

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System and Aggregate Discretely Presented Component Units)**

*Audited Combined Financial Statements*  
*(and Required Supplementary Information)*

*Years Ended June 30, 2010 and 2009*



**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY  
(d/b/a Erlanger Health System)**

*Audited Combined Financial Statements (and Required Supplementary Information)*

*Years Ended June 30, 2010 and 2009*

---

Independent Auditor's Report..... 1

Management's Discussion and Analysis..... 3

*Audited Combined Financial Statements*

Combined Balance Sheets..... 10

Combined Statements of Revenue, Expenses and Changes in Net Assets ..... 12

Combined Statements of Cash Flows ..... 14

Notes to Combined Financial Statements ..... 16

*Required Supplementary Information*

Schedule of Expenditures of Federal Awards..... 50

Schedule of Expenditures of State and Other Financial Assistance ..... 52

Notes to Schedules of Expenditures of Federal Awards and State and

Other Financial Assistance..... 53

Schedule of Prior Audit Findings..... 54

Report on Internal Control Over Financial Reporting and on Compliance and Other

Matters Based on an Audit of Financial Statements Performed in Accordance

With *Government Auditing Standards* ..... 55

Report on Compliance with Requirements that Could Have a Direct and Material

Effect on Each Major Program and on Internal Control Over Compliance in Accordance

with OMB Circular A-133 ..... 57

Schedule of Findings and Questioned Costs..... 59



CERTIFIED PUBLIC ACCOUNTANTS

Pershing Yoakley & Associates, P.C.  
One Cherokee Mills, 2220 Sutherland Avenue  
Knoxville, TN 37919  
(p) (865) 673-0844 (f) (865) 673-0173  
(w) www.pyapc.com

## INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of  
Chattanooga-Hamilton County Hospital Authority  
(d/b/a Erlanger Health System):

We have audited the accompanying combined balance sheets of Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) and aggregate discretely presented component units, as of June 30, 2010 and 2009 and the related combined statements of revenue, expenses and changes in net assets and cash flows for the years then ended. These combined financial statements are the responsibility of Chattanooga-Hamilton County Hospital Authority's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of ContinuCare HealthServices, Inc., a discretely presented component unit, were not audited in accordance with *Government Auditing Standards*. 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 Chattanooga-Hamilton County Hospital Authority'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 respective financial position of the business-type activities and the aggregate discretely presented component units of Chattanooga-Hamilton County Hospital Authority as of June 30, 2010 and 2009, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2010 on our consideration of Chattanooga-Hamilton County Hospital Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and

compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's discussion and analysis on pages 3 through 9 is not a required part of the basic financial statements but supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Chattanooga-Hamilton County Hospital Authority's basic financial statements. The accompanying schedule of expenditures of federal awards and schedule of expenditures of state and other financial assistance are presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the State of Tennessee Comptroller of the Treasury, respectively, and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects in relation to the basic financial statements taken as a whole.

*Pauling Yarnley: Associate PC*

Knoxville, Tennessee  
November 8, 2010

*Management's Discussion and Analysis*

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY  
(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis*

*Years Ended June 30, 2010 and 2009*

---

MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis of Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System's financial performance provides an overview of the Primary Health System's financial activities for the fiscal year ended June 30, 2010

Erlanger Health System (the Primary Health System) is the largest health care provider in Southeast Tennessee. The Primary Health System maintains a number of very specialized clinical services such as Level I trauma, Level III neonatal, kidney transplantation, Regional Cancer Unit, a full service children's hospital, and open heart surgery, all of which are serviced by three "Life Force" helicopters and supported by subspecialty physicians (residents, faculty and private attending physicians) located on its campuses. In the fiscal year 2002, the Primary Health System entered into a partnership agreement with TriState Partners, L.L.P. and Plaza Physicians, LLC to form Plaza Surgery, G.P. In the fiscal year 2007, the Primary Health System sold 4.63% interest in Plaza Surgery, G.P. to Spine Surgery, P.C. The Primary Health System owns a controlling 51% share of this partnership.

OVERVIEW OF THE COMBINED FINANCIAL STATEMENTS

The combined financial statements consist of two parts: Management's Discussion and Analysis and the combined financial statements. The combined financial statements also include notes that explain in more detail some of the information in the combined financial statements.

The combined financial statements of the Primary Health System offer short-term and long-term financial information about its activities. The combined balance sheets include all of the Primary Health System's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to the Primary Health System's creditors (liabilities). The assets and liabilities are presented in a classified format, which distinguishes between current and long-term assets and liabilities. It also provides the basis for computing rate of return, evaluating the capital structure of the Primary Health System and assessing the liquidity and financial flexibility of the Primary Health System.

All of the current fiscal year's revenues and expenses are accounted for in the combined statements of revenues, expenses, and changes in net assets. These statements measure the success of the Primary Health System's operations over the past fiscal year and can be used to determine whether the Primary Health System has successfully recovered all of its costs through the services provided, as well as its profitability and credit worthiness.

The final required financial statement is the combined statements of cash flows. The primary purpose of this statement is to provide information about the Primary Health System's cash receipts, cash payments and net changes in cash resulting from operating, investing, non-capital

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY  
(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis - Continued*

*Years Ended June 30, 2010 and 2009*

---

OVERVIEW OF THE COMBINED FINANCIAL STATEMENTS - Continued

financing and financing activities. The statement also provides answers to such questions as: where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

The analyses of the combined financial statements of the Primary Health System begin on the next page. One of the most important questions asked about the Primary Health System's finances is "Is the financial condition of the Primary Health System as a whole better or worse as a result of the fiscal year's activities?" The combined balance sheets and the combined statements of revenues, expenses and changes in net assets report information about the Primary Health System's activities in a way that will help answer this question. These two statements report the net assets of the Primary Health System and changes in them. One can think of the Primary Health System's net assets – the difference between assets and liabilities – as one way to measure financial health or financial position. Over time, increases or decreases in the Primary Health System's net assets are one indicator of whether its financial health is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions, regulations and new or changed government legislation.

REPORTING ENTITY

The Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) was created by a private act passed by the General Assembly of the State of Tennessee on March 11, 1976, and adopted by a majority of the qualified voters of Hamilton County, Tennessee on August 5, 1976. The Primary Health System is considered the primary governmental unit for financial reporting purposes. As required by generally accepted accounting principles, these financial statements present the Primary Health System and its component units. The component units discussed below are included in the Primary Health System's reporting entity because of the significance of their operational or financial relationships with the Primary Health System.

ContinuCare HealthServices, Inc., Plaza Surgery, GP, and Erlanger Health Plan Trust are legally separate organizations for which the Primary Health System is either financially accountable or owns a majority interest. Accordingly, these organizations represent component units of the Primary Health System. The financial statements of Erlanger Health Plan Trust are blended with the financial statements of the Primary Health System, as the Board of Erlanger Health Plan Trust is substantially the same as that of the Primary Health System.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis - Continued*

*Years Ended June 30, 2010 and 2009*

---

**KEY FINANCIAL INDICATORS**

The following key financial indicators are for Erlanger Health System as a whole. They are inclusive of the Primary Health System, ContinuCare HealthServices, Inc., and the 51% controlling share of Plaza Surgery, GP.

- Excess revenues over expenses from operations for Erlanger Health System for the fiscal year 2010 is \$8.6 million compared to excess revenues over expenses from operations of \$10.8 million for the fiscal year 2009.
- Total cash and investment reserves are \$98.2 million (excluding \$106 million for Board restricted and \$37 million of funds held by Trustees or restricted by donors or others) as of June 30, 2010.
- Net days in accounts receivable for Erlanger Health System (utilizing a three month rolling average of net revenue) are 54 days at June 30, 2010 and June 30, 2009.
- For the fiscal year 2010, Erlanger Health System recognized \$7.4 million in essential access payments from the State of Tennessee compared to \$6.1 million in fiscal year 2009.
- For fiscal year 2010, Erlanger Health System recognized and received \$2.9 million in disproportionate share payments from the State of Tennessee compared to \$4.9 million in fiscal year 2009.
- For fiscal year 2010, Erlanger Health System recognized \$1.3 million in trauma fund payments from the State of Tennessee. For the fiscal year 2009, Erlanger Health System recognized trauma fund payments totaling \$2.3 million from the State of Tennessee.
- For fiscal year 2010, Erlanger Health System recognized \$2.1 million in Federally Qualified Health Center (FQHC) cost report settlements from the State of Tennessee.

The required bond covenants ratios for fiscal year 2010 compared to bond requirements are as follows:

	<i>Bond Requirements</i>				
	<i>June 30, 2010</i>	<i>97 Series</i>	<i>98 Series</i>	<i>00 Series</i>	<i>04 Series</i>
Debt service coverage ratio	2.35	1.35	1.35	1.35	1.35
Cushion ratio	10.93	N/A	1.50	N/A	N/A
Current ratio	2.37	1.50	1.50	1.50	1.50
Days cash on hand	121 days			65 days	65 days
Indebtedness ratio	46.83%				65%

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis - Continued*

*Years Ended June 30, 2010 and 2009*

NET ASSETS

Erlanger Health System's net assets for the combined Primary Health System and ContinuCare increased by \$4 million in the fiscal year 2010. Our analysis focuses on the net assets (Table 1) and changes in net assets (Table 2) of the Primary Health System's operating activities. Discussion focuses on the Primary Health System and its blended component unit.

**Table 1 - Net Assets (in Millions)**

	June 30, 2010			June 30, 2009		
	Primary Health System	ContinuCare Health Services, Inc.	Plaza Surgery, G.P.	Primary Health System	ContinuCare Health Services, Inc.	Plaza Surgery, G.P.
Current and other assets	\$ 339	\$ 13	\$ 2	\$ 319	\$ 13	\$ 9
Capital assets	162	2	-	172	2	-
<b>Total assets</b>	<b>\$ 501</b>	<b>\$ 15</b>	<b>\$ 2</b>	<b>\$ 491</b>	<b>\$ 15</b>	<b>\$ 9</b>
Long-term debt outstanding	\$ 183	\$ -	\$ -	\$ 189	\$ -	\$ -
Other liabilities	114	3	1	103	2	-
<b>Total liabilities</b>	<b>\$ 297</b>	<b>\$ 3</b>	<b>\$ 1</b>	<b>\$ 292</b>	<b>\$ 2</b>	<b>\$ -</b>
Net assets						
Capital assets, net of debt	\$ 5	\$ 2	\$ -	\$ 6	\$ 2	\$ 7
Restricted, expendable	2	-	-	3	-	-
Unrestricted	197	10	1	190	11	2
<b>Total net assets</b>	<b>\$ 204</b>	<b>\$ 12</b>	<b>\$ 1</b>	<b>\$ 199</b>	<b>\$ 13</b>	<b>\$ 9</b>

Net assets for the Primary Health System have increased from \$199 million as of June 30, 2009 to \$204 million as of June 30, 2010, a 2.3 percent increase. The current ratio (current assets divided by current liabilities) decreased from 2.52 in 2009 to 2.28 in 2010 for the Primary Health System. The decrease in the current ratio was primarily due to a move of \$17.3 million from short-term investments to long-term investments.

Days in cash increased from 118 days as of June 30, 2009 to 123 days as of June 30, 2010 for the Primary Health System. Days in net accounts receivable increased from 54 days as of June 30, 2009 to 57 days as of June 30, 2010. The Primary Health System recognized \$7.4 million in essential access payments from the State of Tennessee in fiscal year 2010 compared to \$6.1 million in fiscal year 2009. Additionally, the Primary Health System recognized and received \$2.9 million in disproportionate share payments in fiscal year 2010 from the State of Tennessee compared to \$4.9 million in fiscal year 2009. The Primary Health System recognized \$1.3 million in trauma funding in fiscal year 2010 compared to \$2.3 million in fiscal year 2009.

Capital assets for the Primary Health System were \$162 million. Additions for the fiscal year 2010 amounted to \$16.9 million while \$7 million of assets were retired. Depreciation expense was \$27 million for the Primary Health System. Retirement of assets reduced accumulated depreciation by \$7 million in fiscal year 2010. Construction in progress was \$6 million as of June 30, 2009 and \$8 million as of June 30, 2010. Included in construction in progress at June 30, 2009 and 2010 is the Erlanger East expansion of \$3 million.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis - Continued*

*Years Ended June 30, 2010 and 2009*

NET ASSETS - Continued

Property, Plant and Equipment at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Land and improvements	\$ 27	\$ 27
Buildings	239	238
Equipment	347	340
Total	613	605
Less accumulated depreciation	(459)	(439)
Construction in progress	8	6
Net property, plant and equipment	<u>\$ 162</u>	<u>\$ 172</u>

Long-term debt outstanding amounted to \$183 million as of June 30, 2010 compared to \$189 million as of June 30, 2009. The decrease in long-term debt primarily reflects normal scheduled principal payments.

Other liabilities for the Primary Health System increased 10 percent from the prior fiscal year primarily due to increases in accounts payables, accrued salary related expenses, and estimated amounts due to third party payors.

