



**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Basic Financial Statements and Schedules

June 30, 2010 and 2009

(With Independent Auditors' Report Thereon)

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

**Table of Contents**

	<b>Page(s)</b>
Independent Auditors' Report	2 – 3
Basic Financial Statements:	
Balance Sheets – June 30, 2010 and 2009	4
Statements of Revenues, Expenses, and Changes in Net Assets – Years ended June 30, 2010 and 2009	5
Statements of Cash Flows – Years ended June 30, 2010 and 2009	6 – 7
Notes to Basic Financial Statements	8 – 32
Schedule 1 – Combining Balance Sheet – June 30, 2010	33
Schedule 2 – Combining Statement of Revenues, Expenses, and Changes in Net Assets – Year end June 30, 2010	34



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## **Independent Auditors' Report**

The Board of Directors  
Shelby County Health Care Corporation:

We have audited the accompanying balance sheets of Shelby County Health Care Corporation, a component unit of Shelby County, Tennessee (d/b/a The Regional Medical Center at Memphis – “The Med”) as of June 30, 2010 and 2009, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of The Med’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Shelby County Health Care Corporation as of June 30, 2010 and 2009, and the changes in its financial position and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued our report dated November 29, 2010 on our consideration of The Med’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.

The Med has not presented management’s discussion and analysis that U.S. generally accepted accounting principles require to supplement, although not to be part of, the basic financial statements.



Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise The Med's basic financial statements. The combining information included in Schedules 1 and 2 is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The combining 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.

KPMG LLP

November 29, 2010

**SHELBY COUNTY HEALTH CARE CORPORATION**

Balance Sheets

June 30, 2010 and 2009

Assets	2010	2009
Current assets:		
Cash and cash equivalents	\$ 53,576,684	38,602,840
Investments	3,922,517	3,484,123
Patient accounts receivable, net of allowances for uncollectible accounts of \$96,148,000 in 2010 and \$80,528,000 in 2009	20,275,330	22,338,257
Other receivables	10,002,085	9,923,709
Other current assets	4,357,522	5,364,185
Total current assets	92,134,138	79,713,114
Restricted investments	5,235,876	4,464,255
Capital assets, net	53,074,615	60,555,797
Investments in joint ventures	441,193	7,092,667
Other assets	—	36,829
Total assets	\$ 150,885,822	151,862,662
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable	\$ 6,966,427	20,470,874
Accrued expenses and other current liabilities	28,609,381	19,009,466
Current installments of capital lease obligation	—	354,822
Current installments of amounts payable to Shelby County	212,802	1,234,598
Total current liabilities	35,788,610	41,069,760
Capital lease obligation, excluding current installments	—	1,236,562
Amounts payable to Shelby County, excluding current installments	464,311	2,098,320
Accrued professional and general liability costs	11,082,000	10,130,000
Net postemployment benefit obligation	935,000	720,000
Total liabilities	48,269,921	55,254,642
Net assets:		
Invested in capital assets, net of related debt	52,397,502	55,631,495
Restricted for:		
Capital assets	4,372,870	4,193,733
Indigent care	651,783	640,359
Unrestricted	45,193,746	36,142,433
Total net assets	102,615,901	96,608,020
Commitments and contingencies		
Total liabilities and net assets	\$ 150,885,822	151,862,662

See accompanying notes to basic financial statements.

**SHELBY COUNTY HEALTH CARE CORPORATION**

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Operating revenues:		
Net patient service revenue (including additional incremental reimbursement from various state agencies for participation in TennCare/Medicaid programs of approximately \$40,228,000 in 2010 and \$36,505,000 in 2009)	\$ 251,036,699	263,645,491
Other revenue	9,944,314	9,827,446
Total operating revenues	<u>260,981,013</u>	<u>273,472,937</u>
Operating expenses:		
Salaries and benefits	131,437,995	154,009,742
Supplies and services	58,655,297	69,140,114
Physician and professional fees	33,003,305	34,208,794
Purchased medical services	13,266,244	14,344,622
Plant operations	11,208,352	11,877,915
Insurance	6,946,579	7,688,820
Administrative and general	14,627,901	20,429,376
Community services	382,640	418,715
Depreciation and amortization	11,754,357	13,022,436
Total operating expenses	<u>281,282,670</u>	<u>325,140,534</u>
Operating loss	<u>(20,301,657)</u>	<u>(51,667,597)</u>
Nonoperating revenues (expenses):		
Interest expense	(364,280)	(238,310)
Investment income	455,390	505,521
Appropriations from Shelby County	30,616,666	31,291,667
Other	(6,398,238)	(131,584)
Total nonoperating revenues, net	<u>24,309,538</u>	<u>31,427,294</u>
Income (loss) before capital appropriations	4,007,881	(20,240,303)
Capital appropriations from City of Memphis	2,000,000	—
Increase (decrease) in net assets	6,007,881	(20,240,303)
Net assets, beginning of year	96,608,020	116,848,323
Net assets, end of year	<u>\$ 102,615,901</u>	<u>96,608,020</u>

See accompanying notes to basic financial statements.

## SHELBY COUNTY HEALTH CARE CORPORATION

### Statements of Cash Flows

Years ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Cash flows from operating activities:		
Receipts from and on behalf of patients and third-party payors	\$ 251,903,847	272,402,884
Other cash receipts	10,942,031	10,718,934
Payments to suppliers	(138,848,211)	(154,473,499)
Payments to employees and related benefits	(131,859,586)	(154,485,242)
Net cash used in operating activities	<u>(7,861,919)</u>	<u>(25,836,923)</u>
Cash flows from noncapital financing activities:		
Appropriations received from Shelby County	<u>30,616,666</u>	<u>31,291,667</u>
Net cash provided by noncapital financing activities	<u>30,616,666</u>	<u>31,291,667</u>
Cash flows from capital and related financing activities:		
Capital appropriations received from City of Memphis	2,000,000	—
Repayment of capital lease obligation	(1,591,384)	(258,616)
Repayment of amounts payable to Shelby County	(2,655,805)	(1,110,103)
Capital expenditures	(6,021,156)	(2,370,150)
Proceeds from sale of capital assets	2,410	13,416
Interest payments	(759,150)	(597,501)
Net cash used in capital and related financing activities	<u>(9,025,085)</u>	<u>(4,322,954)</u>
Cash flows from investing activities:		
Purchases of investments	(6,521,348)	(4,520,689)
Proceeds from sale of investments	5,376,696	4,499,940
Distributions received from joint venture	1,998,807	1,500,000
Investment income proceeds	390,027	713,400
Net cash provided by investing activities	<u>1,244,182</u>	<u>2,192,651</u>
Net increase in cash and cash equivalents	14,973,844	3,324,441
Cash and cash equivalents, beginning of year	<u>38,602,840</u>	<u>35,278,399</u>
Cash and cash equivalents, end of year	<u>\$ 53,576,684</u>	<u>38,602,840</u>

**SHELBY COUNTY HEALTH CARE CORPORATION**

Statements of Cash Flows

Years ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (20,301,657)	(51,667,597)
Adjustment to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization	11,754,357	13,022,436
Changes in operating assets and liabilities:		
Patients accounts receivable, net	2,062,927	1,235,108
Other receivables	(117,593)	8,273,418
Other current assets	1,006,663	(929,579)
Other assets	36,829	6,916
Accounts payable	(13,465,230)	2,997,455
Accrued expenses and other current liabilities	9,994,785	(1,846,080)
Accrued professional and general liability costs	952,000	2,831,000
Net postemployment benefit obligation	215,000	240,000
Net cash used in operating activities	\$ <u>(7,861,919)</u>	<u>(25,836,923)</u>
Supplemental schedule of noncash investing and financing activities:		
Net increase (decrease) in the fair value of investments	\$ 63,895	(457,914)
Equity in loss of joint ventures	—	(145,000)
Impairment of investment in joint venture	(4,652,667)	—
Capital lease obligation	—	1,850,000
Loss on capital asset disposals	1,745,571	—

See accompanying notes to basic financial statements.

