Consolidated Financial Statements and Schedules

West Tennessee Healthcare and Related Affiliates
Years Ended June 30, 2010 and 2009
With Report of Independent Certified Public Accountants

Ernst & Young LLP

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Years Ended June 30, 2010 and 2009

Contents

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Report of Independent Certified Public Accountants

The Board of Trustees
West Tennessee Healthcare

We have audited the accompanying financial statements of the business-type activities of West Tennessee Healthcare and Related Affiliates (the Company), as of and for the years ended June 30, 2010 and 2009, which collectively comprise the Company's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Company's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States 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. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included 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 Company'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 and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the Company as of June 30, 2010 and 2009, and the changes in financial position and cash flows thereof 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 October 25, 2010, on our consideration of the Company'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 management's discussion and analysis on pages 3 through 10 and the required pension and post employment benefits disclosure information on pages 43 through 45 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. 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 performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards and state financial assistance is 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 is 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.

Ernst & Young LLP

October 25, 2010

West Tennessee Healthcare and Related Affiliates

Management's Discussion and Analysis

Years Ended June 30, 2010 and 2009

This section of the financial statements of West Tennessee Healthcare and Related Affiliates (the Company) presents management's analysis of the Company's financial performance during the fiscal year ended June 30, 2010.

Financial Highlights

2010

- The Company posted a 2% operating margin for the year, an improvement over the prior year, despite lower inpatient volume.

- Total operating revenues increased by 3% compared to the prior year. The growth is attributed to growth in outpatient services as emergency room visits for the flagship hospital increased by 2% over the prior year and increases in various other outpatient services were realized. In addition, other operating revenues were driven up significantly with non-recurring contributions and gains on asset sales.

- Total operating expenses were flat compared with the prior year.

- The Company posted a substantial improvement in non-operating revenue during the fiscal year, with a turnaround in the value of investments. In addition, fiscal year 2009 non-operating revenue was abnormally low with non-recurring losses for that year.

2009

- The Company posted a negative operating margin for the year of 1.2% as volumes for the flagship hospital waned while the Company experienced routine increases in expense and significant one-time and ongoing new expense related to the opening of a new bed tower and debt re-issuance.

- In addition to realizing the impact of physician clinics purchased late in the previous fiscal year, the Company made several service changes during the year. Among them were the establishment of several new physician practices and the transition of home health services to a joint venture arrangement. In addition, skilled nursing services were discontinued through the sale of West Tennessee Transitional Care.

- Total operating revenues increased by 2% compared to the prior year. The growth is attributed to the service changes noted above as well as growth in revenues for services outside the flagship hospital.

- Total operating expenses, excluding interest costs, increased by 5% over the prior year with market adjustments for employees and routine increases in supply costs. In addition, the opening of a new/replacement bed tower drove substantial increases in depreciation and utilities costs as well as some one-time operating costs associated with the transition to the new space.

- The Company incurred substantial non-operating expense during the fiscal year, primarily due to a $35.7 million deterioration in the value of investments. In addition, the Company incurred $18.9 million in interest expense, and a one-time loss of $18.9 million that resulted from the August 2008 fixed rate bond issue and the termination of the interest rate swap agreements related to the refunding of the organization's auction and variable rate debt.

- The Company's bond ratings continue to be positive and consistent, with Moody's assigning a rating of "A1" at the time of the issuance of the Series 2008 bonds and Standard & Poor's assigning an "A+" which was reaffirmed in July of 2009.

Overview of the Consolidated Financial Statements

The financial statements consist of two parts: management's discussion and analysis and the basic financial statements. The basic financial statements also include notes and required supplementary information that explain in more detail some of the information in the financial statements.

Required Basic Consolidated Financial Statements

The Company reports financial information about the Company using accounting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information about its activities. The consolidated balance sheets include all of the Company's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to Company creditors (liabilities). The assets and liabilities are presented in a classified format, which distinguishes between current and long-term assets and liabilities. These statements also provide the basis for computing rate of return, evaluating the capital structure of the Company and assessing the liquidity and financial flexibility of the Company.

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

The final required statement is the consolidated statement of Cash Flows. The primary purpose of this statement is to provide information about the Company's cash receipts and cash payments during the reporting period. The statement reports cash receipts, cash payments, and net changes in cash resulting from operating, investing, non-capital financing and financing activities, and provides information as to where cash came from, what cash was used for, and what the change in the cash balance was during the reporting period.

Financial Analysis

Our analysis of the financial statements of the Company begins below. One of the most important questions asked about the Company's finances is "Is the Company as a whole better off or worse off as a result of the year's activities?" The consolidated balance sheet and the consolidated Statement of revenues, expenses, and changes in net assets report information about the Company's activities in a way that will help answer this question. These statements report the net assets of the Company and changes in them. You can think of the Company'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 Company's net assets are one indicator of whether its financial health is improving or deteriorating. However, you will need to consider other non-financial factors such as changes in interest rates, economic conditions, regulations and new or changed government legislation.

Net Assets

A summary of the Company's consolidated balance sheets is presented in Table A-1.

Table A-1

Condensed Consolidated Balance Sheets (in millions of dollars)

	June 30 2010	2009	2008	Dollar Increase (Decrease) 2009-2010	Percentage Increase (Decrease) 2009-2010	Dollar Increase (Decrease) 2008-2009	Percentage Increase (Decrease) 2008-2009
Current assets	**$ 120.0**	$ 134.0	$ 114.8	$ (14.0)	(10)%	$ 19.20	17%
Capital assets, net	**421.7**	434.3	399.2	(12.6)	(2)	35.1	9
Other long-term assets	**284.1**	229.0	275.0	55.0	24	(46.0)	(17)
Total assets	**$ 825.8**	$ 797.3	$ 789.0	$ 28.5	4%	$ 8.3	1%
Current liabilities	**$ 70.5**	$ 72.1	$ 66.4	$ (1.6)	(2)%	$ 5.7	9%
Long-term liabilities	**295.4**	300.0	229.2	(4.6)	(2)	70.8	31
Total liabilities	**365.9**	372.1	295.6	(6.2)	(2)	76.5	26
Invested in capital assets, net of related financing	**$ 141.8**	$ 148.8	$ 230.7	(7.0)	(4)	(81.9)	(36)
Restricted	**27.2**	27.2	1.1	–	0	26.1	2372
Unrestricted	**290.9**	249.2	261.6	41.7	17	(12.4)	(5)
Total net assets	**459.9**	425.2	493.4	34.7	13	(68.2)	(14)
Total liabilities and net assets	**$ 825.8**	$ 797.3	$ 789.0	$ 28.5	4%	$ 8.3	1%

As indicated in Table A-1, net assets increased from fiscal 2009 by $34.7 million or 13% with the Company's financial performance in fiscal year 2010.

1. Total assets increased by $28.5 million or 4% due primarily to the turnaround in the value of the Company's investment portfolio.

2. Total liabilities decreased by $6.2 million or 2% with the routine decrease in the balance of outstanding debt and a less significant decline in other accrued expenses.

As indicated in Table A-1, net assets decreased from fiscal 2008 by $68.2 million or 14% with the Company's financial performance in fiscal year 2009.

