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City of West Allis Matter Summary

7525 W. Greenfield Ave.
West Allis, WI 53214

File Number	Title	Status
2006-0478	Report	In Committee
West Allis Memorial Hospital, Inc.'s financial statements for the year ended December 31, 2005 and Independent Auditors' report.		
Introduced: 8/1/2006		Controlling Body: Administration & Finance Committee

COMMITTEE RECOMMENDATION Accepted report & Place on file

ACTION DATE:	MOVER	SECONDER		AYE	NO	PRESENT	EXCUSED
AUG 07 2006		<input checked="" type="checkbox"/>	Barczak	<input checked="" type="checkbox"/>			
			Czaplewski	<input checked="" type="checkbox"/>			
			Dobrowski				
			Kopplin				
		<input checked="" type="checkbox"/>	Lajsic	<input checked="" type="checkbox"/>			
			Narlock				
			Reinke	<input checked="" type="checkbox"/>			
			Sengstock				
			Vitale				
		Weigel		<input checked="" type="checkbox"/>			
		TOTAL		5	0		

SIGNATURE OF COMMITTEE MEMBER

[Signature] _____
 Chair Vice-Chair Member

COMMON COUNCIL ACTION PLACE ON FILE APPROVAL

ACTION DATE:	MOVER	SECONDER		AYE	NO	PRESENT	EXCUSED
SEP 05 2006	<input checked="" type="checkbox"/>		Barczak	<input checked="" type="checkbox"/>			
			Czaplewski	<input checked="" type="checkbox"/>			
			Dobrowski	<input checked="" type="checkbox"/>			
			Kopplin	<input checked="" type="checkbox"/>			
			Lajsic	<input checked="" type="checkbox"/>			
			Narlock	<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		10	-		

Deloitte.



***West Allis Memorial
Hospital, Inc.***

***Financial Statements as of and for the Years
Ended December 31, 2005 and 2004 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) as of December 31, 2005 and 2004, 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. 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, 2005 and 2004, and the results of its operations, its changes in net assets, and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 17, 2006

WEST ALLIS MEMORIAL HOSPITAL, INC.

BALANCE SHEETS AS OF DECEMBER 31, 2005 AND 2004 (In thousands)

	2005	2004
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 87	\$ 56
Inventories and other current assets	831	1,057
Advances to and amounts due from affiliates, net	<u>84,788</u>	<u>68,372</u>
Total current assets	85,706	69,485
Assets Whose Use Is Limited	49	47
Advances To Affiliates	21,721	15,153
Property, Plant, And Equipment, Net	116,773	122,909
Other Assets, Including Interest In Net Assets Of Unconsolidated Foundation	<u>2,811</u>	<u>2,775</u>
TOTAL ASSETS	<u>\$ 227,060</u>	<u>\$ 210,369</u>
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Current installments of long-term debt	\$ 2,735	\$ 2,630
Accounts payable	5,151	4,187
Estimated third-party payor settlements	6,221	6,253
Due to affiliates	5,449	2,858
Accrued expenses	<u>4,935</u>	<u>4,594</u>
Total current liabilities	24,491	20,522
Long-Term Debt, Less Current Installments	38,650	41,373
Other Long-Term Liabilities	<u>237</u>	<u>-</u>
Total liabilities	<u>63,378</u>	<u>61,895</u>
Net Assets:		
Unrestricted	163,014	147,854
Temporarily restricted	<u>668</u>	<u>620</u>
Total net assets	<u>163,682</u>	<u>148,474</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 227,060</u>	<u>\$ 210,369</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, 2005 AND 2004 (In thousands)

	2005	2004
Revenue:		
Net Patient Service Revenue	\$ 172,443	\$ 164,901
Other Revenue	<u>6,730</u>	<u>5,537</u>
Total revenue	<u>179,173</u>	<u>170,438</u>
Expenses:		
Salaries	46,157	44,131
Fringe benefits	14,346	13,674
Professional fees	3,228	3,078
Supplies	22,314	20,705
Depreciation and amortization	8,820	8,860
Interest	2,256	2,345
Management services and operational support	40,674	39,709
Provision for bad debts	5,241	4,488
Other	<u>20,832</u>	<u>18,464</u>
Total expenses	<u>163,868</u>	<u>155,454</u>
Operating income	15,305	14,984
Nonoperating Gain	<u>9</u>	<u>18</u>
Excess of Revenue over Expenses	15,314	15,002

(Continued)

WEST ALLIS MEMORIAL HOSPITAL, INC.

STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004 (In thousands)

	2005	2004
Unrestricted Net Assets:		
Excess of revenue over expenses	\$ 15,314	\$ 15,002
Transfers from affiliates, net	53	139
Cumulative effect of accounting change	<u>(207)</u>	<u>-</u>
Increase in unrestricted net assets	15,160	15,141
Temporarily Restricted Net Assets:		
Change in interest in net assets of unconsolidated foundation	<u>48</u>	<u>63</u>
Total increase in net assets	15,208	15,204
Net Assets:		
Beginning of year	<u>148,474</u>	<u>133,270</u>
End of year	<u>\$ 163,682</u>	<u>\$ 148,474</u>
See notes to financial statements.		(Concluded)

WEST ALLIS MEMORIAL HOSPITAL, INC.

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004 (In thousands)

	2005	2004
Cash Flows From Operating Activities:		
Change in net assets	\$ 15,208	\$ 15,204
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	8,820	8,860
Provision for bad debts	5,241	4,488
Transfers from affiliates, net	(53)	(139)
Change in interest in net assets of unconsolidated foundation	(48)	(63)
Cumulative effect of accounting change	207	-
(Decrease) increase in estimated third-party payor settlements	(32)	1,501
Other, net	<u>1,555</u>	<u>(2,221)</u>
Net cash provided by operating activities	<u>30,898</u>	<u>27,630</u>
Cash Flows From Investing Activities:		
Capital expenditures	(2,654)	(2,854)
Increase in assets whose use is limited, net	(2)	(1)
Advances, transfers and amounts due to (from) affiliates, net	<u>(25,581)</u>	<u>(22,262)</u>
Net cash used in investing activities	<u>(28,237)</u>	<u>(25,117)</u>
Cash Flows From Financing Activities:		
Repayment of long-term debt	<u>(2,630)</u>	<u>(2,555)</u>
Net cash used in financing activities	<u>(2,630)</u>	<u>(2,555)</u>
Net Decrease in Cash and Cash Equivalents	31	(42)
Cash and Cash Equivalents:		
Beginning of year	<u>56</u>	<u>98</u>
End of year	<u>\$ 87</u>	<u>\$ 56</u>

See notes to financial statements.

WEST ALLIS MEMORIAL HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

1. DESCRIPTION OF ORGANIZATION

West Allis Memorial Hospital, Inc. (the Hospital) is a Wisconsin nonstock, not-for-profit corporation. 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 the sole corporate member of the Hospital.

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 network of 99 physician clinic facilities, home health services, 128 retail pharmacies, and other health care and related services.

During 2005 and 2004, management and administrative expenses comprised of 24.2% and 23.9% of total expenses, respectively. The remaining expenses were primarily related to the provision of health care services.

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 and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue 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 (including cash and cash equivalents, advances to and amounts due from affiliates, assets whose use is limited, accounts payable, accrued expenses, and estimated third-party settlements) approximates their fair value, due to their short-term maturities.

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 of three months or less.

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 sheet. Investment income or loss (including realized gains and losses, other than temporary declines in fair value, interest income, and dividends) is included in excess of revenue over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from excess of revenue over expenses unless such investments are classified as trading securities. The Hospital considers all of its investments to be other than trading securities.

Investment income, including investment income on advances to affiliates (see Note 7), is reported as other revenue. Investment income reported as other revenue totaled \$2,465,000 and \$1,459,000 in 2005 and 2004, respectively. Investment income on temporarily 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.

Accounts Receivable—The Hospital has an agreement to sell all of its receivables to Aurora, in connection with a system-wide, revolving period securitization transaction (see Note 7).

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 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 services, defined capital costs, medical education costs, certain drugs, certain 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.
- **Other Third-Party Payors** – Services rendered to patients insured by other third-party payors are primarily reimbursed based on a discount from customary charges or prospectively determined rates per discharge. Other payment arrangements include negotiated fee schedules, per diems, and capitated payments.

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

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.

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. To date, no such impairment adjustments have been necessary.

Deferred Financing Costs and Bond Discount—Long-term debt discount and 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 which approximate the interest yield method.

Capitalized Interest—Interest expense incurred during the period of construction is capitalized as a component of the cost of the asset, except in the case of restricted borrowings, where an alternative approach is applied. The amount capitalized is determined by applying an interest rate to the average amount of accumulated expenditures for the constructed assets until the assets are ready for their intended use.

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.

Net Assets—Unrestricted net assets arise as a result of the operations of the Hospital. Restricted net assets, which consist of temporarily 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. At December 31, 2005 and 2004, temporarily restricted net assets comprise assets held by an unconsolidated foundation for the benefit of the Hospital.

Net Patient Service Revenue—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. 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 decreased net patient service revenue by approximately \$900,000 in 2005 and \$1,400,000 in 2004. During 2005, the Hospital entered into a settlement agreement with a managed care provider to settle certain disputed patient claims relating to prior years. This settlement payment increased net patient service revenue by \$342,000 in 2005.