CHANGES IN NET ASSETS

The focus for Erlanger Health System's management team during fiscal year 2010 was to maintain the Primary Health System's volumes in a number of key product lines in a downturned economy, improve relationships with stakeholders, grow the employed physician practices, and improve operating efficiencies. Staffing was benchmarked by department against best practices. Bi-weekly sessions were held to monitor the flexing of staff as volumes fluctuated. Renegotiated contracts continued to result in supply and purchased service savings for the System.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis - Continued*

*Years Ended June 30, 2010 and 2009*

CHANGES IN NET ASSETS - Continued

**Table 2 - Changes in Net Assets (in Millions)**

	<i>June 30, 2010</i>			<i>June 30, 2009</i>		
	<i>Primary Health System</i>	<i>ContinuCare Health Services, Inc.</i>	<i>Plaza Surgery, G.P.</i>	<i>Primary Health System</i>	<i>ContinuCare Health Services, Inc.</i>	<i>Plaza Surgery, G.P.</i>
Net patient revenue	\$ 473	\$ 10	\$ 5	\$ 463	\$ 9	\$ 5
Other revenue	20	16	-	18	17	-
Total revenue	493	26	5	481	26	5
Expenses:						
Salaries	264	12	2	255	11	2
Supplies and expenses	103	15	3	103	16	3
Purchased services	85	-	-	78	-	-
Insurance and taxes	5	-	-	4	-	-
Depreciation and amortization	27	-	-	29	-	-
Impairment of goodwill	-	-	7	-	-	-
Total expenses	484	27	12	469	27	5
Operating income revenues in excess of (less than) expenses	9	(1)	(7)	12	(1)	-
Nonoperating gains	5	-	-	6	-	-
Interest expense and other	(9)	-	-	(14)	-	-
Operating/capital contributions	-	-	(1)	1	-	(1)
Change in net assets	\$ 5	\$ (1)	\$ (8)	\$ 5	\$ (1)	\$ (1)

Net patient service revenue for the Primary Health System increased from \$463 million in fiscal year 2009 to \$473 million in fiscal year 2010. Admissions were 1.4 percent under fiscal year 2009. Surgical inpatients were 3.7% over fiscal year 2009. Surgical outpatients were 3.2% over fiscal year 2009 also. Births and emergency room visits exceeded fiscal year 2009 amounts by 2.4% and 2.8%, respectively.

Salaries for the Primary Health System increased from \$255 million in fiscal year 2009 to \$264 million in fiscal year 2010 due primarily to a 3% cost of living adjustment for all employees.

Supplies and expenses were \$103 million in fiscal year 2009 and fiscal year 2010. Management continues to standardize and renegotiate supply contracts.

Purchased services increased from \$78 million in fiscal year 2009 to \$85 million in fiscal year 2010. A new advertising campaign was rolled out in fiscal year 2010. Billing and collection fees increased as a result of growth in employed physician practices. Consulting fees increased in fiscal year 2010 resulting from continued efforts in compliance monitoring.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Management's Discussion and Analysis - Continued*

*Years Ended June 30, 2010 and 2009*

---

CHANGES IN NET ASSETS - Continued

Insurance and taxes increased from \$4 million in fiscal year 2009 to \$5 million in fiscal year 2010. The increase is due to an increase in malpractice insurance resulting from growth in employed physicians.

Depreciation and amortization expense decreased from \$29 million in fiscal year 2009 to \$27 million in fiscal year 2010 due to decreased capital spending.

Interest expense, including loss on mark-to-market of interest rate swaps, decreased from \$14 million in fiscal year 2009 to \$10 million in fiscal year 2010. The final payment of the 1993 Series Bonds was made October 1, 2009. During the year ended June 30, 2010, the Primary Health System remarketed previously issued debt of approximately \$39,800,000 and \$85,000,000 as it relates to the Series 2000 and Series 2004 Hospital Revenue Refunding Bonds, respectively, and converted such bonds from a variable auction rate to a fixed rate.

OUTLOOK

The State of Tennessee continues to review the TennCare program (the State's Medicaid program). For fiscal year 2011, the State passed a Hospital Coverage Fee to offset shortfalls in the State's budget for TennCare. Although not permanent, the fee would be renewed annually. Changes in the Medicaid program in the State of Georgia would also impact the Primary Health System. TennCare and Medicaid patients represent approximately 25% of the payor mix. Self Pay patients represent approximately 10.4% of the charge utilization. Healthcare reform and future changes in Medicare regulations could also have an adverse effect on the Primary Health System's future operations since Medicare represents approximately 27% of the payor mix.

Disproportionate share and trauma fund payments from the State of Tennessee to the Primary Health System were recognized and received in fiscal year 2010. Additional disproportionate share payments for fiscal year 2011 as well as trauma fund payments are expected to be approved and paid by the State of Tennessee during fiscal year 2011.

*Audited Combined Financial Statements*

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

***Combined Balance Sheets***

	<i>June 30, 2010</i>		
	<i>Primary</i>	<i>Component Units</i>	
		<i>Health</i>	<i>ContinuCare</i>
	<i>System</i>	<i>Health</i>	<i>Surgery,</i>
		<i>Services, Inc.</i>	<i>G.P.</i>
<b>ASSETS</b>			
<b>CURRENT ASSETS:</b>			
Cash and cash equivalents	\$ 60,357,225	\$ 1,938,757	\$ 323,360
Temporary investments	12,980,160	5,605,984	-
Assets limited as to use available for current liabilities	5,502,561	-	-
Patient accounts receivable, net	74,477,551	1,817,477	685,206
Due from other governments, net	167,114	273,832	-
Inventories	10,294,860	1,183,548	466,071
Other current assets	11,611,084	580,848	6,697
TOTAL CURRENT ASSETS	175,390,555	11,400,446	1,481,334
NET PROPERTY, PLANT AND EQUIPMENT	162,479,387	1,824,458	90,023
LONG-TERM INVESTMENTS	17,297,663	-	-
ASSETS LIMITED AS TO USE	137,836,728	-	-
<b>OTHER ASSETS:</b>			
Deferred financing costs	7,536,619	-	-
Other assets	-	1,342,963	12,820
TOTAL OTHER ASSETS	7,536,619	1,342,963	12,820
TOTAL ASSETS	\$ 500,540,952	\$ 14,567,867	\$ 1,584,177
<b>LIABILITIES AND NET ASSETS</b>			
<b>CURRENT LIABILITIES:</b>			
Accounts payable and accrued expenses	\$ 33,514,393	\$ 368,593	\$ 134,749
Accrued salaries and related liabilities	26,675,137	1,472,734	177,774
Estimated amounts due to third party payors	6,201,725	93,625	-
Due to other governments	273,832	167,114	-
Current portion of long-term debt and capital lease obligations	7,820,568	-	25,500
Other current liabilities	2,345,544	-	6,200
TOTAL CURRENT LIABILITIES	76,831,199	2,102,066	344,223
LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS	183,291,459	-	48,731
OTHER LONG-TERM LIABILITIES	36,435,944	-	-
<b>NET ASSETS:</b>			
Unrestricted	196,605,845	10,641,343	1,162,611
Invested in capital assets, net of related debt	5,101,777	1,824,458	28,612
Restricted expendable	2,274,728	-	-
TOTAL NET ASSETS	203,982,350	12,465,801	1,191,223
TOTAL LIABILITIES AND NET ASSETS	\$ 500,540,952	\$ 14,567,867	\$ 1,584,177

	<i>June 30, 2009</i>		
	<i>Primary Health System</i>	<i>Component Units</i>	
		<i>ContinuCare Health Services, Inc.</i>	<i>Plaza Surgery, G.P.</i>
<b>ASSETS</b>			
<b>CURRENT ASSETS:</b>			
Cash and cash equivalents	\$ 56,168,170	\$ 1,238,694	\$ 475,189
Temporary investments	23,345,647	6,149,011	-
Assets limited as to use available for current liabilities	6,089	-	-
Patient accounts receivable, net	68,946,556	2,079,921	749,208
Estimated amounts due from third party payors, net	271,327	-	-
Due from other governments, net	43,770	215,412	-
Inventories	10,129,929	1,227,782	456,931
Other current assets	11,544,078	621,203	4,613
TOTAL CURRENT ASSETS	170,455,566	11,532,023	1,685,941
NET PROPERTY, PLANT AND EQUIPMENT	172,343,908	1,888,444	17,916
ASSETS LIMITED AS TO USE	141,729,089	-	-
<b>OTHER ASSETS:</b>			
Deferred financing costs	6,407,312	-	-
Other assets	-	1,155,963	7,414,883
TOTAL OTHER ASSETS	6,407,312	1,155,963	7,414,883
TOTAL ASSETS	<u>\$ 490,935,875</u>	<u>\$ 14,576,430</u>	<u>\$ 9,118,740</u>
<b>LIABILITIES AND NET ASSETS</b>			
<b>CURRENT LIABILITIES:</b>			
Accounts payable and accrued expenses	\$ 30,538,549	\$ 724,268	\$ 214,504
Accrued salaries and related liabilities	23,498,360	1,014,852	191,303
Estimated amounts due to third party payors	-	93,625	-
Due to other governments	215,412	43,770	-
Current portion of long-term debt and capital lease obligations	12,336,040	-	-
Other current liabilities	1,000,135	-	11,829
TOTAL CURRENT LIABILITIES	67,588,496	1,876,515	417,636
LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS	188,662,257	-	-
OTHER LONG-TERM LIABILITIES	35,314,522	-	-
<b>NET ASSETS:</b>			
Unrestricted	190,231,539	10,811,471	1,268,305
Invested in capital assets, net of related debt	6,613,725	1,888,444	7,432,799
Restricted expendable	2,525,336	-	-
TOTAL NET ASSETS	199,370,600	12,699,915	8,701,104
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 490,935,875</u>	<u>\$ 14,576,430</u>	<u>\$ 9,118,740</u>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

***Combined Statements of Revenue, Expenses and Changes in Net Assets***

	<i>Year Ended June 30, 2010</i>		
	<i>Component Units</i>		
	<i>Primary Health System</i>	<i>ContinuCare Health Services, Inc.</i>	<i>Plaza Surgery, G.P.</i>
<b>OPERATING REVENUE:</b>			
Charges for services:			
Net patient service revenue, net	\$ 472,827,645	\$ 10,308,382	\$ 5,136,023
Other revenue	20,604,836	15,988,639	99
<b>TOTAL OPERATING REVENUE</b>	<b>493,432,481</b>	<b>26,297,021</b>	<b>5,136,122</b>
<b>OPERATING EXPENSES:</b>			
Salaries, wages and benefits	264,297,673	11,617,831	1,993,551
Supplies and other expenses	103,356,407	15,072,538	2,704,741
Purchased services	85,238,650	-	386,453
Insurance and taxes	4,603,860	-	67,380
Depreciation	26,576,824	368,968	11,622
Impairment of goodwill	-	-	7,402,063
<b>TOTAL OPERATING EXPENSES</b>	<b>484,073,414</b>	<b>27,059,337</b>	<b>12,565,810</b>
<b>OPERATING INCOME (LOSS)</b>	<b>9,359,067</b>	<b>(762,316)</b>	<b>(7,429,688)</b>
<b>NONOPERATING REVENUE (EXPENSES):</b>			
Gain (loss) on disposal of assets	28,704	(13,346)	-
Interest and investment income	5,267,434	351,047	-
Interest expense	(8,782,300)	-	(193)
Benefit from income taxes	-	190,501	-
Loss on mark-to-market of interest rate swaps	(1,317,375)	-	-
<b>NET NONOPERATING REVENUE (EXPENSES)</b>	<b>(4,803,537)</b>	<b>528,202</b>	<b>(193)</b>
Income (loss) before contributions	4,555,530	(234,114)	(7,429,881)
Operating distributions	(232,318)	-	(80,000)
Capital contributions/other, net	288,538	-	-
<b>CHANGE IN NET ASSETS</b>	<b>4,611,750</b>	<b>(234,114)</b>	<b>(7,509,881)</b>
<b>NET ASSETS AT BEGINNING OF YEAR</b>	<b>199,370,600</b>	<b>12,699,915</b>	<b>8,701,104</b>
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ 203,982,350</b>	<b>\$ 12,465,801</b>	<b>\$ 1,191,223</b>

	<i>Year Ended June 30, 2009</i>		
	<i>Primary Health System</i>	<i>Component Units</i>	
		<i>ContinuCare Health Services, Inc.</i>	<i>Plaza Surgery, G.P.</i>
<b>OPERATING REVENUE:</b>			
Charges for services:			
Net patient service revenue	\$ 462,847,750	\$ 9,322,563	\$ 5,358,337
Other revenue	17,858,380	16,809,232	996
<b>TOTAL OPERATING REVENUE</b>	<b>480,706,130</b>	<b>26,131,795</b>	<b>5,359,333</b>
<b>OPERATING EXPENSES:</b>			
Salaries, wages and benefits	254,782,353	10,664,331	2,162,660
Supplies and other expenses	102,940,577	16,380,358	2,724,088
Purchased services	77,611,213	-	515,435
Insurance and taxes	4,121,625	-	102,285
Depreciation	29,171,048	312,271	11,820
<b>TOTAL OPERATING EXPENSES</b>	<b>468,626,816</b>	<b>27,356,960</b>	<b>5,516,288</b>
<b>OPERATING INCOME (LOSS)</b>	<b>12,079,314</b>	<b>(1,225,165)</b>	<b>(156,955)</b>
<b>NONOPERATING REVENUE (EXPENSES):</b>			
Gain (loss) on disposal of assets	(259,755)	5,424	-
Interest and investment income	6,430,842	106,388	-
Interest expense	(10,070,931)	(676)	(5,832)
Benefit from income taxes	-	394,241	-
Loss on mark-to-market of interest rate swaps	(4,227,607)	-	-
<b>NET NONOPERATING REVENUE (EXPENSES)</b>	<b>(8,127,451)</b>	<b>505,377</b>	<b>(5,832)</b>
Income (loss) before contributions	3,951,863	(719,788)	(162,787)
Operating contributions (distributions)	469,894	-	(550,000)
Capital contributions/other, net	790,722	-	-
<b>CHANGE IN NET ASSETS</b>	<b>5,212,479</b>	<b>(719,788)</b>	<b>(712,787)</b>
<b>NET ASSETS AT BEGINNING OF YEAR</b>	<b>194,158,121</b>	<b>13,419,703</b>	<b>9,413,891</b>
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ 199,370,600</b>	<b>\$ 12,699,915</b>	<b>\$ 8,701,104</b>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