1. Total assets increased by $8.3 million or 1% with proceeds from the bond issue in August. As a result of the capital markets crises that began in fiscal year 2008, the District issued $318,980,000 of Series 2008 Hospital Revenue Refunding and Improvement Bonds in August 2008. With this issue, the District refunded all existing auction rate and variable rate debt. A portion was used to establish a debt service reserve fund.

2. Total liabilities increased by $76.5 million or 26% primarily due to the bond issue in August 2008.

Table A-2

Condensed Consolidated Statements of Revenues, Expenses and Changes in Net Assets (in millions of dollars)

	Year Ended June 30 2010	2009	2008	Dollar Increase (Decrease) 2009-2010	Percentage Increase (Decrease) 2009-2010	Dollar Increase (Decrease) 2008-2009	Percentage Increase (Decrease) 2008-2009
Net patient service revenues	**$ 529.2**	$ 519.4	$ 510.1	$ 9.8	2%	$ 9.3	2%
Other operating revenues	**40.0**	33.2	33.0	6.8	20	0.2	1
Total operating revenues	**569.2**	552.6	543.1	16.6	3	9.5	2
Salaries and benefits	**292.6**	302.5	288.9	(9.9)	(3)	13.6	5
Supply expenses	**115.9**	113.3	110.5	2.6	2	2.8	3
Other expenses	**131.0**	124.6	118.1	6.4	5	6.5	6
Total expenses	**539.5**	540.4	517.5	(0.9)	0	22.9	4
Income from operations	**29.7**	12.2	25.6	17.5	143	(13.4)	(52)
Net nonoperating revenues and expenses	**6.1**	(73.5)	(15.4)	79.6	(108)	(58.1)	377
Change in net assets	**35.8**	(61.3)	10.2	97.1	(158)	(71.5)	(701)
Beginning net assets	**425.2**	487.4	482.5	(62.2)	(13)	(4.9)	(1)
Less contributions	**(1.1)**	(0.9)	(5.3)	(0.2)	23	4.4	(83)
Ending net assets	**$ 459.9**	$ 425.2	$ 487.4	$ 34.7	9%	$ (62.2)	(12)%

While the consolidated balance sheets show the change in financial position or net assets, the consolidated statements of revenues and expenses and changes in net assets, as indicated above, provide answers as to the nature and source of these changes (i.e., the financial result of current year operations).

Operating revenues increased by 3% from 2009 to 2010. The increase was driven primarily by increases in outpatient revenue and other operating revenue, as follows:

1. Although inpatient volumes were down from the previous year, the Company experienced growth in outpatient volume, both for emergency services, with visits up 2% at the flagship hospital, and other outpatient services. Increases in non-emergent outpatient volumes were most pronounced for cardiology and gastrointestinal services.

2. Other operating revenue increased significantly over the prior year, driven primarily by revenue derived from non-recurring transactions. The Company received a contribution of $2.5 million in June 2010 toward the development of a Cancer Center. In addition, the Company realized gains on certain asset sales during the year.

Operating expense remained flat when comparing 2009 to 2010.

1. Total salaries and benefits expense decreased by 3% from the prior year as the Company's staffing levels (measured in paid full-time-equivalent employees, or FTEs) decreased by 2% and employee benefit costs decreased by 10%. The decrease in staffing levels was driven primarily by changes in services from the previous year and the Company's efforts to curb hiring and otherwise control staffing costs. Although the Company did not award a salary increase for employees during the year, a one-time bonus was awarded.

2. Total supply cost for the Company increased by 2% from the prior year driven largely by the increase in cardiology volume and an increase in pharmaceutical costs resulting from growth in chemotherapy volume and increased utilization and cost of drugs overall.

3. Other expenses increased by 5% from the prior year with the following notable changes:

    a. Depreciation expense increased by 8% or $3.9 million due to routine additions of property, plant and equipment.

    b. Administrative and other expenses increased by 3.3% or $2.5 million over the prior year, with routine costs escalation and non-recurring losses on asset sales, etc.

Operating revenues increased by 2% from 2008 to 2009. The increase was driven primarily by service changes and revenue growth outside the flagship hospital, as noted below:

1. At the flagship hospital, revenues were flat compared to the prior year as routine increases in reimbursement were offset by volume declines.

2. Several changes were made during the year which contributed to an increase in revenue over the prior year. In addition to realizing the full impact of several clinic purchases made late in the previous fiscal year, the Company purchased or established several new practices during the year. The Company also entered into a joint venture arrangement for Home Health services which contributed to increased revenue.

3. Outside the flagship hospital, routine increases in reimbursement combined with some volume increases generated revenues in excess of prior year.

Operating expense increased by 4% from 2008 to 2009.

1. Total salaries and benefits expense for the system increased by 5%. The Company's staffing levels as measured by total paid full-time-equivalent employees (FTEs) increased by 2% driving a portion of the increase. The remainder of the increase was driven by adjustments to salaries (merit and market-based salary adjustments in the first quarter of 2009) and routine growth of health plan claims cost. These increases were offset by the

Company's efforts to control and reduce cost with reduced volumes. The most significant of these efforts included the discontinuation of employer matching for employee 403(b) plan contributions in February. In addition, the Company instituted controls to curb the rate of hiring, increase productivity and reduce the usage of premium pay.

2. Total supply cost for the system increased by 3% from the prior year driven largely by increases in pharmaceutical costs. In addition to inflation of drug costs beyond expectations, the Company experienced an increase in utilization of certain high-cost drugs.

3. Other expenses increased by 6% from 2008 to 2009 with the following notable changes:

   a. Depreciation expense increased by 17% or $6.8 million. With the completion of the major construction project for a replacement bed tower, the Company took on a significant increase in depreciation expense early in the fiscal year.

   b. Administrative and other expenses increased by 2.5% or $1.9 million over the prior year, primarily driven by an increase in utilities cost of $2.7 million with increases in rates and a substantial increase in cost for the flagship hospital with the opening of the new bed tower.

Significant nonoperating expense totaling $73.5 million was incurred with the combination of $35.7 million in market-driven investment losses and certain debt transactions described below.

1. In August 2008, the District issued $318,980,000 of Series 2008 Hospital Revenue Refunding and Improvement Bonds. With this issue, the District refunded all existing auction rate and variable rate debt.

2. The District realized increased interest expense over the prior year, $18,863,711 in total, primarily due to the higher interest rate on the new fixed rate bond issue.

3. In connection with the August 2008 bond issue and refunding of all auction rate and variable rate debt, the District also terminated all interest rate swap agreements. The cost and one-time expense of such terminations totaled $18,912,223.

Capital Assets and Long-Term Debt

Capital Assets

As of June 30, 2010, the Company had $421.7 million invested in a variety of capital assets, as reflected in Table A-3, which represents a net decrease (additions, disposals and depreciation) of $12.6 million or 2% from the end of last year. Construction in progress includes costs for an emergency room renovation at an affiliate hospital and renovations to the main campus.

