



# City of West Allis

## Matter Summary

7525 W. Greenfield Ave.  
West Allis, WI 53214

File Number	Title	Status
2004-0519	Report	In Committee
West Allis Memorial Hospital, Inc.'s financial statements for December 31, 2003 and 2002.		
Introduced: 9/7/2004		Controlling Body: Administration & Finance Committee

### COMMITTEE RECOMMENDATION

*Place on file*

ACTION DATE:	MOVER	SECONDER		AYE	NO	PRESENT	EXCUSED
<u>SEP 07 2004</u>	<input checked="" type="checkbox"/>		Barczak	<input checked="" type="checkbox"/>			
			Czaplewski	<input checked="" type="checkbox"/>			
			Dobrowski				
			Kopplin				
			Lajsic	<input checked="" type="checkbox"/>			
			Narlock				
		<input checked="" type="checkbox"/>	Reinke	<input checked="" type="checkbox"/>			
			Sengstock				
			Vitale				
			Weigel	<input checked="" type="checkbox"/>			
			TOTAL	<u>5</u>	<u>0</u>		

### SIGNATURE OF COMMITTEE MEMBER

Chair

Vice-Chair

Member

### COMMON COUNCIL ACTION **PLACE ON FILE**

ACTION DATE:	MOVER	SECONDER		AYE	NO	PRESENT	EXCUSED
<u>SEP 07 2004</u>	<input checked="" type="checkbox"/>		Barczak	<input checked="" type="checkbox"/>			
			Czaplewski	<input checked="" type="checkbox"/>			
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			Lajsic	<input checked="" type="checkbox"/>			
			Narlock	<input checked="" type="checkbox"/>			
		<input checked="" type="checkbox"/>	Reinke	<input checked="" type="checkbox"/>			
			Sengstock	<input checked="" type="checkbox"/>			
			Vitale	<input checked="" type="checkbox"/>			
			Weigel	<input checked="" type="checkbox"/>			
			TOTAL	<u>10</u>	<u>0</u>		



**WEST ALLIS MEMORIAL HOSPITAL, INC.**

Financial Statements

December 31, 2003 and 2002

(With Independent Auditors' Report Thereon)

# **WEST ALLIS MEMORIAL HOSPITAL, INC.**

## **Table of Contents**

	<b>Page</b>
Independent Auditors' Report	1
Balance Sheets, December 31, 2003 and 2002	2
Statements of Operations and Changes in Net Assets, Years ended December 31, 2003 and 2002	3
Statements of Cash Flows, Years ended December 31, 2003 and 2002	5
Notes to Financial Statements	6



KPMG LLP  
777 East Wisconsin Avenue  
Milwaukee, WI 53202

### Independent Auditors' Report

Board of Directors  
West Allis Memorial Hospital, Inc.:

We have audited the accompanying balance sheets of West Allis Memorial Hospital, Inc. (the Hospital), as of December 31, 2003 and 2002, 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of December 31, 2003 and 2002, and the results of its operations and changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

**KPMG LLP**

February 13, 2004



KPMG LLP, a U.S. limited liability partnership, is the U.S. member firm of KPMG International, a Swiss cooperative.

**WEST ALLIS MEMORIAL HOSPITAL, INC.**

**Balance Sheets**

**December 31, 2003 and 2002**

**(In thousands)**

<b>Assets</b>	<b>2003</b>	<b>2002</b>
Current assets:		
Cash and cash equivalents	\$ 98	237
Inventories and other current assets	851	847
Advances to and amounts due from affiliates	53,902	35,185
Total current assets	54,851	36,269
Assets whose use is limited	46	3,086
Advances to affiliate	9,341	4,016
Property, plant, and equipment, net	128,915	134,296
Other assets, including interest in net assets of unconsolidated foundation	2,308	2,166
Total assets	\$ 195,461	179,833
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Current installments of long-term debt	\$ 2,555	2,380
Accounts payable	5,778	4,936
Estimated third-party payor settlements	4,752	4,225
Accrued expenses	5,116	4,658
Total current liabilities	18,201	16,199
Long-term debt, less current installments	43,990	46,498
Total liabilities	62,191	62,697
Net assets:		
Unrestricted	132,713	116,717
Temporarily restricted	557	419
Total net assets	133,270	117,136
Total liabilities and net assets	\$ 195,461	179,833

See accompanying notes to financial statements.