***Combined Statements of Cash Flows***

	<i>Primary Health System</i>	
	<i>Year Ended June 30,</i>	
	<i>2010</i>	<i>2009</i>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Receipts from third-party payors and patients	<b>\$ 471,093,116</b>	\$ 475,653,444
Payments to vendors and others for supplies, purchased services, and other expenses	<b>(188,222,421)</b>	(190,536,148)
Payments to and on behalf of employees	<b>(261,008,064)</b>	(252,624,385)
Other receipts	<b>20,722,480</b>	17,638,770
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>42,585,111</b>	50,131,681
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>		
Contributions (distributions)	<b>(232,318)</b>	469,894
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Acquisition and construction of capital assets, net	<b>(16,933,037)</b>	(12,528,389)
Principal paid on bonds, capital lease obligations and other	<b>(12,356,219)</b>	(11,603,179)
Proceeds from sale of assets	<b>249,438</b>	574,149
Interest payments on long-term debt	<b>(8,455,247)</b>	(9,248,093)
Premium on remarketing of bonds	<b>2,311,642</b>	-
Capital contributions/other, net	<b>288,538</b>	790,722
<b>NET CASH USED IN CAPITAL AND RELATED FINANCING ACTIVITIES</b>	<b>(34,894,885)</b>	(32,014,790)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Interest, dividends, and net realized gains on investments	<b>3,191,580</b>	5,148,229
Purchases of investments, net	<b>(4,856,322)</b>	(21,265,711)
Cash used by assets limited as to use	<b>(1,604,111)</b>	(6,791,614)
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(3,268,853)</b>	(22,909,096)
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>4,189,055</b>	(4,322,311)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<b>56,168,170</b>	60,490,481
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ 60,357,225</b>	\$ 56,168,170

	<i>Primary Health System</i>	
	<i>Year Ended June 30,</i>	
	<i>2010</i>	<i>2009</i>
<b>RECONCILIATION OF OPERATING INCOME</b>		
<b>TO NET CASH PROVIDED BY OPERATING</b>		
<b>ACTIVITIES:</b>		
Operating income	\$ 9,359,067	\$ 12,079,314
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	26,576,824	29,171,048
Provision for self-insurance	1,686,121	1,805,432
Changes in assets and liabilities:		
Patient accounts receivable, net	(5,530,995)	11,769,192
Estimated amounts due from (due to) third party payors, net	6,473,052	1,397,961
Inventories and other current assets	(355,281)	(2,443,432)
Other long-term assets	-	31,348
Accounts payable and accrued expenses	1,658,469	(8,162,040)
Accrued salaries and related liabilities	3,176,777	1,290,109
Other current and long-term liabilities	(458,923)	3,192,749
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>\$ 42,585,111</b>	<b>\$ 50,131,681</b>

**SUPPLEMENTAL INFORMATION:**

During the year ended June 30, 2010, the Primary Health System remarketed previously issued debt of approximately \$39,800,000 and \$85,000,000 as it relates to the Series 2000 and Series 2004 Hospital Revenue Refunding Bonds, respectively (see Note G).

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY  
(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements*

*Years Ended June 30, 2010 and 2009*

---

**NOTE A--SIGNIFICANT ACCOUNTING POLICIES**

*Reporting Entity:* The Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) was created by a private act passed by the General Assembly of the State of Tennessee on March 11, 1976, and adopted by a majority of the qualified voters of Hamilton County, Tennessee on August 5, 1976. The Chattanooga-Hamilton County Hospital Authority consists of the Primary Health System and its discretely presented component units as disclosed below.

The Primary Health System provides comprehensive healthcare services throughout Hamilton and Bledsoe counties, as well as outlying areas in southeastern Tennessee and north Georgia. These services are provided primarily through the hospital and other facilities located on the Baroness campus of Erlanger Medical Center. The Primary Health System also operates other hospitals and clinics throughout the area. The Primary Health System is considered the primary governmental unit for financial reporting purposes. As required by accounting principles generally accepted in the United States of America, these combined financial statements present the Primary Health System and its component units. The component units discussed below are included in the Primary Health System's reporting entity because of the significance of their operational or financial relationships with the Primary Health System.

The primary mission of the Primary Health System and its component units is to provide healthcare services to the citizens of Chattanooga, Hamilton County and the surrounding area. Only those activities directly associated with this purpose are considered to be operating activities. Other activities that result in gains or losses unrelated to the Primary Health System's primary mission are considered to be nonoperating.

ContinuCare HealthServices, Inc., Plaza Surgery, G.P., and Erlanger Health Plan Trust are legally separate organizations for which the Primary Health System is financially accountable. Accordingly, these organizations represent component units of the Primary Health System.

*Blended Component Unit:* The financial statements of Erlanger Health Plan Trust are blended with the Primary Health System in the basic combined financial statements as the board of Erlanger Health Plan Trust is substantially the same as that of the Primary Health System.

*Discretely Presented Component Units:* The component unit columns in the basic combined financial statements include the financial data of the Primary Health System's other component units. They are reported in separate columns to emphasize that they are legally separate from the Primary Health System.

1. ContinuCare HealthServices, Inc. and subsidiary (ContinuCare) provide health and supportive services to individuals in their homes in the Hamilton County and north

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

Georgia areas. ContinuCare also provides retail pharmacy goods and services at four locations in Hamilton County. The Primary Health System owns 100% of the stock of ContinuCare. Separately audited financial statements for ContinuCare HealthServices, Inc. may be obtained by mailing a request to 1501 Riverside Drive, Suite 140, Chattanooga, Tennessee 37406.

As a for-profit entity, ContinuCare is subject to state and federal income taxes. ContinuCare HealthServices, Inc. and its subsidiary file consolidated federal income tax returns separately from the Primary Health System.

ContinuCare owes the Primary Health System for various services, supplies, and rents provided to, or expenses paid on its behalf. Actual expenses incurred were \$1,323,045 and \$423,299 in 2010 and 2009, respectively. In addition, ContinuCare provides staffing, contract nurse visits, and administrative services to the Primary Health System. Such revenues were \$298,610 and \$215,766 in 2010 and 2009, respectively. Amounts due at June 30, 2010 and 2009 are included in amounts due to/from other governments in the accompanying combined financial statements.

The Primary Health System charged approximately \$33,000 in management services to ContinuCare for each of the fiscal years ending June 30, 2010 and 2009.

2. Plaza Surgery, G.P. (the Partnership) operates an ambulatory surgery center on the Primary Health System's campus. At June 30, 2010 and 2009, the Primary Health System owns a controlling 51% of the Partnership. As a general partnership, general partners are jointly and separately liable for the debts of the Partnership. Accordingly, the Partnership is fiscally dependent on the Primary Health System.

Effective September 1, 2001, Plaza Surgery, G.P. was capitalized by the contribution by the Primary Health System of cash of \$566,000 and the going concern value (i.e., goodwill) of Plaza Ambulatory Surgery Center (valued at \$7,402,000 by an appraisal agreed to by all of the general partners) and the contribution of cash from certain minority partners of \$3,369,000. Concurrent with the capitalization of the Partnership, and execution of an Asset Transfer Agreement, the Partnership distributed cash of \$2,935,000 to the Primary Health System such that the partners' capital of the Primary Health System and the minority partners after the distribution were in accordance with the Amended and Restated Partnership Agreement. The distribution of cash from the Partnership has been reflected in other long-term liabilities of the Primary Health System in the accompanying combined financial statements as a result of certain put and call rights that the minority partners had with respect to the Partnership. Upon the

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

expiration of the put and call rights at August 31, 2003, the Primary Health System began amortizing this amount to income over the remaining term of the lease agreement associated with the Asset Transfer Agreement. Such amortization totaled \$163,034 in both 2010 and 2009, and is reflected within other revenue in the accompanying combined statements of revenue, expenses and changes in net assets.

The total value of assets contributed by all general partners was approximately \$8,402,000 and was included as other assets for the component unit, Plaza Surgery, G.P., in the accompanying combined balance sheets. During 2010, due to a change in circumstances, goodwill was reviewed for possible impairment. Management has determined that goodwill was impaired, and an impairment loss of approximately \$7,402,000 is included as an operating expense for the component unit, Plaza Surgery, G.P., in the accompanying combined statements of revenue, expenses and changes in net assets.

Income from the Partnership is allocated to general partners based on ownership percentages and taxed at the partner level based upon the tax status of the partner. The portion of income allocated to the Primary Health System is exempt from income taxes based on the Primary Health System's tax-exempt status.

*Use of Estimates:* The preparation of the combined 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 as of the date of the combined financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

*Enterprise Fund Accounting:* The Primary Health System and its blended component unit utilize the enterprise fund method of accounting whereby revenue and expenses are recognized on the accrual basis using the economic resources measurement focus. Pursuant to the 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 Primary Health System 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.

*Recently Issued or Effective Accounting Pronouncements:* In June 2009, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles (GAAP) - a Replacement of FASB Statement No. 162*. This Statement modifies the GAAP hierarchy by establishing only two levels of GAAP, authoritative and nonauthoritative accounting literature.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

Effective September 2009, the FASB Accounting Standards Codification (ASC), also known collectively as the "Codification," is considered the single source of authoritative U.S. accounting and reporting standards, except for authoritative pronouncements, rules and interpretive releases issued by the GASB if the organization is a governmental entity. FASB ASC 105-10, *Generally Accepted Accounting Principles*, became applicable during fiscal year 2010. All accounting references have been updated, and therefore SFAS references have been replaced with ASC references.

In March 2009, the GASB issued Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards (the GASB Codification)*. This Statement became effective upon issuance and addresses three issues not included in the authoritative literature that establishes accounting principles - related party transactions, going concern considerations, and subsequent events. This Statement does not establish new accounting standards but rather incorporates the existing guidance (to the extent appropriate in a governmental environment) into the GASB standards. The Primary Health System evaluated related party transactions and determined that they are in compliance with all accounting and financial reporting standards. In addition, there are no substantial doubts regarding the Primary Health System's ability to continue as a going concern. This Statement establishes general standards of accounting for, and disclosure of, events that occur after the balance sheet date but before financial statements are issued. The Primary Health System evaluated all events or transactions that occurred after June 30, 2010, through November 8, 2010, the issuance date of the combined financial statements. During this period, management did not note any material recognizable subsequent events that required recognition or disclosure in the June 30, 2010 combined financial statements.

In November 2006, the GASB issued Statement No. 49, *Accounting and Financial Reporting of Pollution Remediation Obligations*. This Statement provides guidance with respect to evaluating the obligations related to the participation in pollution remediation activities, such as site cleanup, related to existing pollution. The scope of the Statement excludes pollution prevention or control obligations with respect to current operations and future pollution remediation activities that are required upon retirement of an asset. The requirements of this Statement were adopted by the Primary Health System in fiscal year 2009 and the adoption did not have a material impact on the combined financial statements.

In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This Statement is effective for years beginning after June 15, 2009 and provides guidance on amortization of certain intangible assets and provides guidance on financial statement recognition of intangible assets, including internally developed software. The provisions of this Statement generally are required to be applied retroactively. The requirements

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

of this Statement were adopted by the Primary Health System in fiscal year 2010 and the adoption did not have a material impact on the combined financial statements.

In June 2008, the GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This Statement is effective for years beginning after June 15, 2009 and provides guidance on how governmental entities report information about derivative instruments and other new accounting requirements. The Statement specifically requires governments to measure most derivative instruments at fair value in their financial statements that are prepared using the economic resources measurement focus and the accrual basis of accounting. The requirements of this Statement were adopted by the Primary Health System in fiscal year 2010 and the adoption did not have a material impact on the combined financial statements.

In March 2009, the GASB issued Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This Statement is effective upon issuance and incorporates the hierarchy of GAAP for state and local governments into the GASB's authoritative literature. The requirements in this Statement will improve financial reporting by contributing to the GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source. The adoption of this Statement did not have a material impact on the combined financial statements.

In June 2010, the GASB issued Statement No. 59, *Financial Instruments Omnibus*. The Statement is effective for years beginning after June 15, 2010 and updates current standards regarding the financial reporting of financial instruments and external investment pools. The requirements of this Statement will improve financial reporting by providing more complete information, by improving consistency of measurements, and by providing clarifications of existing standards. Management of the Primary Health System is evaluating the impact of this Statement on the combined financial statements but does not anticipate any material impact upon adoption.

The Primary Health System adopted the applicable portions of FASB ASC 820, *Fair Value Measurements and Disclosures* (FASB ASC 820), during fiscal year 2009. FASB ASC 820 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and expands disclosures about fair value measurements. FASB ASC 820 applies only to fair value measurements that are already required, or permitted, by other accounting standards. There was no significant impact on the combined financial statements from adopting this standard (Note O).

In August 2009, FASB issued Accounting Standard Update 2009-05, *Measuring Liabilities at Fair Value*, as it relates to FASB ASC 820. This Update provides clarifications of alternative

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY  
(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

techniques to measure fair value in which a quoted price in an active market for the identical liability is not available. The guidance provided in this Update is effective for the first reporting period beginning after issuance. Management of the Primary Health System is evaluating the impact of this Update on the combined financial statements but does not anticipate any material impact upon adoption.