Other Revenue/Expense—Other revenue primarily comprises revenues from cafeteria sales, rental of hospital space, investment income, and other miscellaneous services. Other expense primarily consists of occupancy, maintenance and repairs, and other administrative costs.

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. Charges relating to charity care provided were \$4,830,000 and \$4,574,000 in 2005 and 2004, respectively.

Excess of Revenue over Expenses—The statement of operations includes excess of revenue over expenses. Changes in unrestricted net assets which are excluded from excess of revenue over expenses, consistent with industry practice, include unrealized gains and losses on investments not restricted by donor or by law, permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets), and other items that are required by generally accepted accounting principles to be reported separately (such as extraordinary items, the effect of discontinued operations, and the cumulative effect of accounting changes).

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 which 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 Aurora 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 plan administrator. The Hospital's expense for the Aurora Pension Plan was \$2,508,000 and \$2,532,000 in 2005 and 2004, respectively, representing 6.1% and 7.3%, of the total recorded pension expense for the Aurora Pension Plan, respectively. At December 31, 2005 and 2004, the projected benefit obligation of the Aurora Pension Plan totaled \$649,771,000 and \$525,456,000, respectively. The accumulated benefit obligation totaled \$565,451,000 and \$478,310,000, and the fair value of the related plan assets totaled \$414,297,000 and \$330,922,000, at December 31, 2005 and 2004, respectively.

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 contributory defined contribution plan which is sponsored and administered by Aurora. The Aurora 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. The Hospital's expense for the Aurora Savings Plan was \$620,000 and \$584,000 in 2005 and 2004, respectively.

New Accounting Pronouncements—The Hospital adopted FIN 47, *Accounting for Conditional Asset Retirement Obligations*, during 2005. FIN 47 clarifies the term conditional asset retirement obligation as used in SFAS No. 143, *Accounting for Asset Retirement Obligations*, and requires a liability to be recorded if the fair value of the obligation to retire an asset can be reasonably estimated. Asset retirement obligations covered by FIN 47 include those for which an entity has a legal obligation to perform an asset retirement activity, however the timing and (or) method of settling the obligation are conditional on a future event that may or may not be within the control of the entity.

Consistent with FIN 47, the Hospital records all known asset retirement obligations for which the fair value of the liability can be reasonably estimated, including certain obligations relating to asbestos abatement and storage tank removal. As a result of adopting FIN 47, the Hospital recorded a cumulative effect of accounting change of \$207,000 during 2005. In addition, the Hospital recognized asset retirement obligations of \$237,000 (including cumulative accretion) and asset retirement costs of \$30,000 (net of accumulated depreciation). Had FIN 47 been applied as of the earliest period presented, the pro forma effect on the Hospital's financial position and results of operations would not have been materially different from amounts presented at or for the years ended December 31, 2005 and 2004.

In addition to the amounts recorded, the Hospital may have other conditional asset retirement obligations as yet unknown to management. Such obligations have not been recorded in the financial statements. A liability for these obligations will be recorded in the period when the matters become known and sufficient information becomes available to estimate the fair value of the related amounts.

Reclassifications—Certain items in the 2004 financial statements have been reclassified to conform with the presentations used in 2005, including operational support amounts reclassified from advances to and amounts due from affiliates to due to affiliates at December 31, 2004.

3. ASSETS WHOSE USE IS LIMITED

Assets whose use is limited or restricted is comprised of a certificate of deposit valued at \$49,000 and \$47,000 at December 31, 2005 and 2004, respectively, and is stated at fair market value. The funds are designated for continuing education for the board of directors and are classified in the balance sheet as a long-term asset.

4. PROPERTY, PLANT, AND EQUIPMENT

The following is a summary of the components of property, plant and equipment (see Note 8) at December 31, 2005 and 2004 (in thousands):

	2005	2004
Land and improvements	\$ 1,794	\$ 1,710
Buildings and fixed equipment	174,508	173,109
Movable equipment	45,030	44,579
Construction in progress	<u>1,484</u>	<u>1,620</u>
	222,816	221,018
Less accumulated depreciation	<u>(106,043)</u>	<u>(98,109)</u>
Property, plant and equipment, net	<u>\$ 116,773</u>	<u>\$ 122,909</u>

At December 31, 2005, construction in progress consisted of various improvement projects. There was no capitalized interest recorded in 2005 or 2004.