**WEST ALLIS MEMORIAL HOSPITAL, INC.**  
**Statements of Operations and Changes in Net Assets**  
**Years ended December 31, 2003 and 2002**  
(In thousands)

	<u>2003</u>	<u>2002</u>
Net patient service revenue	\$ 168,737	144,785
Other revenue	<u>5,715</u>	<u>5,631</u>
Total revenues	<u>174,452</u>	<u>150,416</u>
Expenses:		
Salaries	45,808	42,441
Fringe benefits	12,841	10,176
Professional fees	3,041	2,769
Supplies	21,655	20,578
Depreciation	9,074	7,838
Interest	3,528	2,180
Provision for bad debts	4,640	4,374
Management services purchased	39,894	29,444
Other	<u>17,977</u>	<u>15,035</u>
Total expenses	<u>158,458</u>	<u>134,835</u>
Operating income	15,994	15,581
Nonoperating loss, net	<u>(2)</u>	<u>(64)</u>
Revenues in excess of expenses	<u>\$ 15,992</u>	<u>15,517</u>

**WEST ALLIS MEMORIAL HOSPITAL, INC.**  
**Statements of Operations and Changes in Net Assets**  
**Years ended December 31, 2003 and 2002**  
(In thousands)

	<u>2003</u>	<u>2002</u>
Unrestricted net assets:		
Revenues in excess of expenses	\$ 15,992	15,517
Net transfers of assets and liabilities to affiliates	<u>4</u>	<u>(601)</u>
Change in unrestricted net assets	15,996	14,916
Unrestricted net assets at beginning of year	<u>116,717</u>	<u>101,801</u>
Unrestricted net assets at end of year	<u>132,713</u>	<u>116,717</u>
Temporarily restricted net assets:		
Change in interest in unconsolidated foundation	138	194
Temporarily restricted net assets at beginning of year	<u>419</u>	<u>225</u>
Temporarily restricted net assets at end of year	<u>557</u>	<u>419</u>
Change in net assets	16,134	15,110
Net assets at beginning of year	<u>117,136</u>	<u>102,026</u>
Net assets at end of year	<u>\$ 133,270</u>	<u>117,136</u>

See accompanying notes to financial statements.

# WEST ALLIS MEMORIAL HOSPITAL, INC.

## Statements of Cash Flows

Years ended December 31, 2003 and 2002

(In thousands)

	<u>2003</u>	<u>2002</u>
Cash flows from operating activities:		
Change in net assets	\$ 16,134	15,110
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Interest income on advances to affiliates	(1,656)	(1,154)
Depreciation	9,074	7,838
Provision for bad debts	4,640	4,374
Net transfers of assets and liabilities to affiliates	(4)	601
Change in interest in unconsolidated foundation	(138)	(194)
Increase in accounts receivable	(7,932)	(6,334)
Increase (decrease) in estimated third-party payor settlements	527	(252)
Other, net	1,573	(4,703)
Net cash provided by operating activities	<u>22,218</u>	<u>15,286</u>
Cash flows from investing activities:		
Capital expenditures	(3,693)	(18,862)
Decrease (increase) in assets whose use is limited, net	3,040	(54)
Advances and transfers (to) from affiliates, net	<u>(19,324)</u>	<u>6,179</u>
Net cash used in investing activities	<u>(19,977)</u>	<u>(12,737)</u>
Cash flows from financing activities:		
Repayments of long-term debt	<u>(2,380)</u>	<u>(2,316)</u>
Net cash used in financing activities	<u>(2,380)</u>	<u>(2,316)</u>
Net (decrease) increase in cash and cash equivalents	(139)	233
Cash and cash equivalents:		
Beginning of year	<u>237</u>	<u>4</u>
End of year	<u>\$ 98</u>	<u>237</u>

See accompanying notes to financial statements.