In January 2010, FASB issued Accounting Standard Update 2010-06, *Improving Disclosures about Fair Value Measurements*, as it relates to FASB ASC 820. This Update provides amendments to FASB ASC 820 that requires both new disclosures and further clarifies existing disclosures. This Update also includes conforming amendments to the guidance on employers' disclosures about postretirement benefit plan assets, FASB ASC 715, *Compensation - Retirement Benefits*. This Update is effective for years beginning after December 15, 2009, except for disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements, which is effective for years beginning after December 15, 2010. Management of the Primary Health System is evaluating the impact of this Update on the combined financial statements but does not anticipate any material impact upon adoption.

*Net Patient Service Revenue/Receivables:* Net patient service revenue is reported on the accrual basis in the period in which services are provided at rates which reflect the amount expected to be collected. Net patient service revenue includes amounts estimated by management to be reimbursable by third-party payor programs under payment formulas in effect. Net patient revenue also includes an estimated provision for bad debts based upon management's evaluation of collectability based upon the age of the receivables and other criteria, such as payor classification and management's assumptions about conditions it expects to exist and courses of action it expects to take. The Primary Health System's policies do not require collateral or other security for accounts receivable, although the Primary Health System routinely accepts assignment or is otherwise entitled to receive patient benefits payable under health insurance programs, plans or policies. Supplemental payments from the State of Tennessee are recognized when determinable (Note B).

*Charity Care:* The Primary Health System accepts patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain policies established by the County Auditor with regard to the Hamilton County indigent program or by the Primary Health System for other patients. Essentially, these policies define charity services as those services for which minimal payment is anticipated. In assessing a patient's inability to pay, the County and the Primary Health System utilize the generally recognized poverty income levels, but also include certain cases where incurred charges are significant when compared to the income of the patient. These charges are not included in net patient service revenue.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

*Inventories:* Inventories consist principally of medical and surgical supplies, general store supplies, and pharmacy items and are stated at lower of cost (first-in, first-out) or fair market value.

*Cash Equivalents:* The Primary Health System considers all highly liquid investments with maturities of three months or less when purchased, excluding amounts whose use is limited by board designation, held by trustees under indenture agreement, or otherwise restricted as to use, to be cash equivalents.

*Investments:* The Primary Health System's investments (including assets limited as to use) are reported at fair market value based on quoted market prices in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Assets limited as to use include funds designated by the Board for capital improvements, funds held by trustees under trust indentures, and funds restricted by donors or grantors for specific purposes. The Primary Health System considers those investments with maturities of 12 months or more when purchased and whose use is not limited by board designation, held by trustees under indenture agreement, or otherwise restricted as to use, to be long-term investments. Investments, including assets limited as to use, consist of United States government and municipal bonds, corporate debt and other short-term investments.

*Temporary Investments:* The Primary Health System considers all highly liquid investments with maturities of more than 3 months when purchased and maturing in less than one year excluding amounts whose use is limited by board designation, held by trustees under indenture agreement, or otherwise restricted as to use, to be temporary investments. Temporary investments consist primarily of bank certificates of deposit.

*Derivative Instruments:* The Primary Health System records all derivatives as assets or liabilities on the combined balance sheets at estimated fair value and includes credit value adjustments. The Primary Health System's derivative holdings consist of interest rate swap agreements. Since these derivatives are not designated as hedging instruments, mark-to-market accounting applies, and the gain or loss resulting from changes in the fair value of the derivatives is recognized in the accompanying combined statements of revenue, expenses and changes in net assets. The Primary Health System's objectives in using derivatives are to take advantage of the differences between taxable and tax-exempt debt, the timing of long-term versus short-term rates, and to manage the mix of fixed versus variable rate debt.

*Net Property, Plant and Equipment:* Property, plant and equipment are recorded on the basis of cost. Donated assets are recorded at their fair market value at the date of donation. Leases that are substantially installment purchases of property are recorded as assets and amortized over

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

their estimated useful lives ranging from three to thirty years; related amortization is included in depreciation expense. Depreciation expense is computed over estimated service lives of the respective classes of assets using the straight-line method. The Primary Health System has established a capitalization threshold for property, plant and equipment of \$2,500 except for computer equipment, which has a threshold of \$1,000. Interest expense and interest income on borrowed funds related to construction projects are capitalized during the construction period, if material. Costs of maintenance and repairs are charged to expense as incurred.

The Primary Health System previously adopted the provisions of GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This Statement also clarifies and establishes accounting requirements for insurance recoveries. The Primary Health System did not experience any prominent events or changes in circumstances affecting capital assets which would require determination as to whether impairment of a capital asset has occurred during the years ended June 30, 2010 and 2009.

*Compensated Absences:* The Primary Health System recognizes an expense and accrues a liability for employees' paid annual leave and extended illness benefits in the period in which the employees' right to such compensated absences are earned. Liabilities expected to be paid within one year are included as accrued salaries and related liabilities in the accompanying combined financial statements.

*Deferred Financing Costs:* Deferred financing costs consist principally of costs associated with bond issues and are being amortized, generally, over the terms of the respective debt issues by the effective interest method.

*Income Taxes:* The Primary Health System is exempt from income taxes under Section 501(a) as an organization described in Section 501(c)(3) of the Internal Revenue Code (IRC). In addition, it qualifies for exemption from federal income taxes pursuant to IRC Section 115 as an instrumentality of the State of Tennessee. Therefore, no provision for income taxes has been recognized in the accompanying combined financial statements for the Primary Health System.

*Contributed Resources:* Resources restricted by donors for specific operating purposes are held as restricted funds until expended for the intended purpose, at which time they are reported as other operating revenue. Contributed resources consist of amounts restricted by donors for specific purposes.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE A--SIGNIFICANT ACCOUNTING POLICIES - Continued

*Net Assets:* Net assets of the Primary Health System are classified in three components. *Net assets invested in capital assets, net of related debt* consist of capital and other 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. *Restricted expendable* net assets are net assets that must be used for a particular purpose that are either externally imposed by creditors, grantors, contributors or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. *Unrestricted* net assets are remaining net assets that do not meet the definition of *invested in capital assets, net of related debt* or *restricted, expendable*.

*Fair Value of Financial Instruments:* The carrying amounts reported in the combined balance sheets for cash, accounts receivable, investments and accounts payable approximate fair value.

The carrying value of long-term debt and capital lease obligations (including the current portion) was \$191,112,027 as of June 30, 2010 and \$200,998,297 as of June 30, 2009. The estimated fair value of long-term debt and capital lease obligations (including current portion) was \$195,421,000 and \$202,094,782 as of June 30, 2010 and 2009, respectively. The fair value of long-term debt related to fixed interest long-term debt and capital lease obligations was estimated using discounted cash flows, based on the Primary Health System's incremental borrowing rates. The fair value of long-term debt related to variable rate debt approximates its carrying value.

*Reclassifications:* Certain reclassifications have been made to the 2009 combined financial statements to conform with the 2010 combined financial statements presentation.

NOTE B--NET PATIENT SERVICE REVENUE

A reconciliation of the amount of services provided to patients at established rates by the Primary Health System to net patient service revenue as presented in the combined statements of revenue, expenses and changes in net assets for the years ended June 30, 2010 and 2009 is as follows:

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE B--NET PATIENT SERVICE REVENUE - Continued

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Inpatient service charges	\$ 900,322,856	\$ 889,686,982
Outpatient service charges	564,901,041	510,404,150
Gross patient service charges	1,465,223,897	1,400,091,132
Less: Contractual adjustments and other discounts	831,193,082	800,675,611
Charity care	75,997,351	63,978,500
Estimated provision for bad debts	85,205,819	72,589,271
	<u>992,396,252</u>	<u>937,243,382</u>
Net patient service revenue	<u>\$ 472,827,645</u>	<u>\$ 462,847,750</u>

*Charity Care and Community Benefit:* The Private Act of the State of Tennessee establishing the Primary Health System obligates the Primary Health System to make its facilities and patient care programs available to the indigent residents of Hamilton County to the extent of funds appropriated by Hamilton County and adjusted operating profits, as defined. The annual appropriation from Hamilton County is not to be less than \$3,000,000 in each fiscal year without approval of the Primary Health System, so long as the 1966 Hamilton County Sales Tax Agreement remains in effect. Total charity care charges for services provided to the certified indigent residents of Hamilton County (net of the appropriation of \$3,000,000 each year) were approximately \$21,414,000 and \$17,414,000 for the years ended June 30, 2010 and 2009 for the Primary Health System.

In addition to charity care provided to specific patients within the hospital setting, the Primary Health System also provides unreimbursed services to the community which includes free and low cost health screenings. The Primary Health System also hosts health fairs and helps sponsor many other events that are free to the public and are spread throughout the year in various community locations. The Primary Health System also places advertisements entitled "Health News" in the *Chattanooga Times Free Press* and sometimes in other newspapers throughout the region (the number of times per year varies). These ads are designed to educate and inform the public of health, wellness, illness and accident prevention issues.

The Primary Health System's Community Relations department, which conducts health, wellness and safety education classes and health screenings, includes Erlanger HealthLink Plus, a free adult membership program with over 17,000 members in the Chattanooga Statistical Metropolitan Service Area. The program provides over 24 classes and/or screenings and fitness opportunities per month that are free or at a low cost to members and to the community. These classes and screenings are held in two primary locations with additional classes at satellite

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

***Years Ended June 30, 2010 and 2009***

**NOTE B--NET PATIENT SERVICE REVENUE - Continued**

locations in the region. As part of Community Relations, Safe & Sound, an injury prevention service of T.C. Thompson Children’s Hospital, offers free educational events regarding childhood injury prevention, including free car seat inspection and installation workshops. The Community Relations program utilizes the services of physicians, nurses, volunteers, educators, registered dietitians, social workers, secretaries and management personnel of the Primary Health System.

The Primary Health System’s consumer call center, Erlanger HealthLink (423-778-LINK) is a free call center staffed by RN’s to answer health questions, offer free physician referrals and to register participants in the programs offered by Community Relations, Women’s & Infant Services and other departments and divisions of the Primary Health System.

*Uncompensated Care Costs (Unaudited):* The following table summarizes the total uncompensated care costs provided by Erlanger Medical Center as defined by the State of Tennessee for the years ended June 30, 2010 and 2009:

	<b><i>2010</i></b>	<b><i>2009</i></b>
Uncompensated cost of TennCare/Medicaid	\$ 28,445,920	\$ 27,464,546
Traditional charity uncompensated costs	25,802,811	22,335,524
Bad debt cost	27,925,767	24,252,673
Total uncompensated care costs	<b>\$ 82,174,498</b>	<b>\$ 74,052,743</b>

The uncompensated cost of TennCare/Medicaid is estimated by taking the estimated cost of providing care to the TennCare/Medicaid patients less payments from the TennCare and Medicaid programs. The payments exclude revenues from essential access and other, one-time supplemental payments from TennCare of approximately \$7,368,760 and \$6,093,600 for the years ended June 30, 2010 and 2009, respectively, as such payments are not guaranteed for future periods. Traditional charity uncompensated costs exclude \$3,000,000 of local government support for each of the years ended June 30, 2010 and 2009.

*Revenue from Significant Payors:* Gross patient service charges related to the Medicare program accounted for approximately 26.9% and 28.1% of the Primary Health System’s patient service charges for the years ended June 30, 2010 and 2009, respectively. Gross patient service charges related to the TennCare/Medicaid programs accounted for approximately 25.7% and 24.3% of the Primary Health System’s patient service charges for the years ending June 30, 2010 and 2009, respectively. TennCare typically reimburses providers at an amount less than their cost of providing services to TennCare patients. At June 30, 2010 and 2009, the Primary Health System

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE B--NET PATIENT SERVICE REVENUE - Continued

has a credit concentration related to the Medicare and TennCare programs. During 2010 and 2009, the Primary Health System recognized revenue related to disproportionate share payments and trauma fund payments of \$4,179,000 and \$7,224,000, respectively.

Laws and regulations governing the Medicare and TennCare/Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates, as they relate to revenue recognized from these programs, will change by a material amount in the near term. The estimated reimbursement amounts are adjusted in subsequent periods as cost reports are prepared and filed and as final settlements are determined. Final determination of amounts earned under prospective payment and cost reimbursement activities is subject to review by appropriate governmental authorities or their agents. Management believes that adequate provisions have been made for adjustments that may result from final determination of amounts earned under Medicare and Medicaid programs. Prior year cost report settlements, or changes in estimates, increased the 2009 net patient service revenue by approximately \$700,000. The effect of prior year cost report settlements, or changes in estimates, had no significant net impact on 2010 net patient service revenue.

The Primary Health System believes that it is substantially in compliance with all applicable laws and regulations and is not aware of any on-going or threatened investigations involving allegations of potential wrongdoing. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers, such as the Medicare Recovery Audit Contractor Program. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

The Primary Health System has also entered into reimbursement agreements with certain commercial insurance companies, health maintenance organizations and preferred provider organizations. The basis for reimbursement under these agreements includes prospectively determined rates, per diems and discounts from established charges.

NOTE C--CASH AND CASH EQUIVALENTS

Cash and cash equivalents reported on the combined balance sheets include cash on hand and deposits with financial institutions including demand deposits and certificates of deposit.

The carrying amount of cash and cash equivalents consists of the following at June 30:

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE C--CASH AND CASH EQUIVALENTS - Continued

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
General Fund:		
Demand deposits	\$ 30,619,460	\$ 24,705,500
Cash on hand	8,528	7,829
Cash equivalents	29,729,237	31,454,841
	<u>\$ 60,357,225</u>	<u>\$ 56,168,170</u>

Cash equivalents include certificates of deposit, money market accounts and U.S. Government agency investments and commercial paper whose maturity, when purchased, was three months or less.