5. LONG-TERM DEBT AND LEASE COMMITMENTS

Long-term debt at December 31, 2005 and 2004 is summarized as follows (in thousands):

	2005	2004
Wisconsin Health and Educational Facilities Authority bonds, net of unamortized discount	\$ 26,093	\$ 26,093
City of West Allis (City) general obligation bonds and promissory notes, net of unamortized discount (see Note 8)	<u>15,292</u>	<u>17,910</u>
	41,385	44,003
Less current installments	<u>(2,735)</u>	<u>(2,630)</u>
Long-term debt, less current installments	<u>\$ 38,650</u>	<u>\$ 41,373</u>

Aurora has issued general obligation 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, unsecured, 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 will 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 2029, 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. The unamortized discount was \$88,000 and \$101,000 at December 31, 2005 and December 31, 2004, respectively. Interest rates are fixed and ranged from 2.0% to 4.5% at December 31, 2005 and 1.1% to 4.25% at December 31, 2004 (see Note 8).

Certain borrowing agreements require deposits to or the establishment and maintenance of sinking or other special funds under the control of trustees. 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. At December 31, 2005, management believes the Hospital and Aurora were in compliance with the covenants contained in the debt agreements.

Scheduled maturities on all long-term debt (excluding amortization of bond discounts of \$88,000) at December 31, 2005 are as follows:

2006	\$ 2,735
2007	2,050
2008	2,125
2009	2,225
2010	2,305
Thereafter	<u>30,033</u>
Total	<u>\$ 41,473</u>

The estimated fair market value of long-term debt, based on discounted cash flows at estimated current borrowing rates, approximated \$42,045,000 and \$44,732,000 at December 31, 2005 and 2004, respectively.

Cash payments for interest totaled \$2,237,000 and \$2,320,000 in 2005 and 2004, respectively.

6. 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 \$6,161,000 and \$4,904,000 in 2005 and 2004, 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.

7. ADVANCES TO AND TRANSACTIONS WITH AFFILIATES

Aurora has entered into a series of agreements under which it sold and will continue to sell certain 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 securitization, the Hospital sells,

without recourse and on an ongoing basis, its patient accounts receivable to Aurora. As consideration for such sales, the Hospital records an intercompany receivable equal to the net value of the patient receivables sold. At December 31, 2005 and 2004, the net patient accounts receivable sold totaled \$16,595,000 and \$16,800,000, respectively, net of allowance for doubtful accounts of \$10,096,000 and \$8,374,000, respectively. The intercompany receivable 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. Affiliates which, on a net basis, have advanced funds earn interest on such advances. Similarly, affiliates which, on a net basis, have borrowed funds incur interest expense on those borrowings. Interest rates credited or charged approximate those earned by Aurora on its centralized depository accounts. At December 31, 2005 and 2004, the Hospital's portion of Aurora's cash concentration accounts totaled \$89,914,000 and \$66,725,000, respectively. Such amounts are classified as current and noncurrent in the accompanying financial statements in the same proportion as Aurora's consolidated current and noncurrent cash and investments. Interest income credited to the Hospital on its portion of Aurora's cash concentration accounts totaled \$2,445,000 and \$1,437,000 in 2005 and 2004, respectively, and is included in other revenue.

Amounts advanced to Aurora have been primarily used to fund advances to or investments in the various operating members of the Aurora system. Management of Aurora believes the 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 \$40,674,000 and \$39,709,000 (including operational support of \$3,256,000 and \$3,164,000) in 2005 and 2004, respectively. At December 31, 2005 and 2004, the Hospital owed \$5,449,000 and \$2,858,000, respectively, to affiliated organizations for such activities, included in due to affiliates in the accompanying financial statements.

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 \$6,451,000 and \$5,796,000 in 2005 and 2004, 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, consistent with industry practice. Net transfers of assets and liabilities from affiliates amounted to \$53,000 in 2005 and \$139,000 in 2004.

The Aurora Foundation, Inc. (the Foundation) holds unrestricted assets of \$668,000 and \$620,000 at December 31, 2005 and 2004, 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 sheet. Amounts received from the Foundation for educational and operating purposes were not significant in 2005 and 2004.

8. 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 \$1,671,000 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 4) and the general obligation bonds related to the leased facilities are included with the Hospital's long-term debt (see Note 5). 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. Historically, these payments have not been material to the Hospital's financial statements. The lease agreement expires in 2038.

Total rent expense on operating leases for property and equipment approximated \$2,118,000 and \$2,350,000 in 2005 and 2004, respectively.

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

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 potential exclusion from the Medicare and Medicaid programs. As a result, there is a reasonable possibility that recorded estimated third-party settlements and related reserves could change by a material amount.

The Hospital believes it has made adequate provision for potential exposures relating to legal and regulatory matters. In the opinion of the Company, 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 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 covered through the Hospital's mandatory participation in the Patients' Compensation Fund of the State of Wisconsin.

Aurora Liability Assurance, Ltd., a wholly owned subsidiary of Aurora, assumes the primary medical professional liability and general liability risks of Aurora and its affiliates, including the Hospital, through a reinsurance agreement with insurance companies. 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; and directors and officers liability. 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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