Table A-3

Capital Assets (In millions of dollars)

	June 30	
	2010	**2009**
Land and land improvements	**$ 44.2**	$ 42.6
Buildings	**275.8**	255.9
Equipment	**529.8**	496.7
Construction in progress	**4.2**	23.8
Total capital assets	**854.0**	819.0
Accumulated depreciation	**(432.3)**	(384.7)
Capital assets, net	**$ 421.7**	$ 434.3

Long-Term Debt

As of June 30, 2010, the Company had $295.4 million in outstanding long-term debt and as of June 30, 2009, the Company had $300.0 million in outstanding long-term debt. This represents a net decrease of $5 million over the prior fiscal year.

For more detailed information regarding the Company's capital assets and long-term debt, please refer to the notes to the financial statements.

Future Outlook

The Board of Trustees and management have a positive outlook for the Company. The Company continues its efforts to control costs and improve operating efficiency to raise margins and strengthen its financial position for the future. In addition, the Company has re-focused attention on improving quality and patient satisfaction to further its mission and strengthen its financial position.

Requests for Information

This financial report is designed to provide a general overview of the Company's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Company.

West Tennessee Healthcare and Related Affiliates

Consolidated Balance Sheets

	June 30 2010	June 30 2009
Assets		
Current assets:		
Cash and cash equivalents	**$ 25,168,148**	$ 28,326,492
Accounts receivable:		
Patient accounts receivable	**72,342,634**	84,436,643
Other	**6,033,629**	4,445,592
Total accounts receivable	**78,376,263**	88,882,235
Inventories	**5,788,126**	5,339,277
Prepaid expenses	**4,995,901**	5,773,854
Assets limited as to use – current portion – restricted	**5,694,454**	5,737,858
Total current assets	**120,022,892**	134,059,716
Assets limited as to use:		
Funded depreciation-buildings	**39,232,756**	28,943,383
Funded depreciation-equipment	**21,094,517**	15,562,167
Debt service reserve fund- restricted	**21,494,449**	21,468,359
Project building fund	**81,677,043**	55,310,965
Operating reserve fund	**88,430,696**	78,569,001
Contingency fund	**6,872,279**	6,077,501
High technology fund	**8,159,372**	7,215,742
	266,961,112	213,147,118
Other assets:		
Unamortized bond issue costs	**2,283,679**	2,396,847
Other	**14,772,509**	13,473,686
	17,056,188	15,870,533
Property, plant, and equipment:		
Land and land improvements *(See Note 12)*	**44,231,507**	42,616,153
Buildings	**275,803,414**	255,914,662
Fixed equipment	**186,429,872**	170,848,174
Moveable equipment	**343,309,352**	325,817,417
Construction in progress	**4,247,262**	23,841,942
	854,021,407	819,038,348
Accumulated depreciation	**(432,282,019)**	(384,760,214)
	421,739,388	434,278,134
Total assets	**$ 825,779,580**	$ 797,355,501

	June 30	
	2010	**2009**
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 16,347,501**	$ 17,234,267
Accrued compensation and related expenses	**20,724,842**	19,891,437
Accrued interest expense	**4,273,656**	4,327,042
Other accrued expenses	**23,111,872**	23,934,007
Long-term debt due within one year	**5,976,315**	6,723,672
Total current liabilities	**70,434,186**	72,110,425
Other liabilities:		
Long-term debt, less amounts due within one year	**295,400,562**	300,035,676
Net assets:		
Unrestricted *(See Note 12)*	**290,897,517**	249,175,326
Invested in capital assets, net of related financing *(See Note 12)*	**141,858,412**	148,827,857
Restricted for debt service	**27,188,903**	27,206,217
Total net assets *(See Note 12)*	**459,944,832**	425,209,400
Total liabilities and net assets	**$ 825,779,580**	$ 797,355,501

See accompanying notes.

West Tennessee Healthcare and Related Affiliates

Consolidated Statements of Revenues and Expenses and Changes in Net Assets

	Year Ended June 30	
	2010	**2009**
Operating revenues		
Net patient service revenues	**$ 529,207,832**	$ 519,406,705
Other revenues	**39,999,195**	33,181,011
Total operating revenues	**569,207,027**	552,587,716
Operating expenses		
Salaries and benefits	**292,536,087**	302,529,385
Supplies and other	**195,608,646**	190,388,299
Depreciation and amortization	**51,293,402**	47,437,696
Total operating expenses	**539,438,135**	540,355,380
Income from operations	**29,768,892**	12,232,336
Nonoperating revenues (expenses)		
Investment income (loss)	**24,454,529**	(35,702,189)
Interest expense	**(18,364,589)**	(18,863,711)
Nonoperating revenue (expenses) before loss on swap termination	**6,089,940**	(54,565,900)
Loss on swap termination	**–**	(18,912,223)
Income (loss) before capital contributions	**35,858,832**	(61,245,787)
Other changes in net assets		
Contribution to City of Jackson & Madison County	**(400,000)**	(400,000)
Contribution to City of Jackson: Sportsplex	**(150,000)**	(150,000)
Contribution to City of Jackson: Skyline Drive	**(85,337)**	–
Contribution to City of Jackson: Jackson Revitalization	**(100,000)**	–
Contribution to West Tennessee Healthcare Foundation	**(388,063)**	(348,063)
Net assets at beginning of year *(See Note 12)*	**425,209,400**	487,353,250
Net assets at end of year *(See Note 12)*	**$ 459,944,832**	$ 425,209,400

See accompanying notes.

West Tennessee Healthcare and Related Affiliates

Consolidated Statements of Cash Flows

	Year Ended June 30 2010	2009
Operating activities		
Receipts from third party payors and patients	**$ 579,712,999**	$ 554,580,445
Payments to suppliers	**(198,562,061)**	(198,482,567)
Payments to employees	**(291,702,683)**	(300,975,463)
Net cash provided by operating activities	**89,448,255**	55,122,415
Noncapital financing activity		
Contributions to City of Jackson and Madison County	**(1,123,400)**	(898,063)
Net cash used in noncapital financing activity	**(1,123,400)**	(898,063)
Investing activities		
Interest, dividends, and realized gain on investments	**4,089,288**	5,370,325
Net change in assets limited as to use	**(33,405,348)**	24,351,202
Net cash (used in) provided by investing activities	**(29,316,060)**	29,721,527
Capital and related financing activities		
Purchases of property, plant, and equipment	**(38,479,862)**	(88,268,428)
Proceeds from 2008 bond issuance	**–**	306,759,348
Establishment of debt service reserve	**–**	(21,299,713)
Repayment of long-term debt	**(5,382,471)**	(233,351,283)
Interest paid on long-term debt	**(18,304,806)**	(12,668,813)
Termination of interest rate swap instruments	**–**	(18,912,223)
Net cash used in capital and related financing activities	**(62,167,139)**	(67,741,112)
(Decrease) increase in cash and cash equivalents	**(3,158,344)**	16,204,767
Cash and cash equivalents at beginning of year	**28,326,492**	12,121,725
Cash and cash equivalents at end of year	**$ 25,168,148**	$ 28,326,492
Reconciliation of income from operations to net cash provided by operating activities		
Income from operations	**$ 29,768,892**	$ 12,232,336
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Depreciation	**51,018,609**	47,223,872
Amortization	**274,793**	213,824
Changes in operating assets and liabilities:		
Accounts receivable	**10,505,972**	1,992,729
Inventory and prepaid expenses	**329,104**	(364,762)
Other assets	**(1,573,618)**	(6,238,297)
Accounts payable and accrued expenses	**(875,497)**	62,713
Net cash provided by operating activities	**$ 89,448,255**	$ 55,122,415
Supplemental schedule of noncash investing activities		
Change in fair value of investments	**$ 20,365,242**	$ (41,072,513)

See accompanying notes.