Bank balances consist of the following at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Insured (FDIC)	\$ 606,096	\$ 1,226,700
Collateralized under the State of Tennessee Bank Collateral Pool	34,962,640	37,029,000
	<u>\$ 35,568,736</u>	<u>\$ 38,255,700</u>

In addition to the above bank balances, the Primary Health System held investments which met the definition of a cash equivalent and are included in cash and cash equivalents. At June 30, 2010 and 2009, amounts totaling \$25,767,085 and \$20,795,173 respectively, were invested in U.S. Government agency securities and commercial paper.

As of October 3, 2008, the Federal Deposit Insurance Corporation (FDIC) insurance limits temporarily increased from \$100,000 to \$250,000 per depositor through December 31, 2009 (as permanently extended on July 21, 2010). Additionally, the Primary Health System maintains bank balances with certain financial institutions which participate in the FDIC Transaction Account Guarantee Program. Under this program, through December 31, 2010, all non-interest bearing transaction accounts and certain interest-bearing accounts are fully guaranteed by the FDIC for the entire balance of the account.

The Primary Health System's deposits would be exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized or are collateralized with

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE C--CASH AND CASH EQUIVALENTS - Continued

securities held by the pledging financial institution's trust department or agent but not in the depositor government's name. The risk is that, in the event of the failure of a depository financial institution, the Primary Health System will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

NOTE D--DISAGGREGATION OF RECEIVABLE AND PAYABLE BALANCES

*Patient Accounts Receivable, Net:* Patient accounts receivable and related allowances are as follows at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Gross patient accounts receivable	\$ 284,697,765	\$ 266,443,262
Estimated allowances for contractual adjustments and uncollectible accounts	(210,220,214)	(197,496,706)
Net patient accounts receivable	<u>\$ 74,477,551</u>	<u>\$ 68,946,556</u>

*Other Current Assets:* Other current assets consist of the following at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Prepaid expenses	\$ 4,424,270	\$ 4,905,304
Other receivables	7,186,814	6,638,774
Total other current assets	<u>\$ 11,611,084</u>	<u>\$ 11,544,078</u>

*Accounts Payable and Accrued Expenses:* Accounts payable and accrued expenses consist of the following at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Due to vendors	\$ 32,010,826	\$ 27,137,208
Other	1,503,567	3,401,341
Total accounts payable and accrued expenses	<u>\$ 33,514,393</u>	<u>\$ 30,538,549</u>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

**NOTE D--DISAGGREGATION OF RECEIVABLE AND PAYABLE BALANCES - Continued**

*Other Long-Term Liabilities:* Other long-term liabilities consist of the following at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Pension obligation	\$ 10,653,044	\$ 10,599,874
Postretirement benefits other than pensions	1,637,602	952,271
Compensated absences	7,637,343	8,013,012
Medical malpractice and general liabilities	4,750,000	5,000,000
Other, including interest rate swaps	11,757,955	10,749,365
Total other long-term liabilities	<b>\$ 36,435,944</b>	<b>\$ 35,314,522</b>

**NOTE E--NET PROPERTY, PLANT AND EQUIPMENT**

Net property, plant and equipment activity for the Primary Health System for the years ended June 30, 2010 and 2009 consisted of the following:

	<i>Balance at June 30, 2008</i>	<i>Additions</i>	<i>Reductions/ Transfers</i>	<i>Balance at June 30, 2009</i>	<i>Additions</i>	<i>Reductions/ Transfers</i>	<i>Balance at June 30, 2010</i>
Capital assets:							
Land and improvements	\$ 27,353,507	\$ 73,985	\$ 520,000	\$ 26,907,492	\$ 55,157	\$ -	\$ 26,962,649
Buildings	236,741,392	1,533,898	3,765	238,271,525	1,148,395	-	239,419,920
Equipment	334,104,453	11,421,075	5,852,834	339,672,694	14,256,093	7,054,298	346,874,489
	598,199,352	13,028,958	6,376,599	604,851,711	15,459,645	7,054,298	613,257,058
Accumulated depreciation :							
Land and improvements	11,611,369	349,680	-	11,961,049	323,587	-	12,284,636
Buildings	151,602,383	8,435,370	3,765	160,033,988	8,290,920	-	168,324,908
Equipment	252,160,654	20,385,998	5,538,930	267,007,722	17,962,317	6,833,564	278,136,475
	415,374,406	29,171,048	5,542,695	439,002,759	26,576,824	6,833,564	458,746,019
Capital assets net of accumulated depreciation	182,824,946	(16,142,090)	833,904	165,848,952	(11,117,179)	220,734	154,511,039
Construction in progress (\$10,372,871 estimated cost to complete at June 30, 2010)	6,995,525	5,558,370	6,058,939	6,494,956	12,751,863	11,278,471	7,968,348
	<b>\$ 189,820,471</b>	<b>\$ (10,583,720)</b>	<b>\$ 6,892,843</b>	<b>\$ 172,343,908</b>	<b>\$ 1,634,684</b>	<b>\$ 11,499,205</b>	<b>\$ 162,479,387</b>

Depreciation expense totaled \$26,576,824 and \$29,171,048 for the years ended June 30, 2010 and 2009, respectively.

Construction in progress at June 30, 2010 consists of various projects for additions and renovations to the Primary Health System's facilities. The Primary Health System has outstanding contracts and other commitments related to the completion of these projects.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE E--NET PROPERTY, PLANT AND EQUIPMENT - Continued

The Primary Health System has included in net property, plant and equipment certain capital lease arrangements, including a twenty-year capital lease with Sports Barn Inc., for the operation of the Lifestyle Center (Note M).

NOTE F--INVESTMENTS AND ASSETS LIMITED AS TO USE

The Primary Health System's investments (including assets limited as to use) are reported at estimated fair value based on quoted market prices in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. The Primary Health System invests in United States government and municipal bonds and corporate debt, certificates of deposit and short-term money market investments that are in accordance with the Primary Health System's investment policy. Temporary investments at June 30, 2010 and 2009 consist primarily of certificates of deposit and United States government obligations.

The carrying and estimated fair values for long-term investments, and assets limited as to use, by type, at June 30 are as follows:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Government and municipal bonds, including bond mutual funds	\$ 138,168,062	\$ 129,931,997
Corporate bonds and commercial paper	5,794,845	3,586,797
Short-term investments and cash equivalents	16,674,045	8,216,384
Total investments	<u>\$ 160,636,952</u>	<u>\$ 141,735,178</u>

Assets limited as to use are classified as follows:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
By board of trustees for capital improvements	\$ 106,205,996	\$ 101,429,271
Under bond indentures - held by trustees	26,957,684	29,625,543
Self-insurance trust	6,767,440	7,212,782
Restricted by donors and other	3,408,169	3,467,582
	<u>143,339,289</u>	<u>141,735,178</u>
Less current portion	(5,502,561)	(6,089)
	<u>\$ 137,836,728</u>	<u>\$ 141,729,089</u>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE F--INVESTMENTS AND ASSETS LIMITED AS TO USE - Continued

Assets limited as to use by the board of trustees for capital improvements are to be used for the replacement of property and equipment or for any other purposes so designated.

Funds held by trustees under bond indenture at June 30 are as follows:

	<i>Primary Health System</i>	
	<u>2010</u>	<u>2009</u>
Construction fund	\$ 605,890	\$ 604,678
Debt service reserve funds	20,695,238	28,860,802
Principal and interest funds	5,502,561	6,089
Other funds	153,995	153,974
Total funds held by trustees under bond indenture	<u>\$ 26,957,684</u>	<u>\$ 29,625,543</u>

These funds held by trustees consist primarily of United States government and government agency obligations, municipal obligations, corporate debt, and other short-term investments and cash equivalents. The debt service reserve fund at June 30, 2010 and 2009 is to be used only to make up any deficiencies in other funds related to the Hospital Revenue and Refunding Bonds Series 1993, Series 1997A, Series 1998A, Series 2000 and Series 2004. The principal and interest funds are to be used only to pay principal and interest, respectively, on the Series 1993, Series 1997A, Series 1998A, Series 2000 and Series 2004 bonds. The final principal and interest payment for the Series 1993 bonds was made in October 2009.

The Primary Health System has implemented the disclosure requirements of GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (GASB No. 40) and, accordingly, the Primary Health System has assessed the custodial credit risk, the concentration of credit risk, credit risk, and investment rate risk of its cash and investments. The Primary Health System's investment policy specifies the types of investments which can be included in board-designated assets limited as to use, as well as collateral or other security requirements. The investment policy also specifies the maximum maturity of the portfolio of board-designated assets. Assets limited as to use and held by trustees are invested as permitted by the bond indenture.

*Custodial Credit Risk:* The Primary Health System's investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the Primary Health System, and are held by either the counterparty or the counterparty's trust department or agent but not in the Primary Health System's name. The investment risk is that, in the event of the failure of the counterparty to a transaction, the Primary Health System will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

**NOTE F--INVESTMENTS AND ASSETS LIMITED AS TO USE - Continued**

As of June 30, 2010 and 2009, the Primary Health System's investments, including assets limited as to use, were comprised of various short-term investments, U.S. government bonds, municipal obligations, corporate bonds, commercial paper, and U.S. Treasury Notes. All of the Primary Health System's investments, including assets limited as to use, are uninsured or unregistered. Securities are held by the counterparty, or by its trust department or agent, but not in the Primary Health System's name.

*Concentration of Credit Risk:* This is the risk associated with the amount of investments the Primary Health System has with any one issuer that exceeds 5% or more of its total investments. Investments issued or explicitly guaranteed by the U.S. Government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement. The Primary Health System's investment policy does not restrict the amount that may be held for any single issuer. At June 30, 2010, none of the Primary Health System's investments with any one issuer exceed 5% of its total investments.

*Credit Risk:* This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. GASB No. 40 requires that disclosure be made as to the credit rating of all debt security investments except for obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government. The Primary Health System's investment policy provides guidelines for its fund managers and lists specific allowable investments.

The credit risk profile of the Primary Health System's investments, including assets limited as to use, as of June 30, 2010, is as follows:

<i>Investment Type</i>	<i>Balance as of June 30, 2010</i>	<i>Rating</i>					
		<i>AAA</i>	<i>AA</i>	<i>A</i>	<i>BBB</i>	<i>BB</i>	<i>N/A</i>
Bond mutual funds and other	\$ 6,803,254	\$ 6,427,971	\$ -	\$ -	\$ -	\$ -	\$ 375,283
Municipal bonds	2,994,159	2,411,040	583,119	-	-	-	-
Corporate bonds and commercial paper	5,794,845	-	-	5,794,845	-	-	-
Cash equivalents	16,674,045	-	-	-	-	-	16,674,045
<b>Total investments</b>	<b>\$ 32,266,303</b>	<b>\$ 8,839,011</b>	<b>\$ 583,119</b>	<b>\$ 5,794,845</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 17,049,328</b>

*Investment Rate Risk:* This is the risk that changes in interest rates will adversely affect the fair value of an investment. The Primary Health System's investment policy authorizes a strategic asset allocation that is designed to provide an optimal return over the Primary Health System's investment horizon and within the Hospital's risk tolerance and cash requirements.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

**NOTE F--INVESTMENTS AND ASSETS LIMITED AS TO USE - Continued**

The distribution of the Primary Health System's investments, including assets limited as to use, and excluding the self-insurance trust, by maturity as of June 30, 2010, is as follows:

<i>Investment Type</i>	<i>Balance as of June 30, 2010</i>	<i>Remaining Maturity</i>				<i>N/A</i>
		<i>12 months or less</i>	<i>13-24 Months</i>	<i>25-60 Months</i>	<i>Over 60 Months</i>	
U.S. Government bonds and agencies, including bond mutual funds and other	\$ 128,745,932	\$ 25,633,810	\$ 25,672,767	\$ 44,890,335	\$ 32,549,020	\$ -
Municipal bonds	2,994,159	583,119	-	510,760	1,900,280	-
Corporate bonds and commercial paper	5,794,845	5,794,845	-	-	-	-
Cash equivalents	16,334,576	16,334,576	-	-	-	-
<b>Total investments</b>	<b>\$ 153,869,512</b>	<b>\$ 48,346,350</b>	<b>\$ 25,672,767</b>	<b>\$ 45,401,095</b>	<b>\$ 34,449,300</b>	<b>\$ -</b>

Additionally, the distribution of the Primary Health System's investment held under the self-insurance trust as of June 30, 2010, is as follows:

<i>Investment Type</i>	<i>Balance as of June 30, 2010</i>	<i>Remaining Maturity</i>					<i>N/A</i>
		<i>12 months or less</i>	<i>13-60 Months</i>	<i>61-120 Months</i>	<i>120-240 Months</i>	<i>Over 240 Months</i>	
U.S. Government bonds and agencies	\$ 6,427,971	\$ 1,136,288	\$ 2,819,955	\$ 1,515,811	\$ 525,754	\$ 430,163	\$ -
Cash equivalents	339,469	339,469	-	-	-	-	-
<b>Total investments</b>	<b>\$ 6,767,440</b>	<b>\$ 1,475,757</b>	<b>\$ 2,819,955</b>	<b>\$ 1,515,811</b>	<b>\$ 525,754</b>	<b>\$ 430,163</b>	<b>\$ -</b>

**NOTE G-- LONG-TERM DEBT**

Long-term debt at June 30 consists of:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Revenue and Refunding Bonds, Series 2004, net of bond discount of \$988,502 in 2010 and \$1,141,644 in 2009 and including bond issue premium of \$1,865,966 in 2010	\$ 85,877,464	\$ 83,858,356
Hospital Revenue Refunding Bonds, Series 2000, including bond issue premium of \$350,134 in 2010	40,150,134	41,400,000

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE G--LONG-TERM DEBT - Continued

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Hospital Revenue Bonds, Series 1998A, net of bond discount of \$324,923 in 2010 and \$339,692 in 2009	19,500,077	19,795,308
Hospital Revenue Bonds, Taxable Series 1997A	41,000,000	41,000,000
Revenue and Refunding Bonds, Series 1993	-	8,920,110
Total bonds payable	186,527,675	194,973,774
Less: unamortized premium paid on advance refunding	(1,067,065)	(1,153,003)
Total bonds payable, net	185,460,610	193,820,771
Capital leases - Note M	5,651,417	7,177,526
	191,112,027	200,998,297
Less: current portion	(7,820,568)	(12,336,040)
	<u>\$ 183,291,459</u>	<u>\$ 188,662,257</u>

During fiscal year 2010, the Primary Health System remarketed the Series 2004 Hospital Revenue Refunding Bonds (Series 2004) and the Series 2000 Hospital Revenue Refunding Bonds (Series 2000), as described below, and converted such bonds from a variable auction rate to a fixed rate, paying a combined premium of \$2,311,642 at the time of remarketing. Interest on the Series 2004 and Series 2000 bonds will be payable on April 1 and October 1 of each year commencing April 1, 2010.