# SHELBY COUNTY HEALTH CARE CORPORATION

(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

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

Shelby County Health Care Corporation (d/b/a The Regional Medical Center at Memphis – “The Med”) was incorporated on June 15, 1981, with the approval of the Board of County Commissioners of Shelby County, Tennessee (the County). The Med is a broad continuum healthcare provider that operates facilities owned by the County under a long-term lease. The lease arrangement effectively provided for the transfer of title associated with operating fixed assets and the long-term lease (for a nominal amount) of related real property. The lease expires in 2031.

The Med is a component unit of the County as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*. The Med’s component unit relationship to the County is principally due to financial accountability as defined in GASB Statement No. 14. The Med is operated by a 13-member board of directors, all of whom are appointed by the Mayor of the County and approved by the County Commission.

The Regional Medical Center Foundation (The Med Foundation) is a component unit of The Med principally due to The Med’s financial accountability for The Med Foundation as defined in GASB Statement No. 14. The Med Foundation is operated by a board of directors, all of whom are appointed by The Med’s board. The Med Foundation is a blended component unit of The Med because it provides services entirely to The Med. The Med Foundation issues separate audited financial statements, which can be obtained by writing to The Regional Medical Center Foundation, 877 Jefferson Avenue, Memphis, TN 38103 or calling 901-545-7482.

GASB Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, requires a management’s discussion and analysis (MD&A) section providing an analysis of The Med’s overall financial position and results of operations; however, The Med has chosen to omit the MD&A from these accompanying financial statements.

The significant accounting policies used by The Med in preparing and presenting its financial statements follow:

### (a) Presentation

The financial statements include the accounts of The Med. All material intercompany accounts and transactions have been eliminated.

### (b) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires that management make estimates and assumptions affecting the reported amounts of assets, liabilities, revenues, and expenses, as well as disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

Significant items subject to estimates and assumptions include the determination of the allowances for contractual adjustments and uncollectible accounts, reserves for professional and general liability claims, reserves for employee healthcare claims, net postretirement benefit cost and obligation, and estimated third-party payor settlements.

**SHELBY COUNTY HEALTH CARE CORPORATION**

(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

In addition, laws and regulations governing the Medicare, TennCare, and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates related to these programs will change by a material amount in the near term.

**(c) *Enterprise Fund Accounting***

The Med's financial statements are prepared using the economic resources measurement focus and accrual basis of accounting. Pursuant to and as permitted by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, The Med has elected to not apply the provisions of any otherwise relevant pronouncements of the Financial Accounting Standards Board (FASB) issued after November 30, 1989. The Med applies the provisions of all relevant pronouncements of the GASB and pronouncements of the FASB issued prior to November 30, 1989 that do not conflict with GASB pronouncements.

**(d) *Cash Equivalents***

The Med considers investments in highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

**(e) *Investments and Investment Income***

Investments are carried at fair value, principally based on quoted market prices. Investment income (including realized and unrealized gains and losses) from investments is reported as nonoperating revenue.

**(f) *Inventories***

Inventories, consisting principally of medical supplies and pharmaceuticals, are stated at the lower of cost (first-in, first-out method) or replacement market.

**(g) *Investments in Joint Ventures***

Investments in joint ventures consist of The Med's equity interests in joint ventures as measured by its ownership interest if The Med has an ongoing financial interest in or ongoing financial responsibility for the joint venture. The investments are initially recorded at cost and are subsequently adjusted for additional contributions, distributions, undistributed earnings and losses, and impairment losses.

**(h) *Capital Assets***

Capital assets are recorded at cost, if purchased, or at fair value at the date of donation. Depreciation is provided over the useful life of each class of depreciable asset using the straight-line method. Maintenance and repairs are charged to operations. Major renewals and betterments are capitalized. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and the gain or loss, if any, is included in nonoperating revenues (expenses) in the accompanying statements of revenues, expenses, and changes in net assets.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

The Med capitalizes interest cost on qualified construction expenditures, net of income earned on related trusteed assets, as a component of the cost of related projects. Interest costs capitalized in 2009 were approximately \$124,000. No such interest costs were capitalized in 2010.

All capital assets other than land are depreciated using the following lives:

Land improvements	5 to 25 years
Buildings and improvements	10 to 40 years
Fixed equipment	5 to 25 years
Movable equipment	3 to 20 years
Software	3 years

**(i) Impairment of Capital Assets**

Capital assets are reviewed for impairment when service utility has declined significantly and unexpectedly. If such assets are no longer used, they are reported at the lower of carrying value or fair value. If such assets will continue to be used, the impairment loss is measured using the method that best reflects the diminished service utility of the capital asset. No charge related to impairment matters was required during 2010 or 2009.

**(j) Compensated Absences**

The Med's employees accumulate vacation, holiday, and sick leave at varying rates depending upon their years of continuous service and their payroll classification, subject to maximum limitations. Upon termination of employment, employees are paid all unused accrued vacation and holiday time at their regular rate of pay up to a designated maximum number of days. Since the employees' vacation and holiday time both accumulates and vests, an accrual for this liability is included in accrued expenses and other current liabilities in the accompanying balance sheets. An accrual is recognized for unused sick leave expected to be paid to employees eligible to retire.

**(k) Net Assets**

Net assets of The Med are classified into the following components:

- *Net assets invested in capital assets, net of related debt*, consist of capital assets net of accumulated depreciation and reduced by outstanding balances of any borrowings used to finance the purchase or construction of those assets.
- *Restricted net assets* include those net assets with limits on their use that are externally imposed (by creditors, grantors, contributors, or the laws and regulations of other governments).
- *Unrestricted net assets* are remaining net assets that do not meet the definition of invested in capital assets, net of related debt or restricted.

When The Med has both restricted and unrestricted resources available to finance a particular program, it is The Med's policy to use restricted resources before unrestricted resources.

**SHELBY COUNTY HEALTH CARE CORPORATION**

(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

The Med Foundation historically and to-date does not maintain donor-restricted endowment funds, or any Board-designated endowments. The Med Foundation's Board has interpreted Tennessee's State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor stipulations to the contrary. In all material respects, income from The Med Foundation's donor-restricted endowment funds is itself restricted to specific donor-directed purposes, and is therefore accounted for within restricted net assets until expended in accordance with the donor's wishes. The Med Foundation oversees individual donor-restricted endowment funds to ensure that the fair value of the original gift is preserved.

**(l) *Statement of Revenues, Expenses, and Changes in Net Assets***

For purposes of presentation, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services, other than financing costs, are reported as operating revenues and operating expenses. Other transactions, such as interest expense, investment income, appropriations from Shelby County, gain (loss) on disposal of capital assets, and equity in earnings and impairment losses of joint ventures, are reported as nonoperating revenues and expenses.

