

**PETALUMA HEALTH CARE DISTRICT**

**Petaluma, California**

**FINANCIAL STATEMENTS WITH  
INDEPENDENT AUDITORS' REPORT**

**June 30, 2007 and 2006**

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June 30, 2007 and 2006

*Petaluma Health Care District*

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Petaluma Health Care District  
Petaluma, California

We have audited the accompanying statements of net assets of Petaluma Health Care District (the District), as of and for the years ended June 30, 2007 and 2006, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of June 30, 2007 and 2006, and the 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, as well as accounting systems prescribed by the State Controller's Office and state regulations governing special districts.

The District has not presented management's discussion and analysis (MD&A) that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be a part of, the basic statements.

*Matson and Isom*

September 24, 2007

**STATEMENTS OF NET ASSETS**

*Petaluma Health Care District*

June 30	<b>2007</b>	<b>2006</b>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 6,061	\$ 53,074
Accounts receivable - net of allowance of \$2,000 (2007 and 2006)	60,268	31,595
Prepaid expenses and deposits	24,774	20,436
Notes receivable - current portion	147,932	257,172
<b>Total Current Assets</b>	<b>239,035</b>	<b>362,277</b>
<b>NONCURRENT INVESTMENTS</b>	<b>3,205,271</b>	<b>4,258,953</b>
<b>OTHER ASSETS</b>		
Deferred affiliation costs - net	172,707	190,719
Notes receivable - net of current portion	124,332	261,045
Goodwill	30,000	40,000
<b>Total Other Assets</b>	<b>327,039</b>	<b>491,764</b>
<b>CAPITAL ASSETS - NET</b>	<b>11,989,989</b>	<b>12,449,830</b>
<b>Total Assets</b>	<b>\$ 15,761,334</b>	<b>\$ 17,562,824</b>
<b>LIABILITIES AND NET ASSETS</b>		
<b>CURRENT LIABILITIES</b>		
Current maturities of long-term debt	\$ 36,240	\$ 154,673
Line of credit	-	200,000
Accounts payable	91,824	98,510
Accrued liabilities:		
Payroll and vacation	63,175	65,986
Benefits	189,695	193,611
Interest	-	14,908
<b>Total Current Liabilities</b>	<b>380,934</b>	<b>727,688</b>
<b>LONG-TERM DEBT</b>		
Net of current maturities	24,438	735,997
<b>OTHER LIABILITIES</b>	57,422	48,555
<b>DEFERRED REVENUE - NET</b>	<b>3,998,179</b>	<b>4,416,955</b>
<b>Total Liabilities</b>	<b>4,460,973</b>	<b>5,929,195</b>
<b>NET ASSETS</b>		
Invested in capital assets - net of related debt	11,929,311	11,559,160
Unrestricted (Deficit)	(628,950)	74,469
<b>Total Net Assets</b>	<b>11,300,361</b>	<b>11,633,629</b>
<b>Total Liabilities and Net Assets</b>	<b>\$ 15,761,334</b>	<b>\$ 17,562,824</b>

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

**STATEMENTS OF REVENUES, EXPENSES,  
AND CHANGES IN NET ASSETS**

*Petaluma Health Care District*

Years Ended June 30	2007	2006
<b>OPERATING REVENUE</b>		
Program service fees	\$ 1,392,211	\$ 1,270,974
Rental income	1,053,215	1,160,863
<b>Total Revenue</b>	2,445,426	2,431,837
<b>OPERATING EXPENSES</b>		
Salaries, wages, and benefits	899,006	776,544
Depreciation and amortization	794,079	780,606
Professional fees	126,720	146,115
Purchased services	558,013	480,555
Bad debt expense	107,805	69,823
Operating supplies	35,890	26,400
Office supplies	38,037	40,941
Insurance	35,665	32,891
Utilities	46,538	46,048
Repairs and maintenance	45,055	47,701
Rents and leases	123,707	77,602
Advertising and promotion	56,498	54,273
Community support	57,089	28,765
Meetings and training	10,582	15,690
Dues and subscriptions	13,597	15,481
Travel	17,972	26,493
Due diligence	-	41,743
Other	55,730	28,275
<b>Total Expenses</b>	3,021,983	2,735,946
<b>Loss From Operations</b>	(576,557)	(304,109)
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Investment income	238,583	57,096
Other income	17,729	-
Interest expense	(13,023)	(120,492)
<b>Total Nonoperating Revenues (Expenses)</b>	243,289	(63,396)
<b>Change in Net Assets</b>	(333,268)	(367,505)
<b>Net Assets - Beginning of Year</b>	11,633,629	12,001,134
<b>Net Assets - End of Year</b>	\$ 11,300,361	\$ 11,633,629