On January 1, 2004, the Primary Health System issued \$85,000,000 insured Series 2004 bonds for the purpose of refunding \$80,925,000 of the total outstanding Series 1993 bonds (described below). The Primary Health System also utilized the proceeds to pay certain issuance costs and contributed a portion of the bond proceeds in the amount of \$1,633,658 to establish a debt service fund.

The Series 2004 bonds were issued on parity, with respect to collateral, with other outstanding bonds, described below. The Series 2004 bonds are also secured by a mortgage on a portion of the Primary Health System's main campus. The Series 2004 bonds mature annually on October 1 beginning in 2010 through 2023 in varying amounts. The Series 2004 bonds maturing after October 1, 2019 (excluding those maturing on October 1, 2023) may be redeemed by the Primary Health System after October 1, 2019 at a redemption price equal to the principal amount plus accrued interest. The bonds maturing on October 1, 2023 may be redeemed prior to

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE G--LONG-TERM DEBT - Continued

maturity pursuant to the extraordinary optional redemption and redemption upon damage or condemnation provisions as described in the Remarketing Memorandum by the Primary Health System after October 1, 2014 at a redemption price equal to 100% of the principal amount plus accrued interest. At June 30, 2009, interest on the Series 2004 bonds was payable at a variable auction rate for a 7-day period, which was 0.62%. At June 30, 2010, interest rates for the Series 2004 bonds ranged from 2% to 5%.

In August 2000, the Primary Health System issued \$47,300,000 insured Series 2000 bonds for the purpose of refunding \$40,000,000 of then outstanding Series 1987 bonds and funding a debt service reserve fund in an original amount of \$4,407,377 and to pay issuance costs. The Series 2000 bonds were issued on parity with other outstanding bond issues. The Series 2000 bonds consist of term bonds maturing on October 1, 2022 and 2023 (\$2,590,000 and \$3,100,000, respectively); and serial bonds maturing on October 1 annually beginning in 2010 through 2025. The bonds maturing on October 1, 2023 are subject to mandatory sinking fund redemption prior to maturity and without premium at the principal amount thereof on October 1 in the principal amounts \$2,590,000 and \$3,100,000, for the years 2022 and 2023, respectively. The Series 2000 bonds maturing after October 1, 2014 may be redeemed by the Primary Health System after October 1, 2014 at a redemption price equal to the principal amount plus accrued interest. At June 30, 2009, the Series 2000 bonds were payable at a variable auction rate for a 7-day period, which was 0.62%. At June 30, 2010, interest rates for the Series 2000 bonds are as follows:

Series Bonds	- 2.0% to 5.0%
Term Bonds	- 5.0%

The Primary Health System's 1997A and 1998A Hospital Revenue Bonds (Series 1997A and Series 1998A, respectively) were issued to fund capital improvements for Erlanger Medical Center and establish a debt service reserve fund (1998A only) in an original amount of \$2,174,125. The Series 1997A bonds are taxable and are secured on a parity under a Master Trust Indenture with other outstanding bond issues. The bonds mature beginning in fiscal year 2015 through fiscal year 2028. The 1997A bonds are subject to optional redemption at 100% plus accrued interest. Interest is payable at a variable auction rate for a 35-day period, which was 0.79% at June 30, 2010 and 0.70% at June 30, 2009.

The Series 1998A insured bonds are tax-exempt and consist of \$6,080,000 serial bonds maturing annually on October 1 of each year through 2013 in varying amounts; and term bonds maturing on October 1, 2018 and 2028 (\$5,825,000 and \$17,095,000, respectively). Such bonds are secured on parity with other outstanding bonds. The bonds maturing after October 1, 2008 may be redeemed by the Primary Health System after April 1, 2008 at amounts ranging from 100% to 101% of par value plus accrued interest.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE G--LONG-TERM DEBT - Continued

Interest rates for the Series 1998A bonds are as follows:

\$ 6,080,000 Series Bonds	-	4.50% to 5.00%
\$ 5,825,000 Term Bonds	-	5.0%
\$17,095,000 Term Bonds	-	5.0%

During fiscal year 2002, the Primary Health System defeased \$5,320,000 of the 1998A bond issuance because IRS regulations do not permit tax-exempt debenture proceeds to be used to fund for-profit endeavors. These funds were used in the construction of the Plaza Ambulatory Surgery Center that was contributed to Plaza Surgery, G.P. on September 1, 2001, as discussed in the Discretely Presented Component Units section of Note A. The Primary Health System contributed to an escrow account funds generated from its operations sufficient to fund all principal and interest payments for approximately \$5,320,000 of debentures until maturity. The Primary Health System was released from being the primary obligor and cannot be held liable for the defeased obligation, of which approximately \$4,830,000 remains outstanding at June 30, 2010.

The Primary Health System Hospital Revenue and Refunding Bonds Series 1993 (Series 1993) were issued to advance refund the previously outstanding \$84,000,000 Revenue and Refunding Bonds Series 1986A and \$40,000,000 Hospital Revenue Bonds Series 1991A, 1991B, and 1991C and provide additional capital for expansion. The Series 1993 bonds are secured on parity with other outstanding bonds and consist of \$96,245,000 Serial Bonds with interest rates from 5.5% to 5.625%. The Series 1993 bonds represent general unsecured obligations of the Primary Health System. All remaining Series 1993 serial bonds are insured. As of October 1, 2009, the final principal and interest payment was made for the Series 1993 bonds.

The trust indentures and related documents underlying the bonds contain certain covenants and restrictions. Management believes the Primary Health System was in compliance with all such covenants at June 30, 2010.

The Primary Health System's scheduled principal and interest payments (estimated for variable rate debt based on rates at June 30, 2010) on bonds payable are as follows for the years ending June 30:

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE G--LONG-TERM DEBT - Continued

	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2011	\$ 6,840,193	\$ 6,921,738	\$ 13,761,931
2012	6,670,000	6,726,158	13,396,158
2013	7,155,000	6,436,124	13,591,124
2014	7,230,000	6,090,036	13,320,036
2015	9,910,000	5,702,848	15,612,848
2016-2020	58,020,000	22,125,861	80,145,861
2021-2025	66,520,000	9,586,860	76,106,860
2026-2029	23,279,807	1,042,905	24,322,712
<b>TOTAL</b>	<b>\$ 185,625,000</b>	<b>\$ 64,632,530</b>	<b>\$ 250,257,530</b>

Long-term debt activity for the Primary Health System for the years ended June 30, 2010 and 2009 consisted of the following:

	<i>Balance at June 30, 2008</i>	<i>Additions/ Amortizations</i>	<i>Reductions</i>	<i>Balance at June 30, 2009</i>	<i>Additions/ Amortizations</i>	<i>Reductions</i>	<i>Balance at June 30, 2010</i>
Bonds Payable							
Series 2004	\$ 83,698,727	\$ 159,629	\$ -	\$ 83,858,356	\$ 2,019,108	\$ -	\$ 85,877,464
Series 2000	43,100,000	-	1,700,000	41,400,000	350,134	1,600,000	40,150,134
Series 1998A	20,120,539	14,769	340,000	19,795,308	14,769	310,000	19,500,077
Series 1997A	41,000,000	-	-	41,000,000	-	-	41,000,000
Series 1993	17,065,110	-	8,145,000	8,920,110	-	8,920,110	-
Premium paid on advance refunding	(1,238,941)	85,938	-	(1,153,003)	85,938	-	(1,067,065)
Total bonds payable	203,745,435	260,336	10,185,000	193,820,771	2,469,949	10,830,110	185,460,610
Capital leases	8,595,705	-	1,418,179	7,177,526	-	1,526,109	5,651,417
Total long-term debt	\$ 212,341,140	\$ 260,336	\$ 11,603,179	\$ 200,998,297	\$ 2,469,949	\$ 12,356,219	\$ 191,112,027

NOTE H--PENSION PLAN

The Primary Health System sponsors a single-employer, non-contributory defined benefit pension plan covering substantially all employees meeting certain age and service requirements. In addition to normal retirement benefits, the plan also provides for early retirement, delayed retirement, disability and death benefits. The Primary Health System funds the plan as contributions are approved by the Board of Trustees but not in amounts less than the minimum

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE H--PENSION PLAN - Continued

required contribution determined by the plan's consulting actuary. During the years June 30, 2010 and 2009, the Primary Health System made contributions of \$7,501,056 and \$6,634,155, respectively to the plan. The Primary Health System has the right to amend, in whole or in part, any or all of the provisions of the plan. The plan issues a publicly available financial report that includes a financial statement and required supplementary information for the plan. That report may be obtained by writing to Erlanger Health System, Attention: Human Resources Department, 975 East Third Street, Chattanooga, Tennessee 37403 or by calling 423-778-7000.

The annual pension cost and net pension obligation for the years ended June 30, 2010 and 2009 are as follows:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Annual required contribution	\$ 7,501,004	\$ 7,192,948
Interest on net pension obligation	794,991	749,318
Adjustment to annual required contribution	(741,769)	(699,154)
Annual pension cost	7,554,226	7,243,112
Contributions made	(7,501,056)	(6,634,155)
Change in net pension obligation	53,170	608,957
Net pension obligation at beginning of year	10,599,874	9,990,917
Net pension obligation at end of year	<u>\$ 10,653,044</u>	<u>\$ 10,599,874</u>

The annual expected contribution for the years ended June 30, 2010 and 2009, was determined as part of the January 1, 2010 and 2009 actuarial valuations, respectively, using the projected unit credit cost method. The following actuarial assumptions were utilized:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Investment rate of return	7.5%	7.5%
Projected salary increases	4.5%	4.5%
Inflation	2.5%	2.5%
Increase in Social Security taxable wage base	3.5%	3.5%

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE H--PENSION PLAN - Continued

Annual pension costs, contribution information and the net pension obligation for the last three fiscal years follows:

*Three-Year Trend Information*

<i>Fiscal Year Ending</i>	<i>Annual Pension Cost (APC)</i>	<i>Percentage of APC Contributed</i>	<i>Net Pension Obligation</i>
June 30, 2008	\$ 6,777,948	89%	\$ 9,990,917
June 30, 2009	7,243,112	92%	10,599,874
June 30, 2010	7,554,226	99%	10,653,044

The schedule of funding progress shown below presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. The actuarial asset values are determined using prior year valuations with the addition of current year contributions and expected investment return on market value of assets based on an assumed rate of 7.5%, and deducting benefit payments and administrative expenses for the year. The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments using an average of cost and market value. The plan will reset the amortization base each year equal to the unfunded actuarial accrued liability to be amortized over a 20 year period from each valuation date and using a level percentage of payrolls to assumed general wage inflation as the amortization factor.

*Schedule of Funding Progress*

<i>Actuarial Valuation Date</i>	<i>Actuarial Value of Assets</i>	<i>Actuarial Accrued Liability (AAL)</i>	<i>Total Unfunded AAL (UAAL)</i>	<i>Funded Ratio %</i>	<i>Annual Covered Payroll</i>	<i>UAAL as a Percentage of Covered Payroll</i>
1/1/08	\$118,955,710	\$ 119,927,714	\$ 972,004	99.2%	\$ 138,478,848	0.7%
1/1/09	118,999,412	124,029,646	5,030,234	95.9%	139,291,860	3.6%
1/1/10	120,326,010	136,794,907	16,468,897	88.0%	144,176,724	11.4%

Effective July 1, 2009, the Chattanooga-Hamilton County Hospital Authority Pension Plan was amended to be closed to new employees or rehires, and to further clarify the maximum years of service to be 30. The benefits of current employees will be protected and they will continue to participate in, and accrue services under, the Plan.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

***Years Ended June 30, 2010 and 2009***

**NOTE I--403(b) RETIREMENT PLAN**

On July 1, 1997, the Primary Health System implemented a defined contribution plan under Section 403(b) and 401(a) of the IRC which provides for voluntary contributions by employees upon employment and matching contributions by the Primary Health System after 12 months of service. The plan is for the benefit of generally all employees 25 years of age or older.

The Primary Health System matches 50% of the participant's contribution up to 4% of the employee's earnings. Employer contributions to the plan were \$1,620,228 and \$1,556,167 for the years ended June 30, 2010 and 2009, respectively. Employee contributions to the plan were \$7,710,966 and \$7,764,877 for the years ended June 30, 2010 and 2009, respectively.