**(m) *Net Patient Service Revenue***

Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. Changes in estimates related to prior cost reporting periods resulted in an increase in net patient service revenue of approximately \$642,000 and \$1,750,000 in 2010 and 2009, respectively.

**(n) *Charity Care***

The Med provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because The Med does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

**(o) *Income Taxes***

The Med and The Med Foundation have been recognized by the Internal Revenue Service as exempt from federal income tax under Internal Revenue Code Section 501(a) as organizations described in Section 501(c)(3) and, therefore, related income is generally not subject to Federal or state income taxes.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(p) Appropriations**

The County has historically appropriated funds annually to The Med to partially offset the cost of medical care for indigent residents of the County. Appropriations for indigent residents from the County for 2010 and 2009 were approximately \$30.6 million and \$31.3 million, respectively. Appropriations from the County are reported as nonoperating revenue in the accompanying statements of revenues, expenses, and changes in net assets. During 2010, The Med received \$2 million of capital appropriations from the City of Memphis. Capital appropriations are reported as such in the 2010 statement of revenues, expenses, and changes in net assets.

**(2) Deposits and Investments**

The composition of cash and cash equivalents follows:

	<u>2010</u>	<u>2009</u>
Cash	\$ 12,678,543	6,821,710
Money market funds	40,898,141	31,781,130
	<u>\$ 53,576,684</u>	<u>38,602,840</u>

The Med's and The Med Foundation's bank balances that are considered to be exposed to custodial credit risk at June 30, 2010 and 2009 follow:

	<u>2010</u>	<u>2009</u>
Uninsured, uncollateralized, or collateralized by securities held by the pledging institution or by its trust department or agent in other than The Med's name	\$ 40,933,252	38,016,519

Investments and restricted investments include amounts held by both The Med and The Med Foundation.

The composition of investments and restricted investments follows:

	<u>2010</u>	<u>2009</u>
U.S. agencies	\$ 4,431,673	4,221,697
Certificates of deposit	480,000	100,000
Corporate bonds	2,061,327	1,488,957
Discount notes	—	139,986
U.S. government funds	804,608	1,009,064
Common stock	1,345,997	955,354
Accrued interest	34,788	33,320
	<u>\$ 9,158,393</u>	<u>7,948,378</u>

Custodial credit risk is the risk that, in the event of a bank failure, an organization's deposits may not be returned. Neither The Med nor The Med Foundation has a deposit policy for custodial credit risk.

**SHELBY COUNTY HEALTH CARE CORPORATION**

(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

At June 30, 2010, The Med and The Med Foundation had investments in debt securities with the following maturities:

	<b>Fair value</b>	<b>Investment and restricted investment maturities (in years)</b>			
		<b>Less than 6 months</b>	<b>6 months to 1 year</b>	<b>1 – 5 years</b>	<b>5+ years</b>
U.S. agencies	\$ 4,431,673	710,548	530,018	3,089,970	101,137
Corporate bonds	2,061,327	50,866	92,881	1,587,788	329,792
	<u>\$ 6,493,000</u>	<u>761,414</u>	<u>622,899</u>	<u>4,677,758</u>	<u>430,929</u>

At June 30, 2009, The Med and The Med Foundation had investments in debt securities with the following maturities:

	<b>Fair value</b>	<b>Investment and restricted investment maturities (in years)</b>		
		<b>Less than 6 months</b>	<b>6 months to 1 year</b>	<b>1 – 5 years</b>
U.S. agencies	\$ 4,221,697	343,180	96,375	3,782,142
Corporate bonds	1,488,957	100,226	102,088	1,286,643
Discount notes	139,986	139,986	—	—
	<u>\$ 5,850,640</u>	<u>583,392</u>	<u>198,463</u>	<u>5,068,785</u>

At June 30, 2010 and 2009, The Med Foundation had one investment totaling \$778,387 and \$594,911, respectively, in the SEI Daily Income Trust Government Fund that represents 5% or more of total investments.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

At June 30, 2010, The Med's and The Med Foundation's corporate bonds, collectively, had the following credit ratings:

	<u>Fair value</u>	<u>Credit rating</u>
\$	48,582	BB+
	267,188	BBB-
	159,449	BBB
	456,229	BBB+
	268,681	A-
	569,756	A
	25,596	AA-
	61,038	AA+
	204,808	AAA
\$	<u>2,061,327</u>	

At June 30, 2009, The Med's and The Med Foundation's corporate bonds, collectively, had the following credit ratings:

	<u>Fair value</u>	<u>Credit rating</u>
\$	39,862	BB+
	154,766	BBB
	304,431	BBB+
	237,034	BBB-
	487,870	A
	204,424	A-
	60,570	AA+
\$	<u>1,488,957</u>	

The Med's and The Med Foundation's investments in discount notes at June 30, 2009 were not rated.

As of June 30, 2010, The Med's investment, per its investment policy, is to provide liquidity to fund ongoing operating needs and to act as a repository for both the accumulation of cash reserves needed to cushion economic down cycles and to provide cash earmarked for strategic needs.

The portfolio objectives of The Med, listed in order of importance, are as follows:

1. Preserve principal.
2. Maintain sufficient liquidity to meet forecasted cash needs.
3. Maintain a diversified portfolio in order to minimize credit risk.
4. Maximize yield subject to the above criteria.

## SHELBY COUNTY HEALTH CARE CORPORATION

(A Component Unit of Shelby County, Tennessee)

### Notes to Basic Financial Statements

June 30, 2010 and 2009

The authorized investments are as follows:

1. *Commercial Paper* – Any commercial paper issued by a domestic corporation with a maturity of 270 or less days that carries the highest rating by a recognized investor service, preferably Standard and Poor's and Moody's. Commercial paper shall not represent more than 50% of the portfolio.
2. *U.S. Treasury Securities* – U.S. Treasury notes, bills, and bonds with remaining maturities not to exceed one year. There is no upper limit restriction as to the maximum dollar amount or percentage of the portfolio that may be invested in U.S. Treasury securities.
3. *Bank Obligations* – Any certificate of deposit, time deposit, Eurodollar CD issued by a foreign branch of a U.S. bank, bankers' acceptance, bank note, or letter of credit issued by a (U.S.) bank possessing at least the second highest long-term debt rating from at least two recognized investor services, preferably Standard and Poor's and Moody's. Aggregate exposure to any bank may not exceed 20% of the portfolio. If aforementioned is not achieved, provision can be met by 100% collateralization by U.S. government securities.
4. *Repurchase Agreements* – Any Repurchase Agreement purchased from one of the top 25 U.S. banks or one of the primary dealers regulated by the Federal Reserve that is at least 102% collateralized by U.S. government obligations. Repurchase Agreements may not represent more than 20% of the portfolio.
5. *Funds* – Any open-end money market fund regulated by the U.S. government under Investment Company Act Rule 2a-7. Any investment fund regulated by a Registered Investment Advisor under Rule 3c-7. Such fund investment guidelines must state that "the fund will seek to maintain a \$1 per share net asset value." The Company's investment in any one fund may not exceed 10% of the assets of the fund into which it is invested.
6. *United States Government Obligations* – Any obligation issued or backed (federal agencies) by the U.S. government with a maturity of 24 months or less. No more than 25% may be invested in obligations of any one federal agency.