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

**STATEMENTS OF CASH FLOWS***Petaluma Health Care District*

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<u>Years Ended June 30</u>	<u>2007</u>	<u>2006</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts for services and support	\$ 1,363,538	\$ 1,256,499
Rental receipts	634,439	742,087
Payments to suppliers and contractors	(1,339,922)	(1,118,381)
Payments on behalf of employees	(905,733)	(854,014)
Other receipts and payments	8,867	(146,121)
<b>Net Cash Used by Operating Activities</b>	<u>(238,811)</u>	<u>(119,930)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchase of capital assets	(306,228)	(386,133)
Line of credit (payments) proceeds	(200,000)	200,000
Proceeds from long-term debt	29,000	36,200
Debt payments	(858,992)	(815,063)
Interest paid on long-term debt	(8,884)	(94,521)
<b>Net Cash Used by Capital and Related Financing Activities</b>	<u>(1,345,104)</u>	<u>(1,059,517)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Investment income received	336,877	155,339
Net transfer of investments	954,072	1,013,948
Change in physician loans	245,953	15,794
<b>Net Cash Provided by Investing Activities</b>	<u>1,536,902</u>	<u>1,185,081</u>
<b>Net (Decrease) Increase in Cash and Cash Equivalents</b>	(47,013)	5,634
<b>Cash and Cash Equivalents - Beginning of Year</b>	<u>53,074</u>	<u>47,440</u>
<b>Cash and Cash Equivalents - End of Year</b>	<u>\$ 6,061</u>	<u>\$ 53,074</u>

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

**STATEMENTS OF CASH FLOWS**

Years Ended June 30	<b>2007</b>	<b>2006</b>
<b>RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES</b>		
Operating loss	\$ (576,557)	\$ (304,109)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation and amortization	794,079	780,606
Deferred revenue amortization	(418,776)	(418,776)
Changes in:		
Accounts receivable	(28,673)	(14,475)
Prepaid expenses	(4,338)	1,659
Accounts payable	(6,686)	58,756
Accrued liabilities	(6,727)	(77,470)
Other liabilities	8,867	(146,121)
<b>Net Cash Used by Operating Activities</b>	<b>\$ (238,811)</b>	<b>\$ (119,930)</b>

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

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The following is a summary of significant accounting policies followed in the preparation of the financial statements.

**Nature of Operations** Petaluma Health Care District (the District) was organized in 1946 and is governed by elected officials. The District's purpose is to promote health care services in Petaluma, California, and the surrounding community.

**Basis of Accounting** Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the District has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, established financial reporting requirements for all state and local governments. The District has adopted the financial reporting provisions of GASB No. 34 but has elected not to present Management's Discussion and Analysis (MD&A) that GASB has determined is necessary to supplement, although not required to be part of, the basic financial statements.

**Use of Estimates** The preparation of financial statements, in conformity with generally accepted accounting principles, 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, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Cash and Cash Equivalents** Cash and cash equivalents include cash on hand and demand deposits in a financial institution.

**Investments** Noncurrent investments are designated by the Board of Directors for future programs and expansion over which the Board retains control and may, at its discretion, subsequently use for other purposes.

In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, highly liquid investments with maturities of one year or less at the time of purchase are stated at amortized cost. All other investments are stated at fair value. Fair value is determined from quoted market prices. The District is restricted by state law and the Board's investment policy in the types of investments that can be made.