**NOTE J--POSTRETIREMENT BENEFITS OTHER THAN PENSIONS**

The Primary Health System sponsors three defined benefit postretirement plans, other than pensions, for full-time employees who have reached retirement age, as defined. The respective plans provide medical, dental and life insurance benefits, along with a lump-sum cash payment for one-half of the hours in the participant's extended illness benefit bank at retirement. The postretirement health and dental plan is contributory and contains other cost-sharing features, such as deductibles and coinsurance. The life insurance plan and the extended illness bank are noncontributory.

The Primary Health System reports other postemployment benefits in accordance with the GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This Statement addresses how state and local governments should account for and report their costs and obligations related to postemployment healthcare and other nonpension benefits. Collectively, these benefits are commonly referred to as other postemployment benefits, or OPEB. This Statement also establishes disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and, for certain employers, the extent to which the plan has been funded over time.

The following table shows the plan's funded status as of the actuarial valuation date as of June 30:

	<u>2010</u>	<u>2009</u>
Actuarial accrued liability	\$ 20,854,837	\$ 18,114,464
Market value of assets	-	-
Unfunded actuarial accrued liability	<u>\$ 20,854,837</u>	<u>\$ 18,114,464</u>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

***Years Ended June 30, 2010 and 2009***

**NOTE J--POSTRETIREMENT BENEFITS OTHER THAN PENSIONS - Continued**

The following is a summary of the components of the annual OPEB cost recognized by the Primary Health System for the years ended June 30:

	<b><i>2010</i></b>	<b><i>2009</i></b>
Annual required contribution	\$ 2,200,640	\$ 1,986,541
Interest on the net obligation	60,761	47,485
Amortization of net obligation	(59,206)	(46,270)
OPEB cost recognized	<b>\$ 2,202,195</b>	<b>\$ 1,987,756</b>

Reconciliation of the net OPEB obligation for the fiscal years ended June 30:

	<b><i>2010</i></b>	<b><i>2009</i></b>
Net OPEB obligation beginning of the year	\$ 1,519,016	\$ 1,187,124
OPEB cost recognized	2,202,195	1,987,756
Actual contributions	(1,311,556)	(1,655,864)
Net OPEB obligation end of the year	<b>\$ 2,409,655</b>	<b>\$ 1,519,016</b>

***Trend Information***

<b><i>Fiscal Year Ending</i></b>	<b><i>Annual OPEB Cost</i></b>	<b><i>Percentage of Annual OPEB Cost Contributed</i></b>	<b><i>Net OPEB Obligation at the End of Year</i></b>
June 30, 2010	\$ 2,202,195	59.56%	\$ 2,409,655
June 30, 2009	1,987,756	83.30%	1,519,016
June 30, 2008	1,945,436	38.98%	1,187,124

***Schedule of Funding Progress***

<b><i>Actuarial Valuation Date</i></b>	<b><i>Actuarial Value of Assets</i></b>	<b><i>Actuarial Accrued Liability</i></b>	<b><i>Unfunded Actuarial Accrued Liability</i></b>	<b><i>Annual Covered Payroll</i></b>	<b><i>Unfunded Actuarial Accrued Liability as a Percent of Covered Payroll</i></b>	<b><i>Funded Ratio</i></b>
June 30, 2010	\$ -	\$ 20,854,837	\$ 20,854,837	\$144,176,724	14.5%	0%
June 30, 2009	-	18,114,464	18,114,464	139,291,860	13.0%	0%
June 30, 2008	-	17,176,864	17,176,864	138,478,848	12.4%	0%

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

**NOTE J--POSTRETIREMENT BENEFITS OTHER THAN PENSIONS - Continued**

The actuarial calculations reflect a long term perspective. Accordingly, the actuarial valuation involves estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The schedule of funding progress presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability. The calculations are based on the benefits currently provided under the terms of the plan as of the date of each valuation and on the sharing of cost between employer and plan members at that point.

The actuarial cost method utilized is the projected unit credit method. The 2010 postretirement benefit cost assumed an average weighted annual rate increase in per capita cost of pre-Medicare covered health benefits of 8.2%, decreasing gradually to 4.5% in 2028 and subsequent years and a weighted average annual rate increase in per capita cost of post-Medicare covered health care benefits of 8.7%, decreasing gradually to 4.5% in 2028 and subsequent years. The 2009 postretirement benefit cost assumed an average weighted annual rate increase in per capita cost of pre-Medicare covered health benefits of 8.4%, decreasing gradually to 4.5% in 2028 and subsequent years and a weighted average annual rate increase in per capita cost of post-Medicare covered health benefits of 8.9%, decreasing gradually to 4.5% in 2028 and subsequent years. The amortization method used is the level percent of payroll method over a thirty year amortization. Other assumptions include a 4% discount rate, and assumed salary increases of 4.5% annually until age 65. The plan is currently open.

The Primary Health System also has a job injury program to provide benefits to workers injured in employment-related accidents. This program provides medical and indemnity benefits to employees injured in the course of employment for a period up to 24 months from the date of injury. The Primary Health System has recorded a projected liability of approximately \$1,350,000 and \$1,200,000 at June 30, 2010 and 2009, respectively. The projected liability was discounted using a 4% and 5% rate of return at June 30, 2010 and 2009, respectively.

**NOTE K--MEDICAL MALPRACTICE AND GENERAL LIABILITY CLAIMS**

As of January 1, 1976, the Primary Health System adopted a self-insurance plan to provide for malpractice and general liability claims and expenses arising from services rendered subsequent to that date. In 1980, the Primary Health System's Self-Insurance Trust Agreement (the Agreement) was amended to include all coverages that a general public liability insurance policy would cover. In 1988, the Agreement was amended and restated to comply with amendments to the Tennessee Governmental Tort Liability Act and to formally include any claims and expenses

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

**NOTE K--MEDICAL MALPRACTICE AND GENERAL LIABILITY CLAIMS - Continued**

related to acts of employees of the Primary Health System. The Primary Health System is funding actuarial estimated liabilities through a revocable trust fund with a bank included as a part of Assets Limited as to Use in the accompanying combined balance sheets. Such amounts in the trust can be withdrawn by the Primary Health System only to the extent there is an actuarially determined excess. The annual deposit to the self-insurance trust fund is determined by management based on known and threatened claims, consultation with legal counsel, and a report of an independent casualty actuary. Losses against the Primary Health System are generally limited by the Tennessee Governmental Tort Liability Act to \$300,000 for injury or death to any one person in any one occurrence or \$700,000 in the aggregate. However, claims against healthcare practitioners are not subject to the foregoing limits applicable to the Primary Health System. Any such individuals employed by the Primary Health System are covered by the Trust to the limits set forth therein. Employed physicians are not subject to the Tort Liability Act and are not covered by the Trust as the Primary Health System has purchased insurance coverage for such individuals.

In the opinion of management, the revocable trust fund assets are adequate at June 30, 2010, to cover potential liability and malpractice claims and expenses that may have been incurred to that date.

The Primary Health System provides for claims and expenses in the period in which the incidence related to such claims occur based on historical experience and consultation with legal counsel. It is the opinion of management that the reserve for estimated losses and loss adjustment expense (LAE) at June 30, 2010 and 2009, respectively, is adequate to cover potential liability and malpractice claims which may have been incurred but not reported (IBNR) to the Primary Health System. Such reserve for IBNR claims reflect a discount rate of 5.5% based on the Primary Health System's expected investment return during the payout period.

The following is a reconciliation of changes in the estimated losses and LAE that have been recognized in the combined financial statements for the years ended June 30, 2010 and 2009:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Reserve for losses and LAE at beginning of year	\$ 5,000,000	\$ 5,000,000
Provision for claims	1,436,121	1,805,432
Payments on claims	(1,686,121)	(1,805,432)
Reserve for losses and LAE at end of year	<u>\$ 4,750,000</u>	<u>\$ 5,000,000</u>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE L--COMMITMENTS AND CONTINGENCIES

*Litigation:* The Primary Health System is subject to claims and suits which arise in the ordinary course of business. In the opinion of management, the ultimate resolution of such pending legal proceedings has been adequately provided for in its combined financial statements, and will not have a material effect on the Primary Health System's results of operations or financial position.

*Government Investigation:* The Primary Health System resolved an investigation, without any admission of wrongdoing by the Primary Health System, in October 2005 by entering into a civil settlement agreement with the U.S. Department of Justice and the Office of Inspector General of HHS. At that time the Primary Health System also entered into a five year Corporate Integrity Agreement. The Primary Health System was not suspended, sanctioned or otherwise restricted from participating in any federal, state or private health insurance program.

NOTE M--LEASES

During 1998, the Primary Health System entered into a twenty-year capital lease with Sports Barn Inc., for the operation of the Lifestyle Center. At the end of the lease term, the Primary Health System will receive a one-half interest in the land and building. Additionally during 2007, the Primary Health System acquired certain equipment and assumed the associated capital leases totaling approximately \$2,920,000.

*Capital:* The following is an analysis of the property under capital leases by major classes at June 30:

	<i>Primary Health System</i>	
	<i>2010</i>	<i>2009</i>
Land and improvements	\$ 500,000	\$ 500,000
Buildings	9,620,457	9,620,457
Equipment	2,817,434	2,920,462
	12,937,891	13,040,919
Less: accumulated amortization	(8,052,659)	(7,221,984)
	<u>\$ 4,885,232</u>	<u>\$ 5,818,935</u>

The following is a schedule of future minimum lease payments under capital leases at June 30, 2010:

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE M--LEASES - Continued

<u>Year Ending June 30,</u>	
2011	\$ 1,244,845
2012	896,445
2013	834,730
2014	841,689
2015	841,690
2016-2020	<u>2,014,222</u>
Total minimum lease payments	6,673,621
Less: amount representing interest	<u>(1,112,204)</u>
Present value of minimum lease payments (including current portion of \$1,019,169)	<u><u>\$ 5,561,417</u></u>

*Operating:* The Primary Health System rents office space and office equipment under non-cancelable operating leases through 2020, containing various lease terms. The leases have other various provisions, including sharing of certain executory costs. Rent expense under operating leases was approximately \$3,532,864 and \$4,040,484 in 2010 and 2009, respectively. Future minimum lease commitments at June 30, 2010 for all non-cancelable leases with terms in excess of one year are as follows:

<u>Year Ending June 30,</u>	
2011	\$ 2,504,864
2012	2,479,539
2013	1,966,048
2014	1,799,152
2015	832,922
Thereafter	<u>1,246,290</u>
	<u><u>\$ 10,828,815</u></u>

NOTE N--DERIVATIVE FINANCIAL INSTRUMENTS

Simultaneous with the issuance of the \$85,000,000 Series 2004 bonds discussed in Note G, the Primary Health System entered into interest rate swap agreements. In an effort to balance its exposure to market fluctuations with respect to interest rates as well as to balance its mix of fixed and variable rate debt instruments, the Primary Health System executed three distinct interest rate swap agreements with Lehman Brothers Special Financing, Inc.

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

---

NOTE N--DERIVATIVE FINANCIAL INSTRUMENTS - Continued

With respect to the Series 2004 bonds, the Primary Health System executed a swap where the Primary Health System receives a variable rate equal to 67% of the one-month LIBOR-BBA rate and pays a fixed rate of 3% on a notional amount of \$40,100,000. Unless terminated at an earlier date (at the Primary Health System's option), this agreement terminates on October 1, 2013.

With respect to the 1997A Series bonds, the Primary Health System executed a swap agreement whereby the Primary Health System receives a variable rate equal to the one-month LIBOR-BBA rate and pays a fixed rate equal to 5.087% on a notional amount of \$41,000,000. Unless terminated at an earlier date (at the Primary Health System's option), this agreement terminates on October 1, 2027.

With respect to the 1998A Series bonds, the Primary Health System executed a swap agreement whereby the Primary Health System receives a fixed rate of 3.932% and pays a variable rate equal to the Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index on a notional amount of \$16,305,000. Unless terminated at an earlier date (at the Primary Health System's option), this agreement terminates on October 1, 2027.

Although these swap instruments are intended to manage exposure to interest rate risks associated with the various debt instruments referred to above, none of these swap agreements have been designated as a hedge for accounting purposes. Accordingly, the interest rate swaps are reflected in the accompanying combined balance sheets at their aggregate fair value (a net liability of \$7,632,908 and \$6,315,533 at June 30, 2010 and 2009, respectively) and the changes in the value of the swaps are reflected as a component of nonoperating revenues in the combined statements of revenue, expenses and changes in net assets.

The counter-party to such interest rate swap agreements is Lehman Brothers Special Financing, Inc., which as of June 30, 2010 is considered a debtor-in-possession. Management has considered the effects of any credit value adjustment and while management believes the estimated fair value of the interest rate swap agreements is reasonable, the estimate is subject to change in the near term.

NOTE O--FAIR VALUE MEASUREMENT

The Primary Health System adopted FASB ASC 820 during 2009 (Note A). FASB ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, FASB ASC 820 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE O--FAIR VALUE MEASUREMENT - Continued

obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumption about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

*Valuation Hierarchy:* FASB ASC 820 establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 - Quoted market prices in active markets for identical assets or liabilities.
- Level 2 - Observable market-based inputs or unobservable inputs that are corroborated by market data.
- Level 3 - Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. Level 3 includes values determined using pricing models, discounted cash flow methodologies, or similar techniques reflecting the Hospital's own assumptions.