The Finance Committee of the Board of Directors meets regularly to review asset allocation, investment selection, portfolio performance, and overall adherence to the investment policy guidelines.

As of June 30, 2010, The Med Foundation utilized one investment manager. This manager is required to make investments in adherence to The Med Foundation's current investment policy and objectives.

In order to meet its needs, the investment strategy of The Med Foundation is to maximize total return (i.e., aggregate return from capital appreciation and dividend and interest income) while adhering to certain restrictions designed to promote a conservative portfolio.

Specifically, the primary objective of The Med Foundation investment management strategy is to maintain an investment portfolio designed to generate a high level of current income with above-average stability.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

Guidelines for investments and cash equivalents for The Med Foundation follow:

1. The Med Foundation's assets may be invested only in investment grade bonds rated Baa (or equivalent) or better as determined by Moody's Investor Service.
2. The overall market-weighted quality rating of the bond portfolio shall be no lower than A.
3. The Med Foundation's assets may be invested only in commercial paper rated P-2 (or equivalent) or better by Moody's Investor Service.
4. The market-weighted maturity of the base portfolio shall be no longer than 10 years.
5. Quality of the equity securities will be governed by the federal Employee Retirement and Income Security Act (ERISA), the Tennessee guidelines for investing trust funds, and the "prudent man rule."
6. Conservative option strategies may be used, with a goal of increasing the stability of the portfolio.

The Med Foundation limits investments in common stock to 40% of its investment portfolio. The remainder of the portfolio is to be invested in fixed income investments.

Investment income is comprised of the following:

	<b>2010</b>	<b>2009</b>
Dividend and interest income	\$ 391,495	963,435
Net increase (decrease) in the fair value of investments	63,895	(457,914)
	<b>\$ 455,390</b>	<b>505,521</b>

**(3) Business and Credit Concentrations**

The Med grants credit to patients, substantially all of whom are local area residents. The Med generally does not require collateral or other security in extending credit to patients; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies (e.g. Medicare, Medicaid, Blue Cross, and commercial insurance policies).

The mix of receivables from patients and third-party payors follows, before application of related valuation allowances:

	<b>2010</b>	<b>2009</b>
Commercial insurance	35%	31%
Patients	28	29
Medicaid/TennCare	26	29
Medicare	11	11
	<b>100%</b>	<b>100%</b>

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(4) Other Receivables**

The composition of other receivables follows:

	<b>2010</b>	<b>2009</b>
Accounts receivable from University of Tennessee Center for Health Services	\$ 1,233,612	1,274,864
Accounts receivable from the County	285,264	1,732,948
Accounts receivable from the State of Tennessee	6,328,736	5,132,957
Grants receivable	639,187	433,713
Other	1,515,286	1,349,227
	\$ 10,002,085	9,923,709

**(5) Other Current Assets**

The composition of other current assets follows:

	<b>2010</b>	<b>2009</b>
Inventories	\$ 3,812,504	4,044,685
Prepaid expenses	545,018	1,319,500
	\$ 4,357,522	5,364,185

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(6) Capital Assets**

Capital assets and related activity consist of the following:

	<b>Balances at July 1, 2009</b>	<b>Additions</b>	<b>Retirements</b>	<b>Transfers</b>	<b>Balances at June 30, 2010</b>
Capital assets not being depreciated:					
Construction in progress	\$ 1,735,031	583,542	(1,727,581)	(590,992)	—
Total book value of capital assets not being depreciated	<u>1,735,031</u>	<u>583,542</u>	<u>(1,727,581)</u>	<u>(590,992)</u>	<u>—</u>
Capital assets being depreciated:					
Land improvements	5,979,700	1,566	—	—	5,981,266
Buildings	65,236,701	—	—	—	65,236,701
Fixed equipment	104,615,645	406,075	—	—	105,021,720
Movable equipment	106,909,674	4,704,851	(245,159)	590,992	111,960,358
Software	13,511,221	325,122	—	—	13,836,343
Total book value of capital assets being depreciated	<u>296,252,941</u>	<u>5,437,614</u>	<u>(245,159)</u>	<u>590,992</u>	<u>302,036,388</u>
Less accumulated depreciation for:					
Land improvements	(5,116,611)	(117,822)	—	—	(5,234,433)
Buildings	(52,878,738)	(1,063,173)	—	—	(53,941,911)
Fixed equipment	(80,027,698)	(3,426,271)	—	—	(83,453,969)
Movable equipment	(87,332,417)	(6,268,148)	224,759	—	(93,375,806)
Software	(12,076,711)	(878,943)	—	—	(12,955,654)
Total accumulated depreciation	<u>(237,432,175)</u>	<u>(11,754,357)</u>	<u>224,759</u>	<u>—</u>	<u>(248,961,773)</u>
Capital assets being depreciated, net	<u>58,820,766</u>	<u>(6,316,743)</u>	<u>(20,400)</u>	<u>590,992</u>	<u>53,074,615</u>
Capital assets, net	<u>\$ 60,555,797</u>	<u>(5,733,201)</u>	<u>(1,747,981)</u>	<u>—</u>	<u>53,074,615</u>

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

	<b>Balances at July 1, 2008</b>	<b>Additions</b>	<b>Retirements</b>	<b>Transfers</b>	<b>Balances at June 30, 2009</b>
Capital assets not being depreciated:					
Construction in progress	\$ 1,610,658	135,097	—	(10,724)	1,735,031
Total book value of capital assets not being depreciated	1,610,658	135,097	—	(10,724)	1,735,031
Capital assets being depreciated:					
Land improvements	5,961,701	17,999	—	—	5,979,700
Buildings	65,236,701	—	—	—	65,236,701
Fixed equipment	104,438,869	173,852	—	2,924	104,615,645
Movable equipment	103,185,360	3,783,081	(64,617)	5,850	106,909,674
Software	13,399,150	110,121	—	1,950	13,511,221
Total book value of capital assets being depreciated	292,221,781	4,085,053	(64,617)	10,724	296,252,941
Less accumulated depreciation for:					
Land improvements	(4,983,314)	(133,297)	—	—	(5,116,611)
Buildings	(51,871,766)	(1,006,972)	—	—	(52,878,738)
Fixed equipment	(76,050,193)	(3,977,505)	—	—	(80,027,698)
Movable equipment	(80,583,700)	(6,813,334)	64,617	—	(87,332,417)
Software	(10,985,383)	(1,091,328)	—	—	(12,076,711)
Total accumulated depreciation	(224,474,356)	(13,022,436)	64,617	—	(237,432,175)
Capital assets being depreciated, net	67,747,425	(8,937,383)	—	10,724	58,820,766
Capital assets, net	\$ 69,358,083	(8,802,286)	—	—	60,555,797

**(7) Investments in Joint Ventures**

The composition of investments in joint ventures follows:

	<b>2010</b>	<b>2009</b>
Investment in Memphis Managed Care Corporation (MMCC)	\$ 441,193	2,440,000
Investment in Memphis Medical Center Air Ambulance Service, Inc. (MMCAAS)	—	4,652,667
	\$ 441,193	7,092,667

The Med is a 50% owner in MMCC, a TennCare managed care organization, with which The Med contracts to provide services to MMCC enrollees. MMCC is subject to certain regulatory minimum capital requirements, and in that respect, The Med has guaranteed capital deficiencies funding for MMCC up to

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

The Med's proportionate ownership interest in MMCC. No accrual for this obligation was required at either June 30, 2010 or 2009. During fiscal 2008 The Med and University of Tennessee Medical Group entered into a contract to sell the assets of MMCC to a publicly held managed care company and The Med received cash distributions of \$1,998,807 in fiscal 2010 and \$1,500,000 in fiscal 2009 from the liquidation of the assets of MMCC. No loss on the transaction is anticipated as the remaining assets are liquidated.