## WEST ALLIS MEMORIAL HOSPITAL, INC.

### Notes to Financial Statements

December 31, 2003 and 2002

#### (1) Description of Organization and Summary of Significant Accounting Policies

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

Aurora Health Care, Inc. (Aurora) is 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 13 acute-care hospital campuses, one psychiatric hospital, a residential care retirement community, 123 townhouses for independent senior living, a network of 94 physician clinic facilities, home health services, 138 retail pharmacies, two skilled nursing facilities, and other health care entities. Aurora is the sole corporate member of the Hospital.

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 and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Except as otherwise disclosed, the carrying value of all financial instruments of the Hospital approximates their fair value.

Management and administrative expenses comprised 19.0% and 16.7% of total expenses during 2003 and 2002, respectively. The remaining expenses were primarily related to the provision of health care related services.

Significant accounting policies of the Hospital are as follows:

##### *(a) Net Asset Accounting*

Unrestricted net assets arise as a result of the operations of the Hospital. Restricted net assets, which consist of temporarily and permanently restricted amounts, are used to differentiate resources whose use is limited by donors or grantors. Temporarily restricted net assets are used to account for assets whose use has been limited by donors to later periods of time or to specific purposes. Permanently restricted net assets are used to account for the principal amount of gifts received with donor stipulations that the principal remain intact in perpetuity and that only the income from investment of the principal be expended.

At December 31, 2003, temporarily restricted net assets comprise assets held by an unconsolidated foundation for the benefit of the Hospital. The Hospital has no permanently restricted net assets.

## WEST ALLIS MEMORIAL HOSPITAL, INC.

### Notes to Financial Statements

December 31, 2003 and 2002

#### **(b) Revenues and Accounts Receivable**

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. 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.

A summary of the payment arrangements with major third-party payors follows:

- *Medicare* – Inpatient acute care, skilled nursing care, certain hospital outpatient services, and beginning January 1, 2002, 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 nonacute services, defined capital costs, medical education costs, and certain drugs, biologicals, and outpatient services 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. Medicaid payment methodologies and rates are subject to change based on the amount of funding available to the State of Wisconsin Medicaid Program.
- *Other third-party payors* – Services rendered to patients insured by other third-party payors are primarily reimbursed based on a discount from customary charges. Other payment arrangements include prospectively determined rates per discharge, reimbursed costs, per diems, and to a lesser extent, capitated payments.

In December 2000, the Hospital entered into an agreement to sell all of its receivables to Aurora, in connection with a system-wide, revolving period securitization transaction (note 8).

#### **(c) Charity Care**

The Hospital 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 Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

#### **(d) Investments and Investment Income**

Investments in equity securities with readily determinable fair market values and all investments in debt securities are measured at fair market value in the balance sheets. Investment income or loss (including realized gains and losses, other than temporary declines in fair value, interest income, and dividends) is included in revenues in excess of expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from revenues in excess of expenses unless such investments are classified as trading securities. The Hospital considers all of its investments to be other than trading securities.

# **WEST ALLIS MEMORIAL HOSPITAL, INC.**

## **Notes to Financial Statements**

**December 31, 2003 and 2002**

Investment income, including investment income on advances to affiliates (see note 8), is generally reported as other revenue. Investment income reported as other revenue totaled \$1,691,000 and \$1,231,000 in 2003 and 2002, respectively. Investment income on temporarily restricted net assets and permanently restricted net assets is recorded in the applicable category of restricted net assets, if such income is also donor restricted. Investment income comprises primarily interest income.

**(e) *Inventories***

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

**(f) *Property, Plant, and Equipment***

Property, plant, and equipment acquisitions are recorded at cost. Donated property, plant, and equipment is recorded at fair market value at date of donation, which then is treated as cost. The assets are depreciated on the straight-line method over their estimated useful lives. Plant and equipment subject to the lease agreement between the Hospital and the City of West Allis or capitalized under capital leases are amortized on the straight-line method over the shorter of the related lease term or the estimated useful life of the asset. Amortization of leased plant and equipment is included in the financial statements with depreciation expense.