1. Significant Accounting Policies

Organization and Basis of Presentation

The accompanying consolidated financial statements include West Tennessee Healthcare and its related affiliates (hereinafter collectively referred to as the Company), all of which are under common control of the Jackson-Madison County General Hospital District (the District) and have been presented as blended component units of the Company. The Company presents its financial statements in accordance with generally accepted accounting principles and financial reporting standards. All significant intercompany balances and transactions have been eliminated in consolidation.

Proprietary Fund Accounting

The Company utilizes the proprietary fund method of accounting whereby revenues and expenses are recognized on an accrual basis. Substantially all revenues and expenses are subject to accrual.

Accounting Standards

Government Accounting Standard Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, offers the option of following all Financial Accounting Standards Board (FASB) standards issued after November 30, 1989, unless the latter conflict with or contradict GASB pronouncements, or not following FASB standards issued after such date. The Company elected the option not to follow FASB pronouncements issued after November 30, 1989.

Recent Accounting Pronouncements

In June 2008, the GASB issued GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This statement intended to improve how state and local governments report information about derivative instruments-financial arrangements used by governments to manage specific risks or make investments-in their financial statements. 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 guidance in this Statement also addresses hedge accounting requirements and is effective for financial statements for reporting periods beginning after June 15, 2009 (July 1, 2009 for the Company).

1. Significant Accounting Policies (continued)

The new standard provides specific criteria that governments will use to determine whether a derivative instrument results in an effective hedge. Changes in fair value for effective hedges that are achieved with derivative instruments will be recognized in the reporting period to which they relate. The changes in fair value of these hedging derivative instruments do not affect current investment revenue, but are instead reported as deferrals in the statement of net assets or the balance sheet. Derivative instruments that either do not meet the criteria for an effective hedge or are associated with investments that are already reported at fair value are classified as investment derivative instruments for financial reporting purposes. Changes in fair value of those derivative instruments are reported as part of investment revenue in the current reporting period. The statement also improves disclosures, providing a summary of the government's derivative instrument activity, its objectives for entering into derivative instruments, and their significant terms and risks. Adoption of this statement did not have a material impact on the Company's results of operations or financial position.

On July 1, 2008, the Company adopted the provisions of GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations* (GASB 49). This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the document excludes pollution prevention or control obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and post closure care and nuclear power plant decommissioning. Once any one of five specified obligating events occurs (specified within GASB 49), a government is required to estimate the components of expected pollution remediation outlays and determine whether outlays for those components should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired. The adoption of this statement did not have an impact on the Company's results of operations or financial position.

Cash and Cash Equivalents

The Company considers temporary cash investments with a maturity of three months or less when purchased to be cash and cash equivalents.

1. Significant Accounting Policies (continued)

Investments

The Company's investments are reported at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools.* The Company invests in government bonds, short-term money market investments, equity securities and alternative investments that are in accordance with the Company's investment policy.

Investments include the Company's ownership interest in various limited partnerships and investment funds (collectively referred to as Funds) that, in turn, invest the capital of the Funds in other funds. These Funds have no significant liabilities, and the equity of the Funds is based upon the fair value of the financial instruments held. One of the Company's seven Funds invests directly in other funds that, in turn, invest primarily in financial instruments that are readily marketable in various public markets. The remaining six Funds invest in real estate, hedge funds, and limited partnerships. The fair value of these investments is determined by the underlying asset's manager or independent appraisals (in the case of real estate). Due to inherent uncertainty of these estimates, these values may differ materially from the values that would have been used had a ready market for these investments existed.

The calculation of realized gains and losses is independent of a calculation of the net change in the fair value of investments. Realized gains and losses on investments that had been held in more than one fiscal year and sold in the current year were included as a change in the fair value of investments reported in the prior year and the current year. Realized and unrealized gains and losses are included in investment income in the accompanying consolidated statements of revenues and expenses and changes in net assets.

Inventories

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

Funded Depreciation

The Company reserves funds for future purchases of property, plant and equipment. Investment earnings on funded depreciation funds were $829,678 and $893,328 for the years ended June 30, 2010 and 2009, respectively, and are classified as investment income in the accompanying consolidated statements of revenues and expenses and changes in net assets.

1. Significant Accounting Policies (continued)

Bond Issue Costs and Discounts

Bond issue costs and discounts are amortized over the life of the related bonds by the interest method. Such amortization is included in interest expense in the accompanying consolidated statements of revenues and expenses and changes in net assets.

Property, Plant, and Equipment

Property, plant, and equipment are recorded on the basis of cost. Provisions for depreciation are computed by the straight-line method based on the estimated useful lives of the assets.

Fair Value of Financial Instruments

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable and accounts payable approximate fair value because of the short-term maturity of these instruments. The carrying amounts of the Company’s long-term debt instruments approximate fair value.

Compensated Absences

The Company allows employees to accumulate paid time off to be used for vacation, holiday and sick time. The Company allows employees to be paid for their vacation and holiday time not taken and accrues its liability for such time. Such liability is classified as accrued compensation and related expenses in the accompanying consolidated balance sheets.

Charity Care and Community Benefit

As a community provider, the Company’s policy is to accept all patients regardless of their ability to pay. As a result, no distinction is made between bad debts and charity care for financial reporting purposes. However, management believes that substantially all of the uncollected amounts are due to patients’ inability to pay. Therefore, all amounts which are not collected, other than third-party payor contractual adjustments, are recorded as charity care and excluded from net patient service revenues. The community benefit provided through charity care was $97,874,843 and $79,735,918, based on gross charges, for the years ended June 30, 2010 and 2009, respectively.

1. Significant Accounting Policies (continued)

Net Patient Service Revenues

Net patient service revenues are reported at the net amounts billed to patients, third-party payers and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as changes in estimated provisions and final settlements are determined. Changes in estimated provisions and final settlements are included in net patient service revenues. For the fiscal year ended June 30, 2010, changes in estimated settlements resulted in an increase to revenues of approximately $2,165,297 compared to $1,098,091 for the fiscal year ended June 30, 2009.

The Company has agreements with third-party payors that provide for payments to the Company at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows.

- *Medicare.* Inpatient acute care services and skilled nursing services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The Company receives additional payments from Medicare based on the provision of services to a disproportionate share of Medicaid eligible and other low income patients. The Center for Medicare and Medicaid Services (CMS) (formerly known as the Health Care Financing Administration) established an outpatient prospective payment system. The CMS established groups called ambulatory payment classifications for outpatient procedures. Payments are made based on the group assignment for the service rendered. Additionally, CMS established a prospective payment system for home health services.