MMCAAS is a nonmember not-for-profit corporation organized to operate an air ambulance service for the transportation of medical supplies, equipment, and injured or sick persons. MMCAAS was organized by The Med and two other local healthcare systems. The Med appoints one-third of the board members of MMCAAS and is entitled to one-third of the net assets of MMCAAS in the event of dissolution. During fiscal 2010, management evaluated its investment in MMCAAS and determined that realization of the Med's investment in MMCAAS at dissolution was not probable. Accordingly, management considered the investment impaired and recorded a valuation allowance of approximately \$4,653,000 in fiscal 2010, which is included in nonoperating expenses other in the 2010 statement of revenues, expenses, and changes in net assets.

Separate audited financial statements for MMCC and MMCAAS are available and can be obtained by writing to the management of The Med at 877 Jefferson Avenue, Memphis, TN 38103 or by calling 901-545-7482.

**(8) Accrued Expenses and Other Current Liabilities**

The composition of accrued expenses and other current liabilities follows:

	<u>2010</u>	<u>2009</u>
Due to third-party payors	\$ 12,028,000	1,625,000
Compensated absences	6,844,120	7,034,780
Deferred grant revenue	476,156	5,534
Accrued payroll and withholdings	3,509,329	3,955,206
Accrued employee healthcare claims	1,770,000	1,762,000
Accrued interest	1,482,076	1,876,946
Current professional and general liability costs	2,500,000	2,750,000
	<u>\$ 28,609,681</u>	<u>19,009,466</u>

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(9) Amounts Payable to the County**

The County has allocated proceeds from certain prior bond issuances to assist in funding The Med's acquisition of capital assets. A summary of related amounts payable to the County follows:

	<b>2010</b>	<b>2009</b>
Installment notes payable in semiannual principal payments through August 1, 2009, plus interest of 6.5% due semiannually and at maturity	\$ —	539,335
Installment notes payable in annual principal payments through May 1, 2013, plus interest of 5.0% to 5.6% due annually	677,113	945,095
Installment notes payable in annual installments of \$524,326 at 5.25% interest (paid in fiscal 2010)	—	1,848,488
	677,113	3,332,918
Less current maturities	212,802	1,234,598
	\$ 464,311	2,098,320

A schedule of the changes in The Med's amounts payable to the County for 2010 and 2009 follows:

Description	Date of issuance	Balances at July 1, 2009	Additions	Payments	Balances at June 30, 2010	Due within one year
Notes payable - Shelby County	2/1/1988	\$ 539,335	—	(539,335)	—	—
Notes payable - Shelby County	5/1/1993	945,095	—	(267,982)	677,113	212,802
Notes payable - Shelby County	12/1/2002	1,848,488	—	(1,848,488)	—	—
		\$ 3,332,918	—	(2,655,805)	677,113	212,802
		3,332,918	—	(2,655,805)	677,113	212,802

  

Description	Date of issuance	Balances at July 1, 2008	Additions	Payments	Balances at June 30, 2009	Due within one year
Notes payable - Shelby County	2/1/1988	\$ 1,042,937	—	(503,602)	539,335	539,335
Notes payable - Shelby County	5/1/1993	1,145,629	—	(200,534)	945,095	267,983
Notes payable - Shelby County	12/1/2002	2,254,455	—	(405,967)	1,848,488	427,280
		\$ 4,443,021	—	(1,110,103)	3,332,918	1,234,598
		4,443,021	—	(1,110,103)	3,332,918	1,234,598

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

Future payments to the County as of June 30, 2010 follow:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Fiscal year:			
2011	\$ 212,802	501,276	714,078
2012	239,673	618,939	858,612
2013	224,638	643,090	867,728
	<u>\$ 677,113</u>	<u>1,763,305</u>	<u>2,440,418</u>

Interest paid was approximately \$759,000 and \$598,000 in 2010 and 2009, respectively.

**(10) Net Patient Service Revenue**

The Med has agreements with governmental and other third-party payors that provide for reimbursement to The Med at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between billings at established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursement with major third-party payors follows:

- *Medicare* – Substantially all acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Certain types of exempt services and other defined payments related to Medicare beneficiaries are paid based on cost reimbursement or other retroactive-determination methodologies. The Med is paid for retroactively determined items at tentative rates with final settlement determined after submission of annual cost reports by The Med and audits thereof by the Medicare fiscal intermediary.

The Med's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization. The Med's Medicare cost reports have been audited and settled by the Medicare fiscal intermediary through June 30, 2006. Revenue from the Medicare program accounted for approximately 17% and 20% of The Med's net patient service revenue for the years ended June 30, 2010 and 2009, respectively.

- *TennCare* – Under the TennCare program, patients traditionally covered by the State of Tennessee Medicaid program and certain members of the uninsured population enroll in managed care organizations that have contracted with the State of Tennessee to ensure healthcare coverage to their enrollees. The Med contracts with the managed care organizations to receive reimbursement for providing services to these patients. Payment arrangements with these managed care organizations consist primarily of prospectively determined rates per discharge, discounts from established charges, or prospectively determined per diem rates. Revenue from the TennCare program accounted for approximately 32% and 30% of The Med's net patient service revenue for the years ended June 30, 2010 and 2009, respectively.

The Med has historically received incremental reimbursement in the form of Essential Access payments through its participation in the TennCare Program. Amounts received by The Med under

## SHELBY COUNTY HEALTH CARE CORPORATION

(A Component Unit of Shelby County, Tennessee)

### Notes to Basic Financial Statements

June 30, 2010 and 2009

this program were approximately \$34.2 million and \$36.5 million in 2010 and 2009, respectively. These amounts have been recognized as reductions in related contractual adjustments in the accompanying statements of revenues, expenses, and changes in net assets. There can be no assurance that The Med will continue to qualify for future participation in this program or that the program will not ultimately be discontinued or materially modified. Any material reduction in such funds has a correspondingly material adverse effect on The Med's operations.

- *Arkansas Medicaid* – Substantially all inpatient and outpatient services rendered to Arkansas Medicaid program beneficiaries are paid under prospective reimbursement methodologies established by the State of Arkansas. Certain other reimbursement items (principally inpatient nursery services and medical education costs) are based upon cost reimbursement methodologies. The Med is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by The Med and audits thereof by the Arkansas Department of Health and Human Services (DHHS). The Med's Arkansas Medicaid cost reports have been audited and settled by the Arkansas DHHS through June 30, 2004. Revenue from the State of Arkansas Medicaid program accounted for approximately 1% of The Med's net patient service revenue for both the years ended June 30, 2010 and 2009, respectively.

The Med has historically received incremental reimbursement in the form of Upper Payment Limit (UPL) and Disproportionate Share payments through its participation in the State of Arkansas Medicaid program. The net benefit for The Med associated with this program, totaling approximately \$2,400,000 and \$23,000 for the years ended June 30, 2010 and 2009, respectively, has been recognized as a reduction in related contractual adjustments in the accompanying statement of revenues, expenses, and changes in net assets. There can be no assurance that The Med will continue to qualify for future participation in this program or that the program will not ultimately be discontinued or materially modified.