The Hospital periodically assesses the impairment of long-lived assets (including property, plant, and equipment, and intangibles) 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.

**(g) *Capitalized Interest***

Interest expense incurred during the period of construction is capitalized as a component of the cost of the asset. In situations involving the acquisition of qualifying assets financed with the proceeds of tax-exempt borrowings that are externally restricted to finance the specified assets or to service the related debt, interest earned on the unexpended proceeds of such borrowings is offset against the capitalized interest cost. In such instances, interest cost, net of interest earned, is capitalized from the date of borrowing until the assets are ready for their intended use. In all other instances, the amount capitalized is determined by applying an interest rate to the average amount of accumulated expenditures for the assets during the period until the assets are ready for their intended use.

**(h) *Pension Plan***

The Hospital participates in the Aurora Health Care, Inc. Pension Plan (the Pension Plan). The Pension Plan is a noncontributory defined benefit pension plan which is sponsored and administered by Aurora. The Pension Plan covers substantially all employees of Aurora and its participating affiliates. Periodic pension expense and the related liability for the Pension Plan are reported in Aurora's financial statements. Pension expense reported by the Hospital represents a portion of the total periodic pension costs and is allocated to the Hospital based on guidelines established by the

**WEST ALLIS MEMORIAL HOSPITAL, INC.**

Notes to Financial Statements

December 31, 2003 and 2002

plan administrator. During 2003 and 2002, the Hospital's expense for the Pension Plan was \$1,998,000 and \$1,417,000, respectively.

**(i) Incentive Savings Plan**

The Hospital participates in the Aurora Health Care, Inc. Incentive Savings Plan (the Savings Plan). The Savings Plan is a contributory defined contribution plan which is sponsored and administered by Aurora. The Savings Plan covers regular full or part-time employees of Aurora and its participating affiliates. Employee contributions of up to 4% of compensation are matched 50% by the Hospital. During 2003 and 2002, the Hospital's expense for the Savings Plan was \$543,000 and \$486,000, respectively.

**(j) Deferred Financing Costs and Bond Discount**

Long-term debt discount and issuance costs are deferred and amortized over the term of the debt using various methods, which approximate the interest yield method.

**(k) Cash and Cash Equivalents**

Cash and cash equivalents include highly liquid investments, if any, purchased with an original maturity of three months or less.

**(l) 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.

**(m) New Accounting Guidance**

Effective January 1, 2002, the Hospital adopted Financial Accounting Standards Board (FASB) statements titled *Business Combinations*, (Statement of Financial Accounting Standards (SFAS) No. 141) and *Goodwill and Other Intangible Assets* (SFAS No. 142), applicable to for-profit entities. SFAS No. 141 requires that the purchase method of accounting be used for all business combinations. SFAS No. 141 specifies criteria that intangible assets acquired in a business combination must meet to be recognized and reported separately from goodwill. SFAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead, tested for impairment at least annually. SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment.

In accordance with *Accounting for the Impairment or Disposal of Long-lived Assets* (SFAS No. 144), if the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount exceeds the fair value of the asset. SFAS No. 144 requires companies to separately report discontinued operations and extends that reporting to a component of an entity that either has been disposed of (by sale, abandonment, or in a distribution to owners) or is classified as held-for-sale. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell.

# WEST ALLIS MEMORIAL HOSPITAL, INC.

## Notes to Financial Statements

December 31, 2003 and 2002

In April 2002, the FASB issued a statement titled *Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections*, (SFAS No. 145). SFAS No. 145 amends existing guidance on reporting gains and losses on the extinguishment of debt to prohibit the classification of the gain or loss as extraordinary, as the use of such extinguishments have become part of the risk management strategy of many companies. It also amends existing guidance to require sale-leaseback accounting for certain lease modifications that have economic effects similar to sale-leaseback transactions.

In June 2002, the FASB issued a statement titled *Accounting for Costs Associated with Exit or Disposal Activities*, (SFAS No. 146). The provisions of SFAS No. 146 are effective for exit or disposal activities that are initiated after December 31, 2002.