- *TennCare.* The Company contracts with managed care organizations to receive reimbursement for providing hospital services to patients covered under the TennCare program. Payment arrangements with these managed care organizations consist primarily of prospectively determined rates per discharge, discounts from established charges or prospectively determined daily rates.

1. Significant Accounting Policies (continued)

- *Other*. The Company has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The bases for payment to the Company under these agreements include prospectively determined rates per discharge, discounts from established charges or prospectively determined daily rates.

Charges at the Company's established billing rates (gross patient service charges) related to patients covered by Medicare, Medicaid, and TennCare programs were 59% of gross patient service revenues in both 2010 and 2009.

Charges exceeding amounts reimbursed and not included in net patient service revenues were as follows:

	Year Ended June 30	
	2010	**2009**
Medicare	**$ 405,178,978**	$ 361,629,438
TennCare	**136,367,624**	137,387,574
Other	**300,189,460**	262,589,621
	$ 841,736,062	$ 761,606,633

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 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 (in relation to certain government programs, primarily Medicare, this is generally referred to as the "cost report" filing and settlement process). 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.

Essential access and Medicaid Disproportionate Share payments of approximately $5,747,622 and $6,641,865 received from TennCare/Medicaid were included in net revenues during the years ended June 30, 2010 and 2009, respectively.

1. Significant Accounting Policies (continued)

The Company believes that it is in compliance with all applicable laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and TennCare/Medicaid programs.

Operating Revenues

The Company's primary mission is to provide health care services to the citizens of West Tennessee through its acute care and specialty care facilities. Therefore, operating revenues include those generated from direct patient care and sundry revenues related to the operation of the Company's facilities.

Use of Estimates

The preparation of financial statements in conformity with governmental accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Federal Income Taxes

The Internal Revenue Service has determined that all material affiliates comprising the Company are exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (IRC). The District is also exempt from federal income taxes under Section 115 of the IRC. As qualified tax-exempt organizations, each of the tax-exempt affiliates comprising the Company must operate in conformity with the IRC to maintain its tax-exempt status.

Reclassifications

Certain reclassifications have been made in the 2009 financial statements to conform to the 2010 presentation. These reclassifications have no effect on the results of operations or financial position as previously reported.

2. Assets Limited as to Use

The Company, as authorized by the Board of Trustees, maintains checking accounts necessary for daily operations, deposits for the contingency fund, and deposits and investments for the funded depreciation funds. The bond funds are maintained in accordance with the bond indenture related to the Series 2008 $318,980,000 Hospital Revenue Refunding and Improvement Bonds (see Note 6). The interest fund and bond sinking fund are maintained for the payment of bond principal and interest. A debt service reserve fund is maintained to make up any deficiencies in the interest fund and bond sinking fund. Certain amounts comprising the interest fund, bond sinking fund and debt service reserve fund are included in assets limited as to use-current portion in the accompanying consolidated balance sheets based on debt service requirements during the following fiscal year.

The Company's investments and deposits, classified as assets limited as to use, are categorized to give an indication of the level of risk assumed by the Company as of year-end. All of the Company's investments presented below are included in Category 1. Category 1 includes investments that are insured or registered, or for which the securities are held by the Company or its agent in the Company's name.

The Company's investments are reported at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. The Company invests in government and corporate bonds, equity securities, alternative investments and short-term money market investments that are in accordance with the Company's investment policy.

2. Assets Limited as to Use (continued)

A summary of assets limited as to use follows:

	June 30	
	2010	**2009**
Externally restricted by bond indenture agreement – held by bond trustee:		
Cash and short-term investments	**$ 27,188,903**	$ 27,206,217
Internally designated for capital acquisitions:		
Cash and short-term investments	**495,448**	1,092,749
Corporate and US agency bond funds	**77,373,154**	33,977,929
Real estate mortgage fund	**11,807,601**	12,375,825
Equity securities	**60,487,485**	59,585,757
	150,163,688	107,032,260
Other internally designated funds:		
Cash and short-term investments	**40,959,525**	11,477,413
U.S. government agency obligations	**28,093,631**	23,467,486
Real estate mortgage fund	**4,287,253**	8,547,593
Equity securities	**21,962,566**	41,154,007
	95,302,975	84,646,499
Total assets limited as to use	**272,655,566**	218,884,976
Amounts required to meet current obligations	**(5,694,454)**	(5,737,858)
	$ 266,961,112	$ 213,147,118

3. Cash and Investments

At June 30, 2010 and 2009, the Company had cash on hand and deposits as follows:

	June 30 2010	June 30 2009
Cash on hand	**$ 13,417**	$ 14,847
Cash insured (FDIC) or collateralized with securities held by the Company	**2,025,252**	2,028,642
Cash collateralized by securities held by the pledging financial institution's trust department in the Company's name or in the State of Tennessee Collateral Pool	**23,129,479**	26,283,003
Total	**$ 25,168,148**	$ 28,326,492

The types of securities which are permitted investments for Company funds are established by the Company's Investment Policy in accordance with Tennessee Statutes. All funds of the Company may be invested in obligations of or guaranteed by the United States Government. In addition, certain funds of the Company may be invested in obligations of agencies of the U.S. government; obligations of or guaranteed by the State of Tennessee; collateralized certificates of deposit and repurchase agreements' commercial paper; and other asset classes including fixed income, domestic equities, international equities, and alternative investments.

Investments of the Company are comprised of the following:

	June 30 2010	June 30 2009
Cash and short-term investments	**$ 41,454,974**	$ 12,570,169
Trustee funds	**27,188,903**	27,206,217
Corporate and U.S. agency bond funds	**105,466,782**	57,445,410
Real estate mortgage fund	**16,094,854**	20,923,417
Equity securities	**82,450,053**	100,739,763
Total investments	**$ 272,655,566**	$ 218,884,976

3. Cash and Investments (continued)

At June 30, 2010 and 2009, the Company had $41,454,974 and $12,570,169, respectively, invested in short-term investments, which include U.S. Agencies and a sweep account secured by Agency securities held by the Trustee. All investments are carried at fair value.

In accordance with Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures* (GASB 40), the Company has assessed the Custodial Credit Risk, the Concentration of Credit Risk, Credit Risk, and Interest Rate Risk of its Cash and Investments.

(a) Custodial Credit Risk – The Company's deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized or are collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name. The deposit risk is that, in the event of the failure of a depository financial institution, the Company 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. The Company's investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the Company, and are held by either the counterparty or the counterparty's trust department or agent but not in the Company's name. The investment risk is that, in the event of the failure of the counterparty to a transaction, the Company will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

At June 30, 2010, the Company's bank balances were not exposed to custodial credit risk since the full amount was covered by FDIC insurance or collateralized by securities held by the pledging financial institution's Trust department in the Company's name or by the State of Tennessee Collateral Pool.

As of June 30, 2010 and 2009, the Company's investments were comprised of various short term investments, trustee funds, corporate and U.S. agency bond funds, real estate mortgage funds, equity securities and alternative investments. Since the investments are registered in the Company's name, they are not exposed to custodial credit risk. In addition, the Company's investment policy requires that specific qualifications be met in order to represent the Company as a custodian.