In instances where the determination of the fair value hierarchy measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Primary Health System's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The following table presents assets and liabilities reported at fair value as of June 30, 2010 and their respective classification under the FASB ASC 820 valuation hierarchy:

<i>Carrying Value</i>	<i>Quoted Prices in Active Markets (Level 1)</i>	<i>Significant Other Observable Inputs (Level 2)</i>	<i>Significant Unobservable Inputs (Level 3)</i>
<b>Assets Measured at Fair Value on a Recurring Basis</b>			
Investment in government and municipal bonds	\$ 138,168,062	\$ 138,168,062	\$ -
Investments in corporate bonds and commercial paper	5,794,845	5,794,845	-
Short-term investments and cash equivalents	29,654,205	29,654,205	-

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Combined Financial Statements - Continued*

*Years Ended June 30, 2010 and 2009*

NOTE O--FAIR VALUE MEASUREMENT - Continued

	<i>Carrying Value</i>	<i>Quoted Prices in Active Markets (Level 1)</i>	<i>Significant Other Observable Inputs (Level 2)</i>	<i>Significant Unobservable Inputs (Level 3)</i>
<b>Liabilities Measured at Fair Value on a Recurring Basis</b>				
Interest rate swap agreements	(7,632,908)	-	-	(7,632,908)

A certain portion of the inputs used to value the Primary Health System interest rate swap agreements are unobservable inputs available to a market participant. As a result, the Primary Health System has determined that the interest rate swap valuations are classified in Level 3 of the fair value hierarchy.

The following tables provide a summary of changes in the fair value of the Primary Health System's interest rate swap agreements liabilities during the fiscal year ended June 30, 2010:

	<i>Interest Rate Swap Agreements</i>
Beginning of year	\$ (6,315,533)
Loss on mark-to-market of interest rate swaps	(1,317,375)
End of Year	<u>\$ (7,632,908)</u>

***Required Supplementary Information***

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Schedule of Expenditures of Federal Awards*

*Year Ended June 30, 2010*

<i>Grantor</i>	<i>Pass-Through Grantor Agency</i>	<i>Program Name</i>	<i>CFDA Number</i>	<i>Grant Number (Grant Period)</i>	<i>Federal Expenditures</i>
U.S. Department of Agriculture	Chattanooga-Hamilton County Health Department	Special Supplemental Nutrition Program for Women, Infants, and Children	10.557	GG-09-26525-00 (10/1/08 - 9/30/09)	\$ 13,841
				GG-10-30981-00 (10/1/09 - 9/30/10)	54,334
					68,175
U.S. Department of Agriculture	n/a	Distance Learning and Telemedicine Loans and Grants	10.855	Tennessee 733-A17 (11/3/08 - 11/2/11)	197,500
Total U.S. Department of Agriculture					265,675
U.S. Department of Health and Human Services	University of Tennessee	Environmental Health	93.113	5 R25 ES014317-03 (8/1/08 - 7/31/10)	22,713
U.S. Department of Health and Human Services	n/a	Community Health Centers	93.224	H80CS00091-08-03 (12/1/08 - 11/30/09)	792,310
				H80CS00091-09-01 (12/1/09 - 11/30/10)	1,165,245
					1,957,555
U.S. Department of Health and Human Services	MeHarry Medical College	Community Health Centers Network	93.399	040805JEM101S104 (5/1/09 - 4/30/10)	91,924
U.S. Department of Health and Human Services	n/a	ARRA-Grants to Health Center Programs	93.703*	C81CS13762 (6/29/09 - 6/28/11)	33,319
				H8BCS11874 (3/27/09 - 3/26/11)	179,737
					213,056
U.S. Department of Health and Human Services	State of Tennessee Department of Health, Bureau of TennCare	Medical Assistance Program	93.778*	GG-08-21474-00 (7/1/07 - 6/30/10)	382,320
				GR-09-25330-00 (7/1/08 - 4/15/11)	1,074,005
					1,456,325
U.S. Department of Health and Human Services	State of Tennessee Department of Health	Bioterrorism Hospital Preparedness	93.889	Z-08-200392-00 (9/1/07 - 8/31/09)	101,023
				Z-08-200394-00 (9/1/07 - 8/31/09)	15,000
				Z-08-200392-01 (9/1/07 - 8/31/09)	234,500

*See notes to schedules of expenditures of federal awards and state and other financial assistance.*

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Schedule of Expenditures of Federal Awards - Continued*

*Year Ended June 30, 2010*

<i>Grantor</i>	<i>Pass-Through Grantor Agency</i>	<i>Program Name</i>	<i>CFDA Number</i>	<i>Grant Number (Grant Period)</i>	<i>Federal Expenditures</i>
				Z-08-200467-01 (9/1/07 - 8/31/09)	147,431
				Z-08-200394-01 (9/1/07 - 8/31/09)	34,240
				Z-08-200393-01 (9/1/07 - 8/31/09)	15,000
				GR-10-30003-00 (8/9/09 - 6/30/10)	219,592
				GR-10-30000-00 (8/9/09 - 6/30/10)	53,297
					820,083
U.S. Department of Health and Human Services	State of Tennessee Department of Health	Maternal and Child Health Services Block Grant to the States	93.994	GG-10-31131-00 (7/1/09 - 6/30/10)	202,700
				GG-10-31459-00 (7/1/09 - 6/30/10)	17,200
					219,900
				Total U.S. Department of Health and Human Services	4,781,556
				Total Expenditures of Federal Awards	\$ 5,047,231

\* Denotes major program

*See notes to schedules of expenditures of federal awards and state and other financial assistance.*

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Schedule of Expenditures of State and Other Financial Assistance*

*Year Ended June 30, 2010*

<i>Grantor</i>	<i>Program Name</i>	<i>Contract Number (Contract Period)</i>	<i>Beginning Balance</i>	<i>Cash Received</i>	<i>Grant Expenditures (Adjustments)</i>	<i>Ending Balance</i>
State of Tennessee Department of Health, Bureau of TennCare	Medical Assistance Program	GG-08-21474-00 (7/1/07 - 6/30/10)	\$ 191,575	\$ 477,554	\$ 382,405	\$ 96,426
State of Tennessee Department of Health	Maternal and Child Health Services Block Grant to the States	GG-09-25769-01 (7/1/08 - 6/30/09)	14,707	14,707	-	-
		GG-09-25717-00 (7/1/08 - 6/30/09)	6,674	-	(2,495)	4,179
		GG-10-31131-00 (7/1/09 - 6/30/10)	-	-	85,100	85,100
		GG-10-31459-00 (7/1/09 - 6/30/10)	-	-	16,291	16,291
		GG-09-25768-00 (7/1/08 - 6/30/09)	4,850	4,850	-	-
		GG-10-28785-00 (7/1/09 - 6/30/14)	-	16,039	26,600	10,561
State of Tennessee Department of Health	Project Diabetes	GR-09-25716-00 (7/1/08 - 6/30/09)	9,322	-	(9,322)	-
State of Tennessee Department of Finance and Administration	Medical Assistance Program	GG-10-28378-00 (7/1/09 - 6/30/12)	-	-	143,932	143,932
<b>TOTAL STATE AND OTHER FINANCIAL ASSISTANCE</b>			<b>\$ 227,128</b>	<b>\$ 513,150</b>	<b>\$ 642,511</b>	<b>\$ 356,489</b>

*See notes to schedules of expenditures of federal awards and state and other financial assistance.*

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Notes to Schedules of Expenditures of Federal Awards and State and Other Financial Assistance*

*Year Ended June 30, 2010*

**NOTE A--BASIS OF PRESENTATION**

The accompanying schedule of expenditures of federal awards and the schedule of expenditures of state and other financial assistance includes the grant activity of Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) and is presented on the accrual basis of accounting. The information in these schedules is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and the Tennessee Comptroller of the Treasury, respectively. Therefore, some amounts presented in these schedules may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**NOTE B--CONTINGENCIES**

The Primary Health System's federal programs are subject to financial and compliance audits by grantor agencies which, if instances of material noncompliance are found, may result in disallowed expenditures and affect the Primary Health System's continued participation in specific programs. The amount, if any, of expenditures which may be disallowed by the grantor agencies cannot be determined at this time, although the Primary Health System expects such amounts, if any, to be immaterial.

**NOTE C--BIOTERRORISM HOSPITAL PREPAREDNESS AWARDS**

The following is a reconciliation of the Bioterrorism Hospital Preparedness Awards of the Primary Health System:

<i>Grant</i>	<i>Unexpended Balance at June 30, 2009</i>	<i>Receipts</i>	<i>Awards Earned by Expenditures</i>	<i>Unexpended Balance at June 30, 2010</i>
Z-08-200392-00	\$ (101,023)	\$ -	\$ 101,023	\$ -
Z-08-200394-00	(15,000)	-	15,000	-
Z-08-200392-01	(234,500)	-	234,500	-
Z-08-200467-01	(147,431)	-	147,431	-
Z-08-200393-01	(15,000)	-	15,000	-
Z-08-200394-01	(34,240)	-	34,240	-
GR-10-30003-00	-	359,324	219,592	(139,732)
GR-10-30000-00	-	126,372	53,297	(73,075)
GR-10-30002-00	-	20,000	-	(20,000)
GR-10-30001-00	-	20,000	-	(20,000)
<b>Total</b>	<b>\$ (547,194)</b>	<b>\$ 525,696</b>	<b>\$ 820,083</b>	<b>\$ (252,807)</b>

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Schedule of Prior Audit Findings*

*Year Ended June 30, 2010*

---

There were no prior audit findings.

REPORT ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED  
ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN  
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Trustees of  
Chattanooga-Hamilton County Hospital Authority  
(d/b/a Erlanger Health System):

We have audited the financial statements of the business-type activities and the aggregate discretely presented component units of Chattanooga-Hamilton County Hospital Authority (d/b/a Erlanger Health System) as of and for the year ended June 30, 2010, which collectively comprise the Chattanooga-Hamilton County Hospital Authority's basic combined financial statements and have issued our report thereon dated November 8, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The financial statements of ContinuCare HealthServices, Inc., a discretely presented component unit, were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Chattanooga-Hamilton County Hospital Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Chattanooga-Hamilton County Hospital Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Chattanooga-Hamilton County Hospital Authority's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

#### Compliance and Other Matters

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

This report is intended solely for the information and use of the Board of Trustees, management, federal awarding agencies, pass-through entities, state awarding agencies and the State of Tennessee, Comptroller of the Treasury and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Pauling Yarbey: Associates PC". The signature is written in a cursive, flowing style.

Knoxville, Tennessee  
November 8, 2010



CERTIFIED PUBLIC ACCOUNTANTS

Pershing Yoakley & Associates, P.C.  
One Cherokee Mills, 2220 Sutherland Avenue  
Knoxville, TN 37919  
(p) (865) 673-0844 (f) (865) 673-0173  
(w) www.pyapc.com

REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT  
AND MATERIAL EFFECT ON EACH MAJOR PROGRAM  
AND ON INTERNAL CONTROL OVER  
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Trustees of  
Chattanooga-Hamilton County Hospital Authority  
(d/b/a Erlanger Health System):

Compliance

We have audited Chattanooga-Hamilton County Hospital Authority's (d/b/a Erlanger Health System) compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2010. Chattanooga-Hamilton County Hospital Authority's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Chattanooga-Hamilton County Hospital Authority's management. Our responsibility is to express an opinion on Chattanooga-Hamilton County Hospital Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Chattanooga-Hamilton County Hospital Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Chattanooga-Hamilton County Hospital Authority's compliance with those requirements.

In our opinion, Chattanooga-Hamilton County Hospital Authority complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2010.

## Internal Control Over Compliance

The management of Chattanooga-Hamilton County Hospital Authority is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Chattanooga-Hamilton County Hospital Authority's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Chattanooga-Hamilton County Hospital Authority's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Board of Trustees, management, federal awarding agencies, pass-through entities, state awarding agencies and the State of Tennessee, Comptroller of the Treasury and is not intended to be and should not be used by anyone other than these specified parties.

*Pauling Yarbey: Associates PC*

Knoxville, Tennessee  
November 8, 2010

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
(d/b/a Erlanger Health System)

*Schedule of Findings and Questioned Costs*

*Year Ended June 30, 2010*

---

**Section I - Summary of Auditor's Results**

**FINANCIAL STATEMENTS**

The auditor's report expressed an unqualified opinion on the financial statements of Chattanooga-Hamilton County Hospital Authority.

**Internal control over financial reporting:**

Material weakness(es) identified?	Yes [ ] No [X]
Significant deficiency identified not considered to be material weaknesses?	Yes [ ] No [X]
Noncompliance material to financial statements noted?	Yes [ ] No [X]

**FEDERAL AWARDS**

**Internal control over major programs:**

Material weakness(es) identified?	Yes [ ] No [X]
Significant deficiency identified not considered to be material weaknesses?	Yes [ ] No [X]

The auditor's report expressed an unqualified opinion on compliance for major programs.

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133? Yes [ ] No [X]

**Identification of Major Programs:**

<i>CFDA Number(s)</i>	<i>Name of Federal Program or Cluster</i>
93.703	U.S. Department of Health and Human Services - ARRA - Grants to Health Center Programs
93.778	U.S. Department of Health and Human Services - Medical Assistance Program

Dollar threshold used to distinguish between Type A and Type B programs: \$ 300,000

Auditee qualified as low-risk auditee? Yes [X] No [ ]

**Section II - Financial Statement Findings**

This section identifies the significant deficiencies, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements, and abuse related to the financial statements for which *Government Auditing Standards* require reporting in a Circular A-133 audit.

Not applicable, no financial statement findings.

---

**CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY**  
**(d/b/a Erlanger Health System)**

*Schedule of Findings and Questioned Costs - Continued*

*Year Ended June 30, 2010*

---

**Section III - Federal Award Findings and Questioned Costs**

This section identifies the audit findings required to be reported by Section 510(a) of Circular A-133 (for example, significant deficiencies, material weaknesses, and material instances of noncompliance, including questioned costs), as well as any abuse findings involving federal awards that is material to a major program.

Not applicable, no financial statement findings or questioned costs.