- *Mississippi Medicaid* – Inpatient and outpatient services rendered to Mississippi Medicaid program beneficiaries are generally paid based upon prospective reimbursement methodologies established by the State of Mississippi. Revenue from the State of Mississippi Medicaid program accounted for approximately 2% and 4%, respectively, of The Med's net patient service revenue for the years ended June 30, 2010 and 2009, respectively.

The Med has historically received incremental reimbursement in the form of Disproportionate Share and additional appropriation payments through its participation in the State of Mississippi Medicaid program. The net benefit for The Med associated with this program, totaling approximately \$3.6 million for the year ended June 30, 2010 has been recognized as a reduction in related contractual adjustments in the accompanying statement of revenues, expenses, and changes in net assets. No such amounts were received by The Med from this program for the year ended June 30, 2009.

- *Other* – The Med has also entered into other reimbursement arrangements providing for payment methodologies, which include prospectively determined rates per discharge, per diem amounts, and discounts from established charges.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

The composition of net patient service revenue follows:

	<b>2010</b>	<b>2009</b>
Gross patient service revenue	\$ 835,005,580	910,654,362
Less provision for contractual and other adjustments	478,088,787	570,566,548
Less provision for bad debts	105,880,094	76,442,323
Net patient service revenue	\$ 251,036,699	263,645,491

The composition of incremental reimbursement from various state agencies for participation in TennCare/Medicaid programs follows:

	<b>2010</b>	<b>2009</b>
TennCare Essential Access	\$ 34,229,596	36,481,293
Arkansas UPL/Disproportionate Share	2,436,043	23,401
Mississippi Disproportionate Share	3,562,019	—
Total payments	\$ 40,227,658	36,504,694

**(11) Charity Care**

The Med maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy. Charges foregone, based on established rates, were approximately \$250.7 million and \$295.3 million in 2010 and 2009, respectively. In 2008, the Med implemented processes to better identify and record its charity care, including a discount from standard charges for uninsured patients. Such discount is included in the charges forgone as The Med does not pursue collection and totaled approximately \$113.2 million and \$128.5 million in 2010 and 2009, respectively.

**(12) Retirement Plans**

*(a) Defined Benefit Plan*

The Med contributes to the Shelby County Retirement System (the Retirement System), a cost-sharing single-employer defined benefit public employee retirement system (PERS) established by Shelby County, Tennessee. The Retirement System is administered by a board, the majority of whose members are nominated by the Shelby County Mayor, subject to approval by the Shelby County Board of Commissioners. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the Shelby County Retirement System, Suite 950, 160 N. Main, Memphis, TN 38103 or calling 901-545-3570.

Shelby County provides office space and certain administrative services at no cost to the Retirement System. All other costs to administer the plan are paid from plan earnings.

## **SHELBY COUNTY HEALTH CARE CORPORATION**

(A Component Unit of Shelby County, Tennessee)

### Notes to Basic Financial Statements

June 30, 2010 and 2009

Substantially all full-time and permanent part-time employees of Shelby County (including The Med and Shelby County's other component units), other than the Shelby County Board of Education employees, employees who have elected to be covered by Social Security, employees designated as Comprehensive Employment Training Act employees after July 1, 1979, and certain employees of The Med are required, as a condition of employment, to participate in the Retirement System.

The Retirement System consists of three plans (Plans A, B, and C). In 1990, Plans A and B were merged into one reporting entity, whereby total combined assets of the merged plans are available for payment of benefits to participants of either of the two previously existing plans. In 2005, Plan C was added and merged with Plans A and B for funding purposes. While the plans were merged, the Retirement System has retained the membership criteria of the previous plans, which are as follows:

- Plan C, a contributory cost-sharing multiple-employer defined benefit pension plan for employees who are also eligible for Plan A,
- Plan B, a contributory cost-sharing multiple-employer defined benefit pension plan for employees hired prior to December 1, 1978, and
- Plan A, a noncontributory cost-sharing multiple-employer defined benefit pension plan for employees hired on or after December 1, 1978, and those employees that elected to transfer to Plan A from Plan B before January 1, 1981.

The Shelby County Board of Commissioners establishes the Retirement System's benefit provisions. Once a person becomes a participant, that person will continue to participate as long as he or she is an employee of Shelby County or The Med. The Retirement System provides retirement, as well as survivor and disability defined benefits.

The Retirement System's funding policy for employee contribution requirements is established by the Board of Administration of the Retirement System (the Board). The Shelby County Board of Commissioners establishes the Retirement System's funding policy for employer contribution requirements. For fiscal years 2010, 2009, and 2008, the employer contribution requirements were based on the actuarially determined contribution rates, which were 7.25%, 5.91%, and 5.30%, respectively.

The actuarially determined contribution rate was calculated using a projected unit credit service prorata cost method for Plan A, Plan B, and Plan C participants.

For fiscal 2010, The Med contributed \$495,711 under Plan A, \$375 under Plan B, and \$224,122 under Plan C. Employees contributed \$213 under Plan B and \$119,831 under Plan C. For fiscal 2009, The Med contributed \$343,155 under Plan A, \$283 under Plan B, and \$53,188 under Plan C. Employees contributed \$167 under Plan B and \$83,842 under Plan C. For fiscal 2008, The Med contributed \$359,789 under Plan A, \$6,369 under Plan B, and \$41,978 under Plan C. Employees contributed \$3,916 under Plan B and \$83,956 under Plan C. The contributions as a percentage of earned compensation were the same as those for the Retirement System. The Med contributed 100% of its required contributions in 2010, 2009, and 2008.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(b) Defined Contribution Plan**

Effective July 1, 1985, The Med established, under the authority of its Board of Directors, The Regional Medical Center at Memphis Retirement Investment Plan, a defined contribution pension plan covering employees 21 years of age and older who have completed one year of service, as defined, and are not participating in any other pension program to which The Med makes contributions. The plan provides for employee contributions of between 2% and 6% of compensation and for equal matching contributions made by The Med. Participants are immediately vested in their contributions plus actual earnings thereon. Participants vest 20% in the employers matching contributions after two years of service, 50% after three years, 75% after four years, and 100% after five years. Forfeitures are returned to The Med to reduce future matching contributions. For the defined contribution plan The Med contributed approximately \$2.1 million and \$3.6 million to the plan for years ended June 30, 2010 and 2009, respectively. Defined contribution plan participants contributed approximately \$2.8 million and \$4.1 million to the plan for years ended June 30, 2010 and 2009, respectively. The defined contribution plan ceased accepting contributions on September 30, 2009.

Effective October 1, 2009, The Med established, under the authority of its Board of Directors, The Regional Medical Center at Memphis 403(b) Retirement Plan, a defined contribution pension plan covering employees 21 years of age and older who have completed one year of service. The plan provides for a 50% employer match on employee contributions up to 6% of employee compensation. Participants are immediately vested in their contributions plus actual earnings thereon. Participants vest 20% in the employers matching contributions after two years of service, 50% after three years, 75% after four years, and 100% after five years. Forfeitures remain in the plan for the benefit of other participants. The Med contributed \$1.1 million to the 403(b) plan for the year ended June 30, 2010. 403(b) plan participants contributed approximately \$2.6 million to the 403(b) plan for the year ended June 30, 2010.