3. Cash and Investments (continued)

(b) Concentration of Credit Risk – This is the risk associated with the amount of investments the Company has with any one issuer that exceeds 5 percent 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 Company's investment policy states that no equity may represent more than 8% of any individual portfolio manager and that no single purchase shall represent more than 5% of the Company's total equity position.

(c) Credit Risk – GASB 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. This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Company's investment policy provides guidelines for its fund managers and lists specific allowable investments. The policy provides for the utilization of varying styles of managers so that portfolio diversification is maximized and total portfolio efficiency is enhanced.

The credit risk profile of the Company's investments as of June 30, 2010, is as follows:

Investment Type	Balance as of June 30, 2010	Rating AAA	AA	A	N/A
Short-term investments	**$ 41,454,974**	**$ 41,454,974**	**$ –**	**$ –**	**$ –**
Trustee funds	**27,188,903**	**27,188,903**	**–**	**–**	**–**
Corporate and US agency bond funds	**105,466,782**	**–**	**91,127,202**	**14,339,580**	**–**
Real estate mortgage fund	**16,094,854**	**–**	**–**	**–**	**16,094,854**
Equity securities	**82,450,053**	**–**	**–**	**–**	**82,450,053**
Total investments	**$ 272,655,566**	**$ 68,643,877**	**$ 91,127,202**	**$ 14,339,580**	**$ 98,544,907**

The credit risk profile of the Company's investments as of June 30, 2009 is as follows:

Investment Type	Balance as of June 30, 2009	Rating AAA	AA	A	N/A
Short-term investments	$ 12,570,169	$ 12,570,169	$ –	$ –	$ –
Trustee funds	27,206,217	27,206,217	–	–	–
Corporate and US agency bond funds	57,445,410	–	44,020,848	13,424,562	–
Real estate mortgage fund	20,923,417	–	–	–	20,923,417
Equity securities	100,730,763	–	–	–	100,739,763
Total investments	$ 218,884,976	$ 39,776,386	$ 44,020,848	$ 13,424,562	$ 121,663,180

3. Cash and Investments (continued)

(d) Investment Rate Risk – This is the risk that changes in interest rates will adversely affect the fair value of an investment. The Company's Investment Policy authorizes a strategic asset allocation that is designed to provide an optimal return over the Company's investment horizon and within the Company's risk tolerance and cash requirements.

The distribution of the Company's investments by maturity as of June 30, 2010, is as follows:

		Remaining Maturity (In Months)				
Investment Type	**Balance as of June 30, 2010**	**12 Months or Less**	**13 Months to 24 Months**	**25 Months to 60 Months**	**Greater than 60 Months**	**N/A**
Short-term investments	$ 41,454,974	$ 41,454,974	$ –	$ –	$ –	$ –
Trustee funds	27,188,903	27,188,903	–	–	–	–
Corporate & US agency bond funds	105,466,782	–	–	105,466,782	–	–
Real estate mortgage fund	16,094,854	–	–	–	–	16,094,854
Equity securities	82,450,053	–	–	–	–	82,450,053
Total investments	272,655,566	68,643,877	–	105,466,782	–	98,544,907
Amounts required to meet current obligations	(5,694,454)	(5,694,454)	–	–	–	–
Total	$ 266,961,112	$ 62,949,423	$ –	$ 105,466,782	$ –	$ 98,544,907

For the years ended June 30, 2010 and 2009, investment income (loss) is comprised of the following:

	2010	**2009**
Interest earnings	**$ 4,089,287**	$ 5,370,324
Net increase (decrease) in fair value of investments	**20,365,242**	(41,072,513)
	$ 24,454,529	$ (35,702,189)

4. Disaggregation of Payable Balances

Accounts Payable and Accrued Expenses

Accounts payable at June 30, 2010 and 2009, consisted of the following:

	2010	2009
Due to vendors	**$ 13,983,545**	$ 14,639,486
Due to patients	**2,080,781**	2,486,074
Other	**283,175**	108,707
Total accounts payable	**$ 16,347,501**	$ 17,234,267

Other accrued expenses at June 30, 2010 and 2009, consisted of the following:

	2010	2009
Accruals for self insurance	**$ 9,050,724**	$ 8,775,571
Other	**14,061,147**	15,158,436
Total other accrued expenses	**$ 23,111,871**	$ 23,934,007

5. Net Property, Plant and Equipment

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

	Balance at June 30, 2008	Additions	Reductions	Balance at June 30, 2009	Additions	Reductions	Balance at June 30, 2010
Land	$ 23,977,302	$ 2,951,000	$ (26,000)	$ 26,902,302	$ 9,816,186	$ (7,004,759)	**$ 29,713,728**
Land improvements	12,987,852	2,816,780	(90,781)	15,713,851	235,759	(1,431,831)	**14,517,779**
Less accumulated depreciation	6,855,611	885,701	(301,915)	7,439,397	726,806	489,623	**7,676,580**
Net land and improvements	6,132,241	1,931,079	211,134	8,274,454	(491,047)	(942,208)	**6,841,199**
Buildings	167,820,543	88,627,065	(532,946)	255,914,662	24,145,673	(4,256,921)	**275,803,414**
Less accumulated depreciation	89,157,727	11,933,618	(3,126,458)	97,964,887	10,991,339	2,294,747	**106,661,479**
Net buildings	78,662,816	76,693,447	2,593,512	157,949,775	13,154,334	(1,962,174)	**169,141,935**
Equipment	440,002,910	98,499,781	(41,837,100)	496,665,591	35,978,948	(2,905,315)	**529,739,224**
Less accumulated depreciation	284,079,996	38,682,518	(43,406,584)	279,355,930	40,467,554	1,879,524	**317,943,960**
Net equipment	155,922,914	59,817,263	1,569,484	217,309,661	(4,488,606)	(1,025,791)	**211,795,264**
Construction in progress	128,538,305	36,453,805	(141,150,168)	23,841,942	27,247,293	(46,841,974)	**4,247,262**
	$ 393,233,578	$ 177,846,594	$ (136,802,038)	$ 434,278,134	$ 45,238,160	$ (57,776,906)	**$ 421,739,388**

Depreciation is computed by applying the straight-line method over the estimated remaining useful lives of buildings and improvements (10 to 40 years) and equipment (4 to 20 years). Assets under capital leases are amortized using the straight-line method over the shorter of the estimated useful life of the assets or life of the lease term, excluding any lease renewal, unless the lease renewals are reasonably assured. Amortization expense related to assets under capital leases is included in depreciation expense. The Company’s capitalization threshold is $1,000 and a minimum useful life of 2 years. Depreciation expense totaled $51,018,609 and $47,223,872 during 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 Company’s facilities. The Company has outstanding contracts and other commitments related to the completion of these projects. The Company estimates $4,762,049 in costs to complete these projects.

