 in lieu of annual lease payments. The lease expires in 2063.

The Hospital also has various noncancelable operating lease agreements for medical equipment, which have remaining fixed terms ranging from one to five years at December 31, 2011. Future minimum lease payments related to these operating leases that have initial or remaining lease terms in excess of one year at December 31, 2011, are as follows: \$1,860,000 in 2012; \$1,867,000 in 2013; \$1,517,000 in 2014; \$848,000 in 2015; \$739,000 in 2016; and \$4,155,000 thereafter.

Litigation and Potential Risks — The Hospital is subject to various regulatory investigations, legal proceedings, and claims, which are incidental to its normal business activities.

The Hospital believes it has made adequate provision for potential exposures relating to its legal matters. In the opinion of the management, the amount of ultimate liability with respect to these actions will not materially affect the financial position or results of operations of the Hospital.

Insurance Coverage — The Hospital is a qualified healthcare provider as defined by Wisconsin state statute and has professional liability insurance with limits of \$1,000,000 per incident and \$3,000,000 in aggregate for claims incurred during a policy year, regardless of when the claim is reported (occurrence coverage). Losses in excess of these amounts are fully covered through mandatory participation in the State of Wisconsin Injured Patients and Families Compensation Fund.

Aurora Liability Assurance, Ltd. (ALA), a wholly owned subsidiary of Aurora, assumes the primary medical professional liability and general liability risks of Aurora and its affiliates, including the Hospital. Insurance companies have issued policies covering these liabilities and ceded the risks back to ALA through reinsurance agreements. The Hospital is allocated premium expense based on loss experience and estimated total exposure.

The Hospital is commercially insured for workers' compensation stop-loss; auto, property, boiler, and machinery; directors' and officers' liability; and other customary business liabilities. There are no assurances that the Hospital will be able to renew existing policies or procure coverage on similar terms in the future.

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