June 30, 2007 and 2006

Permissible investments include the county treasury, the state Local Agency Investment Fund (LAIF), federally insured deposits, and individual securities. Individual securities must be backed by the federal government or rated AAA, AA, or A by Standard & Poor's or Aaa, Aa, or A by Moody's indices. In addition, maturities may not exceed five years, unless authorized by the District's investment policy. The proportion of investments in each of the permissible categories is restricted as defined in the *California Government Code* and further limited by the District's investment policy. The maximum maturity of funds invested is approximately ten years. The District's investment policy established safety of principal as the primary investment objective. The District's investment strategy is to realize a reasonable interest yield, and investment decisions are executed with the intent that they will be held to maturity.

The District realized a loss from sales of investments of \$64,754 at June 30, 2007. The calculation of realized gain or loss is independent of the calculation of the net change in the fair value of investments. Realized gains and losses on investments that had been held for more than one fiscal year and subsequently sold in the current year may have been recognized as an increase or decrease in the fair value of investments reported in the prior year. The unrealized gain on investments was \$71,767 at June 30, 2007, and a loss of \$98,294 at June 30, 2006. This amount takes into account all changes in fair value, including purchases and sales that occurred during the year.

**Goodwill** Goodwill is the excess of cost over net tangible assets of acquiring a personal response system program. Goodwill is amortized over five years. Accumulated amortization amounted to \$20,000 and \$10,000 at June 30, 2007 and 2006, respectively.

**Capital Assets** Capital assets are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method.

**Operating Income and Expenses** The statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating income and expenses. Operating revenues result from exchange transactions generated from program service fees and rental income. Nonexchange revenues, including grants and contributions, if any, received for purposes other than capital asset acquisition, are reported as nonoperating income. Operating expenses are all expenses incurred to provide operating income, other than financing costs.

**Equity** Equity is classified into two components. These components consist of: 1) Invested in capital assets net of related debt, which consists of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets; and 2) Unrestricted, which is the remaining equity that does not meet the other criteria.

**Risk Management** The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years. The District participates in two joint powers agreements for comprehensive liability coverage and for workers' compensation coverage.

**2. LEASE/AFFILIATION AGREEMENT**

On November 4, 1996, the District signed an agreement with SRM Alliance Hospital Services, a California nonprofit public benefit corporation (Alliance), to lease Petaluma Valley Hospital, the facility housing the hospice program, and all of the personal property used in connection with those operations. The agreement also contained provisions to assign the District's interest in various leased equipment and real estate, third-party participation agreements, licenses, trademarks, and other intangible property, along with the transfer of ownership of inventory and patient medical records. The agreement commenced on January 19, 1997, for a period of 20 years.

In consideration for this agreement, Alliance agreed to pay cash, pay off certain debts, and become the primary obligor on other debts. The amount of lease payments attributable to real estate was recorded as an operating lease, the amount attributed to personal property was recorded as a sales-type lease, and the amount attributed to goodwill was recorded as a sale. The sales-type lease proceeds and sale of goodwill were recognized as income in 1997. The operating lease proceeds are deferred and amortized over the 20-year lease term. The allocation of lease proceeds was based on the related fair market values.

Alliance is to help fund a District-sponsored free clinic for a minimum of \$15,000 annually. Alliance has also committed to invest at least \$14 million in capital improvements to the Hospital with a minimum investment of \$500,000 annually over the lease term to total at least \$7 million invested by the tenth anniversary, which was January 19, 2007.

**3. CASH AND INVESTMENTS**

The following is a summary of cash and investments at June 30:

	<u>2007</u>	<u>2006</u>
CASH ON HAND	\$ 200	\$ 200
DEPOSITS (1)	<u>5,861</u>	<u>52,874</u>
<b>Subtotal</b>	<u>6,061</u>	<u>53,074</u>
INVESTMENTS THAT ARE NOT SECURITIES (2)		
Local Agency Investment Fund	698	665
Federal treasury obligations	<u>31,242</u>	<u>140,005</u>
<b>Subtotal</b>	<u>31,940</u>	<u>140,670</u>
INVESTMENT SECURITIES		
U.S. government securities	2,160,064	2,900,238
Corporate bonds	<u>1,013,267</u>	<u>1,218,045</u>
<b>Subtotal</b>	<u>3,173,331</u>	<u>4,118,283</u>
<b>Total Cash and Investments</b>	<u>\$ 3,211,332</u>	<u>\$ 4,312,027</u>

**NOTES TO FINANCIAL STATEMENTS***Petaluma Health Care District*

June 30, 2007 and 2006

(1) *Deposits* The carrying amount of deposits includes demand deposits in a financial institution.