6. Long-Term Debt and Capital Lease Obligations

Long-term debt consists of the following:

	June 30	
	2010	**2009**
Hospital Revenue Bonds, Series 2008	**$ 312,415,000**	$ 316,555,000
Less unamortized bond discount	**(5,402,186)**	(5,682,997)
	307,012,814	310,872,003
Hospital Revenue Refunding and Improvement Bonds, Series 1995, unamortized loss on bond refunding	**(492,502)**	(697,351)
Hospital Revenue Bonds, Series 1998, unamortized bond discount	**(2,313,123)**	(2,546,100)
Auction Rate Hospital Revenue Bonds, Series 2003, unamortized loss on defeasance	**(1,736,844)**	(1,897,539)
Auction Rate Hospital Revenue Bonds, Series 2006A, unamortized loss on defeasance	**(323,787)**	(340,327)
Auction Rate Hospital Revenue Bonds, Series 2006B, unamortized loss on defeasance	**(3,164,430)**	(3,309,760)
Capital lease obligation	**1,334,916**	1,518,629
Notes payable	**1,059,833**	3,159,793
	301,376,877	306,759,348
Amounts due within one year	**(5,976,315)**	(6,723,672)
	$ 295,400,562	$ 300,035,676

In September 1995, the District issued $68,200,000 of Series 1995 Hospital Revenue Refunding and Improvement Bonds. A portion of the proceeds of the Series 1995 Bonds were used to advance refund $39,370,000 of its Series 1986 Bonds. The remaining proceeds of the Series 1995 Bonds were used to fund capital improvements of certain facilities of the District.

In September 1998, the District issued $70,000,000 of Series 1998 Hospital Revenue Bonds. A portion of the proceeds of the Series 1998 Bonds were used to advance refund $8,940,000 and $1,150,000 of Series 1992 and 1986 Bonds, respectively. The remaining proceeds of the Series 1998 Bonds were used to fund capital improvements of certain facilities of the District.

6. Long-Term Debt and Capital Lease Obligations (continued)

In October of 2003, the District issued $80,000,000 of Series 2003 Auction Rate Hospital Revenue Bonds. The proceeds of these bonds were used to fund capital improvements of certain facilities of the District.

In August of 2006, the District issued $50,100,000 of Series 2006A Auction Rate Hospital Revenue Refunding Bonds. A portion of the proceeds were used to refund $49,700,000 of its Series 1995 Bonds. The remaining proceeds of the Series 2006A Bonds were used to fund capital improvements of certain facilities of the District.

In August of 2006, the District issued $145,700,000 of Series 2006B Variable Rate Demand Hospital Revenue Refunding and Improvement Bonds. A portion of the proceeds were used to advance refund $57,570,000 of its Series 1998 Bonds. The remaining proceeds of the Series 2006B Bonds were used to fund capital improvements of certain facilities of the District.

In August 2008, the District issued $318,980,000 of Series 2008 Hospital Revenue Refunding and Improvement Bonds. With the 2008 fixed rate bond issue, the District has eliminated all auction rate and variable rate debt. A portion of the proceeds were used to refund $78,350,000 of its Series 2003 Auction Rate Hospital Revenue Bonds; $48,725,000 of its Series 2006A Auction Rate Hospital Revenue Bonds; and $143,600,000 of its Series 2006B Variable Demand Rate Hospital Revenue Refunding and Improvement Bonds. A Debt Service Reserve Fund was created under the 2008 indenture. On the date of issuance of the 2008 bonds, $21,299,713 of the proceeds of the 2008 bonds were deposited in the Debt Service Reserve Fund. The remaining proceeds of the Series 2008 Bonds will be used to fund capital improvements of certain facilities of the District.

The District's revenues are pledged as collateral to the Series 2008.

The Company paid interest of $18,304,806 and $12,668,813 for the years ended June 30, 2010 and 2009, respectively.

6. Long-Term Debt and Capital Lease Obligations (continued)

Long-term debt activity (excluding unamortized bond discount and losses on refunding) for the years ended June 30, 2010 and 2009, consisted of the following:

	Balance at June 30, 2008	Additions	Reductions	Balance at June 30, 2009	Additions	Reductions	Balance at June 30, 2010
Bonds payable	$237,500,000	$352,155,000	$273,100,000	$316,555,000	$ –	$ 4,140,000	**$312,415,000**
Other	–	8,928,795	4,250,373	4,678,422	300,000	2,583,672	**2,394,750**
Total long-term debt	$237,500,000	$361,083,795	$277,350,373	$321,233,422	$ 300,000	$ 6,723,672	**$314,809,750**

During fiscal year 2008, the District purchased $33,175,000, of the Series 2006A Auction Rate Hospital Revenue Refunding Bonds, prior to refinancing all of its outstanding long-term debt in August 2008. These purchases were accounted for as an extinguishment of debt at June 30, 2008.

The 2008 Bond Issue which closed in August 2008 provided for the termination of the District's 2003A, 2006A, and 2006B interest rate swaps. The District made termination payments to the counterparties of $4,073,687, $3,493,889, and $11,344,647, respectively for the 2003A, 2006A, and 2006B interest rate swaps. Subsequent to such termination payments, the District has no risk associated with any interest rate swaps at June 30, 2010.

Scheduled principal and interest payments, including capital lease obligations and notes payable, are as follows:

Fiscal Years Ending June 30	Principal	Interest	Total
2011	$ 5,976,315	$ 17,033,508	$ 23,009,823
2012-2016	25,313,435	81,911,285	107,224,720
2017-2021	31,345,000	75,142,569	106,487,569
2022-2026	40,465,000	66,014,694	106,479,694
2027-2031	52,585,000	53,898,975	106,483,975
2032-2036	68,740,000	37,748,500	106,488,500
2037-2041	90,385,000	16,103,325	106,488,325
Unamortized bond discount, net	(5,402,186)	–	(5,402,186)
Unamortized loss on bond refunding, net	(8,030,687)	–	(8,030,687)
Total	$ 301,376,877	$ 347,852,856	$ 649,229,733

7. Leases

The Company leases equipment under various operating leases. Rent expense for all operating leases was approximately $3,724,464 and $3,913,261 for the years ended June 30, 2010 and 2009, respectively. Approximate minimum future rental payments, by year and in the aggregate, under noncancelable operating leases with initial terms of one year or more are as follows at June 30, 2010.

2011	$ 3,908,313
2012	3,545,402
2013	2,923,065
2014	2,762,048
2015	2,066,854
Thereafter	9,198,501
	$ 24,404,183

8. Concentrations of Credit Risk

The Company grants credit without collateral to its patients, most of whom are individuals and are insured under third-party payor agreements. Accounts receivable from patients and third-party payors are as follows:

	June 30	
	2010	**2009**
Medicare	**35%**	34%
Medicaid and TennCare	**14**	13
Blue Cross	**11**	15
Private pay	**25**	24
Other	**15**	14
	100%	100%

9. Retirement Plans

Defined Benefit Plan

The Company maintains a noncontributory, defined benefit pension plan (the Plan). The Plan was discontinued for employees hired after June 30, 2010. The Plan is a single-employer defined benefit pension plan. All employees hired after October 1, 2005 and prior to June 30, 2010, are covered on the fifth anniversary of their date of hire after they have completed at least 1,800 hours of employment per year. The Plan provides retirement, termination, disability, and death benefits to plan members and beneficiaries. The operation of the Plan is consistent with the laws of Tennessee and the United States federal government. The Plan issues a publicly available financial report as required by GASB Statement No. 25 that includes a financial statement and required supplementary information for the Plan. That report may be obtained by writing to West Tennessee Healthcare, attention: Human Resources, Manager of Benefits, 620 Skyline Drive, Jackson, Tennessee 38301-3956 or by calling 731-541-5000.