**(13) Postretirement Benefit Plan**

Regional Medical Center Healthcare Benefit Plan (the Plan) is a single-employer defined benefit healthcare plan sponsored and administered by The Med. The Plan provides medical and life insurance benefits to eligible retirees and their spouses. The Med's Board of Directors is authorized to establish and amend all provisions. The Med does not issue a publicly available financial report that includes financial statements and required supplementary information for the Plan.

During fiscal year 2010, The Med's Board of Directors approved a plan amendment which eliminated medical coverage for those employees who did not have 15 years of service as of December 31, 2009 and eliminated life insurance coverage for those employees retiring January 1, 2010 or later.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(a) Funding Policy**

The contribution requirements of employees and the Plan are established and may be amended by The Med's Board of Directors. Monthly contributions are required by retirees who are eligible for coverage. The Med pays for costs in excess of required retiree contributions. These contributions are assumed to increase based on future medical plan cost increases. For fiscal 2010 and 2009, The Med contributed approximately \$1,116,000 and \$1,591,000, respectively, net of retiree contributions, to the Plan. Plan members receiving benefits contributed approximately \$432,000 in fiscal 2010 and \$345,000 in fiscal 2009 through their required contributions. The following table summarizes the monthly contribution rates for the year beginning July 1, 2009:

	<b>Single</b>	<b>Family</b>
Pre-Medicare	\$ 1,200.00	1,257.00
Pre-Medicare Eligible	257.00	154.00

**(b) Annual OPEB Cost and Net OPEB Obligation**

The Med's annual other postemployment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period of 30 years. The following table shows the components of The Med's annual OPEB cost for fiscal 2010 and 2009, the amounts actually contributed to the Plan, and changes in The Med's net OPEB obligation:

	<b>2010</b>	<b>2009</b>
Annual required contributions and annual OPEB cost	\$ 1,330,635	1,831,095
Contributions made	1,115,635	1,591,095
Increase in net OPEB obligation	215,000	240,000
Net OPEB obligation, beginning of year	720,000	480,000
Net OPEB obligation, end of year	\$ 935,000	720,000

**(c) Three-Year Trend Information**

<b>Fiscal year ended</b>	<b>Annual OPEB cost</b>	<b>Percentage of annual OPEB cost contributed</b>	<b>Net OPEB obligation</b>
6/30/10	\$ 1,330,635	84%	\$ 935,000
6/30/09	1,831,095	87%	720,000
6/30/08	2,034,704	77%	480,000

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(d) Funded Status and Funding Progress – Required Supplementary Information**

As of July 1, 2009, the most recent actuarial valuation date, the plan was not funded. The actuarial accrued liability for benefits was \$24,769,964 resulting in an unfunded actuarial accrued liability (UAAL) of \$24,769,964.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, as presented below as required supplementary information, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

**(e) Schedule of Funding Progress – Required Supplementary Information**

Analysis of the Plan’s funding status follows:

Actuarial valuation date	Actuarial value of plan assets	Actuarial accrued liability (AAL)	Plan assets less than AAL	Funded ratio	Covered payroll	AAL as of a % of covered payroll
7/1/2009	\$ —	24,769,964	24,769,964	0.0%	\$ 67,042,048	36.9%
7/1/2008	—	25,656,247	25,656,247	0.0%	73,447,453	34.9%
7/1/2007	—	31,744,154	31,744,154	0.0%	88,236,389	36.0%

**(f) Actuarial Methods and Assumptions**

Projections of benefits for financial reporting purposes are based on the substantive plan (the Plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the July 1, 2009 actuarial valuation, the projected unit credit actuarial method was used. The actuarial assumptions included a 4% investment rate of return, which is a long-term rate of return on general account assets, and an annual inflation rate and annual healthcare cost trend rate of 9.0%, reducing each year until it reaches an annual rate of 4.5% in 2027. The UAAL is being amortized, using a level percent of pay method, over a 30-year period under the Projected Unit Credit Method.

**(14) Transactions with University of Tennessee Center for Health Services**

The Med contracts with University of Tennessee Center for Health Services (UTCHS) and University of Tennessee Medical Group (UTMG) to provide, among other things, The Med’s house staff, professional

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

supervision of certain ancillary departments and professional care for indigent patients. The Med also provides its facilities as a teaching hospital for UTCHS.

Operating expenses include approximately \$40.2 million in 2010 and \$41.3 million in 2009 for all professional and other services provided by UTCHS/UTMG.

**(15) Risk Management**

The Med has a self-insurance program for professional and general liability risks, both with respect to claims incurred after the effective date of the program and claims incurred but not reported prior to that date. The Med has not acquired any excess coverage for its self-insurance because The Med is afforded sovereign immunity in accordance with applicable statutes. Presently, sovereign immunity limits losses to \$300,000 per claim. The Med has recorded an accrual for self-insurance losses totaling approximately \$13.6 million and \$12.9 million at June 30, 2010 and 2009, respectively.

Incurred losses identified through The Med's incident reporting system and incurred but not reported losses are accrued based on estimates that incorporate The Med's current inventory of reported claims and historical experience, as well as considerations such as the nature of each claim or incident, relevant trend factors, and advice from consulting actuaries.

The following is a summary of changes in The Med's self-insurance liability for professional and general liability costs for fiscal 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Balance at July 1	\$ 12,880,000	10,049,000
Provision for claims reported and claims incurred but not reported	5,302,000	5,679,000
Claims paid	<u>(4,600,000)</u>	<u>(2,848,000)</u>
	13,582,000	12,880,000
Amounts classified as current liabilities	<u>(2,500,000)</u>	<u>(2,750,000)</u>
Balance at June 30	<u>\$ 11,082,000</u>	<u>10,130,000</u>

Like many other businesses, The Med is exposed to various risks of loss related to theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illness; and natural disasters. Commercial insurance coverage is purchased for claims arising from such matters. Claims settled through June 30, 2010 have not exceeded this commercial coverage in any of the three preceding years.

**SHELBY COUNTY HEALTH CARE CORPORATION**

(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

The following is a summary of changes in The Med's self-insurance liability for employee health coverage (included in accrued expenses and other current liabilities in the accompanying balance sheets) for fiscal 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Balance at July 1	\$ 1,762,000	2,143,000
Claims reported and claims incurred but not reported	10,623,050	9,984,963
Claims paid	<u>(10,615,050)</u>	<u>(10,365,963)</u>
Balance at June 30	<u>\$ 1,770,000</u>	<u>1,762,000</u>

**(16) Commitments**

The Med has outstanding service contracts for management services, equipment maintenance, and blood supply services. Estimated future payments under the contracts follow:

2011	\$ 3,915,516
2012	2,785,824
2013	<u>52,000</u>
	<u>\$ 6,753,340</u>

Expense under these contracts and other contracts was approximately \$9.9 million and \$11.6 million for the years ended June 30, 2010 and 2009, respectively.

**SHELBY COUNTY HEALTH CARE CORPORATION**  
(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

**(17) Leases**

The Med had a capital lease obligation with a vendor for clinical equipment with an original cost of \$1,850,000. The obligation was paid off during fiscal 2010.