(2) *Investments That are Not Securities* A “security” is a transferable financial instrument that evidences ownership, whether in physical or book entry form. Investments that are not securities do not have custodial credit risk because they do not involve a transferable financial instrument. Thus, they are not subject to custodial credit risk.

**Custodial Credit Risk – Deposits**

Custodial credit risk is the risk that in the event of a bank failure, the District’s deposits may not be returned. The District has a collateralization agreement with the bank, which mitigates custodial credit risk. The cash balance in the bank at June 30, 2007, amounted to \$61,373. Deposits amounting to \$100,000 are covered by depository insurance, and the balance, if any, is subject to the collateralization agreement.

**Credit Risk – Investments**

*California Government Code*, Section 53601 limits investments in commercial paper to “prime” quality of the highest ranking or of the highest letter and numerical rating as provided by nationally recognized statistical rating organizations (NRSRO) and limits investments in medium-term notes to a rating of A or better. Individual securities must be backed by the federal government or rated AAA, AA, or A by Standard & Poor’s or Aaa, Aa, or A by Moody’s indices. The District has no investment policy that would further limit its investment choices.

Investments by investment type and ratings are as follows at June 30, 2007:

<b>Investment Type</b>	<b>Fair Value / Amortized Cost</b>	<b>AAA</b>	<b>A+ or AA</b>	<b>A</b>	<b>Not Rated</b>
Local Agency Investment Fund	\$ 698	\$ -	\$ -	\$ -	\$ 698
Federal treasury obligations	31,242	-	-	-	31,242
U.S. government securities	2,160,064	1,477,985	511,075	-	171,004
Corporate bonds	1,013,267	-	711,965	301,302	-
<b>Totals</b>	<b>\$3,205,271</b>	<b>\$1,477,985</b>	<b>\$1,223,040</b>	<b>\$ 301,302</b>	<b>\$ 202,944</b>

**NOTES TO FINANCIAL STATEMENTS**

June 30, 2007 and 2006

*Petaluma Health Care District*

Investments by investment type and ratings are as follows at June 30, 2006:

Investment Type	Fair Value / Amortized Cost	AAA	A+ or AA	A	Not Rated
Local Agency Investment Fund	\$ 665	\$ -	\$ -	\$ -	\$ 665
Commercial paper	140,005	140,005	-	-	-
U.S. government securities	2,900,238	2,702,793	-	-	197,445
Corporate bonds	1,218,045	-	1,018,637	199,408	-
<b>Totals</b>	\$4,258,953	\$2,842,798	\$1,018,637	\$ 199,408	\$ 198,110

**Interest Rate Risk – Investments**

*California Government Code*, Section 53601 limits investments to maturities of five years, unless the governing body has authorized the longer terms. The District has not adopted a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates.

Investments grouped by maturity date at June 30, 2007, are as follows:

Maturity	Fair Value/ Amortized Cost
Less than one year	\$ 1,509,925
One to five years	1,524,342
Six to ten years	12,344
More than ten years	158,660
<b>Total</b>	\$ 3,205,271

Investments grouped by maturity date at June 30, 2006, are as follows:

Maturity	Fair Value/ Amortized Cost
Less than one year	\$ 1,688,294
One to five years	2,373,214
Six to ten years	19,193
More than ten years	178,252
<b>Total</b>	\$ 4,258,953

**NOTES TO FINANCIAL STATEMENTS**

June 30, 2007 and 2006

*Petaluma Health Care District***4. NOTES RECEIVABLE**

Loans have been made to physicians, which are due over one to five years. The loans have varying interest rates and terms. Notes receivable amounted to \$285,686 and \$359,025 at June 30, 2007 and 2006, respectively. The allowances for uncollectible amounts totaled \$78,204 and \$83,500 at June 30, 2007 and 2006, respectively.