In June 2001, the FASB issued a statement titled *Accounting for Asset Retirement Obligations* (SFAS No 143). SFAS No. 143 requires the Hospital to record the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that result from the acquisition, construction, development, and/or normal use of the assets. The Hospital also would record a corresponding asset that is depreciated over the life of the asset. Subsequent to the initial measurement of the asset retirement obligation, the obligation would be adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The Hospital was required to adopt SFAS No. 143 on January 1, 2003.

The adoption of the above noted accounting pronouncements did not have a material effect on the Hospital's financial position or results of operations.

### (n) *Reclassifications*

Certain items in the 2002 financial statements have been reclassified to conform with classifications used in 2003.

### (2) **Assets Whose Use Is Limited**

The following is a summary of assets whose use is limited or restricted at December 31, 2003 and 2002. Investments and assets whose use is limited or restricted are stated at fair market value.

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Certificate of deposit	\$ 46	46
State of Wisconsin Investment Board – Local Government Investment Pool	<u>—</u>	<u>3,040</u>
Total assets whose use is limited	<u>\$ 46</u>	<u>3,086</u>

Included in assets whose use is limited at December 31, 2002 is \$3,040,000 of funds held by trustees under bond indentures. The investments in the pooled investment fund on deposit with the State of Wisconsin comprised primarily of U. S. Government securities, certificates of deposit, and commercial paper. The outstanding debt obligation that required a compensatory balance in the form of an investment pool was

# WEST ALLIS MEMORIAL HOSPITAL, INC.

## Notes to Financial Statements

December 31, 2003 and 2002

retired in 2003. The investment pool was liquidated and made available to the Company upon the debt retirement.

Also included in assets whose use is limited at December 31, 2003 and 2002, are funds valued at \$46,000 designated for continuing education for the board of directors.

Assets whose use is limited are classified in the balance sheet as current assets to the extent they are expected to be used to discharge current liabilities.

### (3) Property, Plant, and Equipment

A summary of the components of property, plant, and equipment (see note 9(c)) at December 31, 2003 and 2002 follows:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Land and improvements	\$ 1,710	1,646
Buildings and fixed equipment	171,627	168,772
Movable equipment	42,164	40,632
Construction in progress	2,692	3,526
	<u>218,193</u>	<u>214,576</u>
Less accumulated depreciation	<u>(89,278)</u>	<u>(80,280)</u>
Property, plant, and equipment, net	<u>\$ 128,915</u>	<u>134,296</u>

At December 31, 2003 and 2002, construction in progress consisted of various improvement projects.

Capitalized interest expense totaled \$487,000 in 2002. There was no capitalized interest recorded in 2003.

### (4) Long-term Debt and Lease Commitments

Long-term debt at December 31, 2003 and 2002 is summarized as follows:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Wisconsin Health and Educational Facilities Authority bonds, net of unamortized discount	\$ 26,093	26,093
City general obligation bonds and promissory notes, net of unamortized discount (note 9(c))	20,452	22,785
	<u>46,545</u>	<u>48,878</u>
Less current installments	<u>(2,555)</u>	<u>(2,380)</u>
Long-term debt, less current installments	<u>\$ 43,990</u>	<u>46,498</u>

**WEST ALLIS MEMORIAL HOSPITAL, INC.**

**Notes to Financial Statements**

**December 31, 2003 and 2002**

In 1999, Aurora issued \$250,000,000 (par value) Series 1999 bonds through the Wisconsin Health and Educational Facilities Authority (WHEFA). All outstanding debt under Aurora's Master Trust Indenture is the general, unsecured, joint, and several obligation of the members of an Obligated Group comprising 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 will be responsible for its respective share of principal and interest as reflected in its financial statements.