A schedule of changes in The Med's capital lease obligation follows:

<u>Description</u>	<u>Date of lease</u>	<u>Balance July 1, 2009</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance June 30, 2010</u>	<u>Due within one year</u>
Omnicell, Inc.	10/1/2008	\$ 1,591,384		(1,591,384)	—	—

  

<u>Description</u>	<u>Date of lease</u>	<u>Balance July 1, 2008</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance June 30, 2010</u>	<u>Due within one year</u>
Omnicell, Inc.	10/1/2008	\$ —	1,850,000	(258,616)	1,591,384	354,822

The Med has entered into noncancelable operating leases for certain buildings and equipment. Rental expense for all operating leases was approximately \$5.0 million and \$6.1 million for the years ended June 30, 2010 and 2009, respectively. The future minimum payments under noncancelable operating leases as of June 30, 2010 follow:

2011	\$ 1,964,268
2012	539,055
2013	476,488
2014	192,186
2015	—
	<u>\$ 3,171,997</u>

**(18) Current Economic Environment**

The U.S. economy continues to suffer in many respects from ongoing characteristics associated with the downturn of the past several years. Management at The Med monitors economic conditions closely, both with respect to potential impacts on the healthcare provider industry and from a more general business perspective. While The Med was able to achieve certain objectives of importance in the current economic environment, management recognizes that economic conditions may continue to impact The Med in a number of ways, including (but not limited to) uncertainties associated with U.S. financial system reform and rising self-pay patient volumes and corresponding increases in uncompensated care.

## **SHELBY COUNTY HEALTH CARE CORPORATION**

(A Component Unit of Shelby County, Tennessee)

Notes to Basic Financial Statements

June 30, 2010 and 2009

Additionally, the general healthcare industry environment is increasingly uncertain, especially with respect to the impacts of the federal healthcare reform legislation which was passed in the spring of 2010. Potential impacts of ongoing healthcare industry transformation include, but are not limited to:

- Significant (and potentially unprecedented) capital investment in healthcare information technology (HCIT);
- Continuing volatility in the state and federal government reimbursement programs;
- Lack of clarity related to the health benefit exchange framework mandated by reform legislation, including important open questions regarding exchange reimbursement levels, changes in combined state/federal disproportionate share payments, and impact on the healthcare “demand curve” as the previously uninsured enter the insurance system;
- Effective management of multiple major regulatory mandates, including achievement of meaningful use of HCIT and the transition to ICD-10;
- Significant potential business model changes throughout the healthcare ecosystem, including within the healthcare commercial payor industry.

The business of healthcare in the current economic, legislative and regulatory environment is volatile. Any of the above factors and changes in appropriations from the County and City of Memphis, along with others both currently in existence and which may or may not arise in the future, could have a material adverse impact on The Med’s financial position and operating results.

## SHELBY COUNTY HEALTH CARE CORPORATION

Combining Schedule - Balance Sheet

June 30, 2010

<b>Assets</b>	<u>Shelby County Health Care Corporation</u>	<u>The Regional Medical Center at Memphis Foundation</u>	<u>Eliminations</u>	<u>Combined</u>
Current assets:				
Cash and cash equivalents	\$ 53,151,772	424,912	—	53,576,684
Investments	3,922,517	—	—	3,922,517
Patient accounts receivable, net	20,275,330	—	—	20,275,330
Other receivables	9,307,134	734,168	(39,217)	10,002,085
Other current assets	4,357,522	—	—	4,357,522
Total current assets	<u>91,014,275</u>	<u>1,159,080</u>	<u>(39,217)</u>	<u>92,134,138</u>
Restricted investments	—	5,235,876	—	5,235,876
Capital assets, net	53,074,615	—	—	53,074,615
Investments in joint ventures	441,193	—	—	441,193
Total assets	<u>\$ 144,530,083</u>	<u>6,394,956</u>	<u>(39,217)</u>	<u>150,885,822</u>
<b>Liabilities and Net Assets</b>				
Current liabilities:				
Accounts payable	\$ 7,005,644	—	(39,217)	6,966,427
Accrued expenses and other current liabilities	28,601,561	7,820	—	28,609,381
Current installments of amounts payable to Shelby County	212,802	—	—	212,802
Total current liabilities	<u>35,820,007</u>	<u>7,820</u>	<u>(39,217)</u>	<u>35,788,610</u>
Amounts payable to Shelby County, excluding current installments	464,311	—	—	464,311
Accrued professional and general liability costs	11,082,000	—	—	11,082,000
Net postemployment benefit obligation	935,000	—	—	935,000
Total liabilities	<u>48,301,318</u>	<u>7,820</u>	<u>(39,217)</u>	<u>48,269,921</u>
Net assets:				
Invested in capital assets, net of related debt	52,397,502	—	—	52,397,502
Restricted for:				
Capital assets	—	4,372,870	—	4,372,870
Indigent care	—	651,783	—	651,783
Unrestricted	43,831,263	1,362,483	—	1,362,483
Total net assets	<u>96,228,765</u>	<u>6,387,136</u>	<u>—</u>	<u>102,615,901</u>
Commitments and contingencies				
Total liabilities and net assets	<u>\$ 144,530,083</u>	<u>6,394,956</u>	<u>(39,217)</u>	<u>150,885,822</u>

See accompanying independent auditors' report.

## SHELBY COUNTY HEALTH CARE CORPORATION

Combining Schedule - Statement of Revenues, Expenses and Changes in Net Assets

June 30, 2010

	Shelby County Health Care Corporation	The Regional Medical Center at Memphis Foundation	Eliminations	Combined
Operating revenues:				
Net patient service revenue	\$ 251,036,699	—	—	251,036,699
Other revenue	9,359,876	584,438	—	9,944,314
Total operating Revenues	<u>260,396,575</u>	<u>584,438</u>	<u>—</u>	<u>260,981,013</u>
Operating expenses:				
Salaries and benefits	131,437,995	—	—	131,437,995
Supplies and services	58,655,297	—	—	58,655,297
Physician and professional fees	33,003,305	—	—	33,003,305
Purchased medical services	13,266,244	—	—	13,266,244
Plant operations	11,208,352	—	—	11,208,352
Insurance	6,946,579	—	—	6,946,579
Administrative and general	14,245,261	382,640	—	14,627,901
Community services	382,640	—	—	382,640
Depreciation and amortization	11,754,357	—	—	11,754,357
Total operating expenses	<u>280,900,030</u>	<u>382,640</u>	<u>—</u>	<u>281,282,670</u>
Operating loss	<u>(20,503,455)</u>	<u>201,798</u>	<u>—</u>	<u>(20,301,657)</u>
Nonoperating revenues (expenses):				
Interest expense	(364,280)	—	—	(364,280)
Investment income	180,872	274,518	—	455,390
Appropriations from Shelby County	30,616,666	—	—	30,616,666
Other	(6,398,238)	—	—	(6,398,238)
Total nonoperating revenues, net	<u>24,035,020</u>	<u>274,518</u>	<u>—</u>	<u>24,309,538</u>
Income before capital appropriations	3,531,565	476,316	—	476,316
Capital appropriations from City of Memphis	<u>2,000,000</u>	<u>—</u>	<u>—</u>	<u>2,000,000</u>
Increase in net assets	5,531,565	476,316	—	6,007,881
Net assets, beginning of year	<u>90,697,200</u>	<u>5,910,820</u>	<u>—</u>	<u>96,608,020</u>
Net assets, end of year	<u>\$ 96,228,765</u>	<u>6,387,136</u>	<u>—</u>	<u>102,615,901</u>

See accompanying independent auditors' report.