**5. CAPITAL ASSETS**

Capital assets consisted of the following at June 30, 2007:

	<b>Balance June 30, 2006</b>	<b>Additions</b>	<b>Balance June 30, 2007</b>
Land	\$ 2,065,516	\$ -	\$ 2,065,516
Buildings and improvements	26,228,193	3,292	26,231,485
Construction in progress	64,799	-	64,799
Furniture and equipment	2,097,446	302,936	2,400,382
<b>Subtotal</b>	<b>30,455,954</b>	<b>306,228</b>	<b>30,762,182</b>
Less: Accumulated depreciation	18,006,124	766,069	18,772,193
<b>Capital Assets - Net</b>	<b>\$ 12,449,830</b>	<b>\$ (459,841)</b>	<b>\$ 11,989,989</b>

Capital assets consisted of the following at June 30, 2006:

	<b>Balance June 30, 2005</b>	<b>Additions</b>	<b>Balance June 30, 2006</b>
Land	\$ 2,065,516	\$ -	\$ 2,065,516
Buildings and improvements	26,091,272	136,921	26,228,193
Construction in progress	56,524	8,275	64,799
Furniture and equipment	1,856,509	240,937	2,097,446
<b>Subtotal</b>	<b>30,069,821</b>	<b>386,133</b>	<b>30,455,954</b>
Less: Accumulated depreciation	17,253,529	752,595	18,006,124
<b>Capital Assets - Net</b>	<b>\$ 12,816,292</b>	<b>\$ (366,462)</b>	<b>\$ 12,449,830</b>

**6. DEFERRED AFFILIATION COSTS**

Costs incurred for the lease/affiliation agreement were allocated between costs attributed to the operating lease, costs attributed to the sale of personal property, and goodwill in the same ratio as the proceeds allocated from the agreement. Costs attributed to the operating lease are capitalized and will be amortized over the life of the lease. Accumulated amortization amounted to \$187,637 and \$169,625 at June 30, 2007 and 2006, respectively.

## NOTES TO FINANCIAL STATEMENTS

June 30, 2007 and 2006

*Petaluma Health Care District*

### **7. LINE OF CREDIT**

The District entered into a revolving line of credit agreement with a bank, which provides for advances up to \$200,000. Interest is payable monthly on the outstanding advances at the rate of 9.25%, secured by the assets of the District. As of June 30, 2007, there was no outstanding balance.

**NOTES TO FINANCIAL STATEMENTS**

June 30, 2007 and 2006

*Petaluma Health Care District*

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**8. LONG-TERM DEBT**

Long-term debt consisted of the following:

	<u>Balance</u> <u>June 30, 2005</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance</u> <u>June 30, 2006</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance</u> <u>June 30, 2007</u>
Note payable to Sonoma County in annual installments, including interest at a variable rate between 5.6% and 7.75% (approximately \$2,100 per year until 2010).	\$ 8,259	-	\$ 1,445	\$ 6,814	\$ -	\$ 1,521	\$ 5,293
Note payable to Municipal Leasing Associates, Inc., payable in monthly installments of \$15,552 from July 1999 to June 2009, including interest at 5.00%. The note was secured by revenues and paid off in 2006.	675,313	-	675,313	-	-	-	-
Note payable to Municipal Finance Corporation, payable in semi-annual installments of \$29,968 through August 2010, including interest at 5.8%. The note is secured by equipment.	278,826	-	44,399	234,427	-	234,427	-
<b>Balance Forward</b>	<u>\$ 962,398</u>	<u>\$ -</u>	<u>\$ 721,157</u>	<u>\$ 241,241</u>	<u>\$ -</u>	<u>\$ 235,948</u>	<u>\$ 5,293</u>