WHEFA bonds consist of \$20,874,000 of fixed rate bonds and \$5,219,000 of variable rate demand bonds and are due annually in various amounts commencing in 2012 and extending through 2029. Interest rates on the fixed rate bonds range from 5.59% to 5.61%, and the effective interest rate on the variable rate demand bonds was 1.05% and 1.42% in 2003 and 2002, respectively. Certain fixed rate WHEFA bonds are collateralized by bond insurance. Other fixed rate WHEFA bonds are unsecured and rated annually by various nationally recognized securities rating agencies. The variable rate WHEFA bonds are collateralized by an irrevocable standby letter-of-credit issued by a commercial bank, which expires in June 2004. At December 31, 2003, no bonds have been called and no draws have been made under the letter-of-credit.

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. The unamortized discount at December 31, 2003 and 2002 was \$113,000 and \$130,000, respectively. Interest rates are fixed and ranged from 1.10% to 4.50% at December 31, 2003 (see note 9(c)).

Certain borrowing agreements require deposits to or the establishment and maintenance of sinking or other special funds under the control of trustees (see note 2). Additionally, certain borrowing agreements contain various covenants regarding maintenance of existence, creation of additional liens, and maintenance of certain financial ratios. To the extent such funds or covenants are required under current WHEFA borrowing agreements, these are being maintained and monitored by Aurora. To the extent such funds or covenants are required under current City borrowing agreements, they are being maintained and monitored by the Hospital.

# WEST ALLIS MEMORIAL HOSPITAL, INC.

## Notes to Financial Statements

December 31, 2003 and 2002

Scheduled maturities on all long-term debt (excluding amortization of bond discounts of \$113,000) at December 31, 2003 are as follows (in thousands):

	Long-term debt
2004	\$ 2,555
2005	2,620
2006	2,745
2007	2,050
2008	2,125
Thereafter	34,563
	<u>\$ 46,658</u>

Total rent expense on operating leases for real property and equipment approximated \$2,688,000 and \$1,827,000 in 2003 and 2002, respectively.

The estimated fair market value of long-term debt, based on discounted cash flows at estimated current borrowing rates, approximated \$47,714,000 and \$48,824,000 at December 31, 2003 and 2002, respectively.

Cash payments for interest, net of amounts capitalized (see note 4), totaled \$3,533,000 and \$2,150,000 in 2003 and 2002, respectively.

### (5) Revenue

Revenue in excess of expenses for 2002 includes certain amounts which relate to differences between original estimates and subsequent revisions of certain accruals (including final settlements with third-party payors). Adjustments for 2002 include a net increase in net patient service revenues of approximately \$638,000 related to the final settlement of certain cost reports and revisions of various other years' third-party payor settlement estimates and other accruals. There were no significant adjustments to revenue in excess of expenses for 2003.

### (6) Charity Care

The Hospital 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. Charges relating to charity care provided were \$2,623,000 and \$3,016,000 in 2003 and 2002, respectively.

### (7) Health and Dental Insurance

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 \$4,248,000 and \$3,314,000 in 2003 and 2002, 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.



## WEST ALLIS MEMORIAL HOSPITAL, INC.

### Notes to Financial Statements

December 31, 2003 and 2002

#### (8) Advances to and Transactions with Affiliates

In December 2000, Aurora entered into a series of agreements under which it sold and will continue to sell certain eligible patient accounts receivable to a qualifying special purpose entity, in a revolving period securitization transaction expected to span a long-term period. In connection with this system-wide securitization, the Hospital became party to an arrangement whereby it sells, without recourse and on an ongoing basis, its net patient accounts receivable to Aurora. As consideration for such sales, the Hospital receives an intercompany credit equal to the aggregate net book value of the receivables sold, which totaled \$19,015,000 and \$15,723,000 at December 31, 2003 and 2002, respectively. The intercompany credit received as consideration for such sales is included in current advances to affiliate in the accompanying financial statements.