**NOTES TO FINANCIAL STATEMENTS**

June 30, 2007 and 2006

*Petaluma Health Care District*

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	<u>Balance</u> <u>June 30, 2005</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance</u> <u>June 30, 2006</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance</u> <u>June 30, 2007</u>
<b>Balance Brought Forward</b>	\$ 962,398	\$ -	\$ 721,157	\$ 241,241	\$ -	\$ 235,948	\$ 5,293
Note payable to Ford Motor Credit, payable in monthly installments of \$603 through May 2011 with no interest. The note is secured by a vehicle.	-	36,200	-	36,200	-	7,843	28,357
Note payable to Municipal Finance Corporation, payable in semi-annual installments of \$64,907 through August 2011, including interest at 5.25%. The note is secured by property and equipment.	707,135	-	93,906	613,229	-	613,229	-
Note payable to Capital One Auto Finance, payable in monthly installments of \$492 through February 2013, including interest at 6.69%. The note is secured by a vehicle.	-	-	-	-	29,000	1,972	27,028
<b>Total Long-Term Debt</b>	<u>\$ 1,669,533</u>	<u>\$ 36,200</u>	<u>\$ 815,063</u>	<u>\$ 890,670</u>	<u>\$ 29,000</u>	<u>\$ 858,992</u>	<u>\$ 60,678</u>



**NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2007 and 2006

*Petaluma Health Care District*

Scheduled principal and interest payments on long-term debt are as follows:

Year Ending June 30	Principal Amount	Interest Amount
2008	\$ 36,240	\$ 978
2009	8,668	283
2010	9,133	147
2011	6,637	-
<b>Total</b>	<b>\$ 60,678</b>	<b>\$ 1,408</b>

**9. OTHER LIABILITIES**

Other liabilities include a rent deposit of \$21,223 and \$42,158 for the years ended June 30, 2007 and 2006, respectively, a \$25,000 refund to Larry L. Hillblom Foundation for June 30, 2007, plus other minor liabilities for both years.

**10. DEFERRED REVENUE**

Deferred revenue includes prepaid operating lease payments. The operating lease payments are recognized as rental income over the term of the lease. Deferred revenue recognized in 2007 and in 2006 amounted to \$418,776, and accumulated revenue amortized amounted to \$4,376,884 and \$3,958,109 at June 30, 2007 and 2006, respectively.

**11. OPERATING LEASE AGREEMENTS**

The District is the lessor of certain land and buildings under noncancelable operating leases. Future minimum rental receipts under the operating leases are as follows:

2008	\$ 503,186
2009	\$ 398,141
2010	\$ 135,122

The District entered into operating leases for professional and office space, which expire in various years through July 2012. Minimum future rental payments under noncancelable operating leases having remaining terms in excess of one year as of June 30, 2007, are as follows:

2008	\$ 174,195
2009	\$ 157,964
2010	\$ 137,335
2011	\$ 142,010
2012	\$ 95,801
Thereafter	\$ 5,925

Rent expense amounted to \$115,664 and \$76,496 at June 30, 2007 and 2006, respectively.

**12. PENSION PLANS**

The District sponsors the Deferred Compensation Plan of Petaluma Health Care District, a defined contribution retirement plan under *Internal Revenue Code*, Section 457. All permanent employees 21 years of age or older are eligible to participate. Participants may contribute up to 22% of their annual salary. The District will match 50% of the participant’s contribution to a maximum of 2.5% of their salary. Total participant and District contributions are immediately 100% vested.

The District also sponsors the Employees’ Retirement Plan of Petaluma Health Care District, a defined contribution profit sharing plan under *Internal Revenue Code*, Section 401(a). All permanent employees 21 years of age or older are eligible to participate. The District contributes 2% of the participant’s annual salary, and contributions are immediately 100% vested. Contributions to the two plans amounted to \$15,940 and \$16,383 for 2007 and 2006, respectively.

**13. POSTRETIREMENT BENEFITS**

Under an amended policy adopted by the Board of Directors in July 2000, retired directors who were in office on January 1, 1991, or retired directors who served in office through December 31, 2000, and who completed 12 years of service prior to retirement, upon termination, were eligible to receive health and welfare benefits afforded to the employees of the District. The District pays the premiums for such retired directors and their eligible dependents. Such benefits extend after a director’s termination for the number of years equal to the number of years served by the director as a member of the Board. The Board of Directors adopted a new policy in 2003 whereby the District will not provide medical benefits to directors assuming office as of January 1, 2001, or to re-elected directors assuming office as of January 1, 2001, but will continue to provide medical benefits both to those who are in office now for the rest of their term (ending this year or two years hence) and to former directors who are subject to the amended policy adopted in July 2000.