Aurora has a centralized cash depository and disbursement arrangement, as a means of improving investment returns and facilitating the settlement of intercompany balances. System foundation deposits are segregated to ensure that donor related funds are expended in accordance with donor restrictions. Transactions of system providers, including cash receipts, vendor and payroll payments, corporate service and operational support charges, and working capital advances are recorded in a concentration account held by Aurora. Aurora maintains sub-accounts representing each provider's net interest in such concentration account. Providers and other system affiliates which, on a net basis, have advanced funds to the system earn interest on such advances. Similarly, providers and other system affiliates which, on a net basis, have borrowed funds from the system incur interest expense on those borrowings. Interest rates credited or charged approximate those earned by Aurora on its centralized depository accounts. At December 31, 2003 and 2002, the Hospital's interest in Aurora's cash concentration accounts totaled \$44,463,000 and \$23,478,000, respectively, classified as advances to affiliates. Such interest is classified as current to the extent of the Hospital's pro-rata share of cash and cash equivalents and current investments held by Aurora at December 31, 2003 and 2002.

Interest credited to the Hospital on its interest in Aurora's cash concentration accounts totaled \$1,656,000 in 2003 and \$1,154,000 in 2002 and is included in other revenue.

Amounts advanced to Aurora have been primarily used to fund advances to or investments in operating members of the Aurora system. Management of Aurora asserts it has 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 and is based upon an interest rate approximating that of other types of unsecured short-term debt instruments of relatively similar risk.

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 system clinics closely associated with the Hospital. Management services expenses totaled \$39,894,000 and \$29,444,000 in 2003 and 2002, respectively, for such activities. At December 31, 2003 and 2002, the Hospital owed \$235,000 and \$351,000, respectively, to affiliated organizations for reimbursable expenditures incurred on behalf of the Hospital. Such amounts due to affiliates are included with accrued expenses in the accompanying financial statements.

## **WEST ALLIS MEMORIAL HOSPITAL, INC.**

### **Notes to Financial Statements**

**December 31, 2003 and 2002**

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 included \$6,210,000 and \$4,900,000 in 2003 and 2002, respectively, related to laboratory services provided by the Co-Tenancy to the Hospital.

Permanent transfers of assets and liabilities to and from affiliates for other than goods and services are reported as changes in unrestricted net assets, consistent with industry practice. In 2003, transfers from affiliates for medical equipment amounted to \$4,000, and in 2002, transfers of medical equipment amounting to \$601,000 were made to affiliated organizations.

At December 31, 2003 and 2002, the Aurora Foundation, Inc. (the Foundation) holds unrestricted assets of \$557,000 and \$419,000, respectively, which 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 sheets. Amounts received from the Foundation for educational and operating purposes were not significant in 2003 or 2002.

#### **(9) Commitments and Contingencies**

##### **(a) Litigation**

The Hospital is subject to various legal proceedings and claims which are incidental to its normal business activities. In the opinion of management of the Hospital, the amount of ultimate liability with respect to these actions will not materially affect the operations or net assets of the Hospital.

##### **(b) Insurance Coverage**

The Hospital is commercially insured for excess malpractice and general liability; workers' compensation; property, boiler, and machinery; directors and officers liability; and certain employee health insurance claims. There are no assurances that the Hospital will be able to renew existing policies or procure coverage on similar terms in the future as a result of current environmental factors affecting the industry.

##### **(c) Lease Agreement**

Under the terms of a noncancelable lease agreement between the Hospital and the City of West Allis (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 \$1,611,000 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 debt obligations on the leased facilities are included with the Hospital's long-term debt (see note 4). The lease agreement does not provide for lease payments; however, a determination is made annually as to the amount of Hospital funds which can, consistent with sound financial management, be turned over to the City. The Hospital paid \$100,000 to the City in both 2003 and 2002. The lease agreement expires in 2038.

**WEST ALLIS MEMORIAL HOSPITAL, INC.**

**Notes to Financial Statements**

**December 31, 2003 and 2002**

**(10) Malpractice Insurance**

The Hospital has professional liability insurance with limits of \$1,000,000 per claim 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 the Hospital's mandatory participation in the Patients' Compensation Fund of the State of Wisconsin.

In May 2003, Aurora formed Aurora Liability Assurance, Ltd. to assume the primary medical professional liability and general liability risks of Aurora and their affiliates through a reinsurance agreement with insurance companies. The primary medical and professional policies remain unchanged.