The District accrued an estimated liability for future costs of benefits provided under this policy based on an actuarial study conducted in 1996. This study utilized an entry age normal actuarial cost method with an interest rate assumption of 6% and a health inflation assumption of 5% per year. The liability amounted to approximately \$186,962 and \$191,964 at June 30, 2007 and 2006, respectively, and is included in accrued employee benefits.

The District finances obligations under this policy on a pay-as-you-go basis. Benefits paid amounted to \$38,534 and \$42,655 at June 30, 2007 and 2006, respectively. At June 30, 2007 and 2006, six participants were eligible to receive benefits under the policy.

#### **14. COMMITMENTS AND CONTINGENCIES**

##### **Joint Powers Agreements**

The District participates in a joint venture under a joint powers agreement (JPA) with the Association of California Healthcare Districts, Inc. – ALPHA FUND (the Fund). The Fund arranges for and provides certain member health care entities with pooled workers' compensation self-insurance.

At June 30, 2006, the Fund reported a deficit of \$7,509,348. Management of the Fund has a plan to strengthen reserves and eliminate the deficit through a variety of measures, including focused loss prevention efforts, cost containment measures, and more restrictive underwriting guidelines. Additionally, management will use actuarially developed rates and will expand their marketing efforts to include more nonprofit healthcare organizations with a favorable risk profile. Under the terms of the JPA, withdrawing or terminated members owe their pro rata share of any fund deficiency. A withdrawing or terminated member's pro rata share is based on its total contributions during its membership in the Fund as a percentage of the total contributions by all members during the same period. However, the District signed an indemnification agreement whereby the District is indemnified for that portion of the deficit payment obligation that is based on claims existing prior to July 1, 2003, and will continue to be indemnified until the last day of the first fiscal year starting on or after July 1, 2003, in which the audited financial statements no longer reflect a fund deficiency.

The District also participates in a joint venture under a joint powers agreement (JPA) with the Program BETA Risk Management Authority (the Program).

The Program was formed for the purpose of operating a comprehensive liability self-insurance program for certain healthcare districts of the Association of California Healthcare Districts, Inc. (ACHD). The Program operates as a separate JPA established as a public agency separate and distinct from ACHD. Each member hospital pays a premium commensurate with the level of coverage requested and shares surpluses and deficits proportionate to its participation in the Program. The Program provides coverage on a claims-made basis.

**NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2007 and 2006

*Petaluma Health Care District*

Condensed financial information of BETA Healthcare Group (which includes the Program BETA JPA) for the year ended December 31, 2006, and of the ALPHA Fund JPA for the year ended June 30, 2006, is as follows:

	<b>ALPHA Fund</b>	<b>BETA Healthcare Group</b>
Total assets	\$ 55,996,015	\$ 370,883,231
Total liabilities	63,505,363	294,084,146
<b>Fund Balance (Deficit)</b>	<b>\$ (7,509,348)</b>	<b>\$ 76,799,085</b>
Total revenues	\$ 32,201,563	\$ 82,369,211
Total expenditures	(19,871,020)	(73,608,383)
Member surplus funds contributed	-	(46,599)
Change in unrealized gains on investments	552,830	1,443,890
Former member assessments	429,515	(2,000,000)
<b>Net Increase in Fund Balance</b>	<b>\$ 13,312,888</b>	<b>\$ 8,158,119</b>

**Revenue Bonds**

Health Facility Revenue Bonds Series 1990A were advance funded in 1997. Funds were used to purchase securities that were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments (for the 1990A Series A Bonds). The 1990A Series A Bonds are considered defeased, and the related liability has been removed from the books. Total principal outstanding on the 1990A Series A Bonds as of June 30, 2007, was \$2,935,000.

**15. SUBSEQUENT EVENT**

On August 9, 2007, the District closed escrow on the sale of 1360 North McDowell Boulevard in Petaluma, California. This sale resulted in a gain of approximately \$2,172,000 for the District.