Funding Policy

The Company has no legal or plan requirements to fund the Plan. The Company has established a policy of funding the end of the Plan year normal cost plus 20-year amortization of the unfunded actuarial accrued liability up to fully funding the accrued liability of the Actuarial Method.

Annual Pension Cost and Net Pension Obligation

Current year contributions made to the Plan equaled 99% of the annual pension cost. Contributions made to the Plan in 2005 equaled the annual pension cost plus an additional one-time discretionary contribution of $6,300,006. Therefore, the net pension obligation had an ending credit balance of $5,424,246 at June 30, 2010, and $5,482,283 at June 30, 2009.

The annual required contribution for the fiscal year ending June 30, 2010, was determined as part of the actuarial valuation for the Plan year beginning January 1, 2009, and was determined using the Actuarial Cost Method with amortization of the unfunded actuarial liability over 30 years. The actuarial assumptions included (a) 7% post-retirement and 7% pre-retirement investment rate of return and (b) a projected salary increase of 5% per year. Both (a) and (b) include an inflation component of 2.5%. The actuarial value of assets is equal to the market value of assets reported by First Tennessee Bank and CNA Insurance Company.

9. Retirement Plans (continued)

The funded status of the defined benefit plan, including three year trend information, was as follows:

Defined Benefit Plan Three-Year Trend Information

Fiscal Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation (Credit)
June 30, 2008	$ 11,447,418	98%	$ (5,686,173)
June 30, 2009	11,140,906	98%	(5,482,283)
June 30, 2010	11,126,262	99%	(5,424,246)

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Total Unfunded AAL (Funding Deficit) (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as a Percentage of Covered Payroll
January 1, 2008	$ 152,712,499	$ 175,027,485	$ 22,314,986	87%	$ 173,007,888	13%
January 1, 2009	160,897,049	192,825,950	31,928,901	83%	170,823,560	19%
January 1, 2010	168,453,833	205,375,259	36,921,426	82%	159,404,388	23%

The Company also maintains a defined contribution plan under Section 403(b) of the IRC which provides for voluntary contributions by employees upon employment and matching contributions by the District after two years of service. Substantially all employees of the District are eligible and may contribute up to 100% of their compensation, subject to certain IRC limitations. Upon January 1 after the completion of two years of credited service, the District matches 100% of the first 3% of compensation contributed and 50% of the next 3% contributed. The District placed a temporary freeze on the match to the 403(b) plan during the fiscal year ended June 30, 2010. The District recognized expense related to the 403(b) Plan of $0 and $3,176,742 in 2010 and 2009, respectively.

9. Retirement Plans (continued)

Supplemental 415(m) Retirement Plan

In 2005, the Company established a supplemental 415(m) retirement plan (the 415 Plan). The 415 Plan will provide monthly benefits equal to the benefit that cannot be paid from the Defined Benefit Plan due to the application of the Code Section 415 limits. The operation of the Plan is consistent with the laws of Tennessee and the United States federal government.

Because the 415 Plan is unfunded, these benefit payments are deemed contributions when paid.

The funded status of the 415 Plan, including three year trend information, was as follows:

Supplemental 415(m) Plan Three-Year Trend Information

Fiscal Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation (Credit)
June 30, 2008	$ 78,744	0%	$ 223,088
June 30, 2009	83,468	77%	242,429
June 30, 2010	82,180	85%	254,652

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Total Unfunded AAL (Funding Deficit) (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as a Percentage of Covered Payroll
July 1, 2008	$ –	$ 957,366	$ 957,366	0%	N/A	0%
July 1, 2009	–	925,935	925,935	0%	N/A	0%
July 1, 2010	–	923,632	923,632	0%	N/A	0%

Other Post-Employment Benefits

Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, was issued in June 2004. The requirements apply to any state or local government employer that provides Other Post-Employment Benefits (OPEB). The primary types of OPEB covered by the statement are postretirement health benefits and life insurance benefits. The effective date of this requirement for the Company was the fiscal year beginning July 1, 2007.

9. Retirement Plans (continued)

Any of six actuarial cost methods can be used to determine the OPEB expense. The Company calculated its OPEB expense using the projected unit credit method.

The unfunded actuarial accrued liability must be amortized over a period of not greater than 30 years. The amortization amount may be computed as a level dollar amount or as a level percentage of pay. The Company used a level percentage of pay with a 30-year closed amortization period for purposes of computing the minimum accrual under GASB 45.

The Annual Required Contribution (ARC) calculated in accordance with GASB 45 for the fiscal years ending June 30, 2010 and 2011, is summarized below.

ARC Based on a Level Percent of Pay Amortization for Fiscal Year Ending

Level Percent of Pay Amortization	**June 30, 2010**	**June 30, 2011**
Medical benefits – projected unit credit	$ 790,751	$ 826,240

GASB 45 does not require funding of OPEB expense, but any differences between the annual expense and the amount funded in a year are recorded in the Company's financial statement as an increase (or decrease) in the net OPEB obligation. The Company elected to fund its OPEB expense and as of June 30, 2010, the fund had net assets in the amount of $1,535,882. This balance represents the June 30, 2008 ARC of $547,951, the June 30, 2009 ARC of $337,343 plus the fiscal year 2010 funding of $643,116 in addition to $7,472 in earnings on the fund. The balance funded by the Company for the fiscal year ended June 30, 2010 was $643,116, which represents the 2010 ARC of $790,751 less actual benefit payments of $147,635.

10. Commitments and Contingencies

The Company is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters.

Settled claims have not exceeded this commercial coverage in any of the three preceding years.

10. Commitments and Contingencies (continued)

Professional Liability

The Company established the contingency fund as a professional liability self-insurance fund in accordance with the Government Tort Liability Act, which restricts the District's exposure to professional liability risks to a pre-determined amount per occurrence.

The District is a "governmental entity" within the meaning of the Tennessee Governmental Tort Liability Act (the Tort Act). As such, its maximum liability for state law tort causes of action is $300,000 for bodily injury or death of any one person in accident, occurrence, or act, and $700,000 for bodily injury or death of all persons in any one accident, occurrence, or act. These limits are subject to change by the Tennessee Legislature. Prior to July 1, 2002, the Tennessee Governmental Tort Liability limited local government tort liability to $130,000 for individual injury or death in any one occurrence and $350,000 for injury or death of all persons in any one occurrence.

Investment earnings on contingency fund assets were $113,084 and $121,989 for the years ended June 30, 2010 and 2009, respectively, and are classified as investment income in the accompanying consolidated statements of revenues and expenses and changes in net assets.

The Company's accrual for self-insured professional liability risks was $4,000,000 and $3,700,000 at June 30, 2010 and 2009, respectively, and was based on asserted claims for occurrences prior to that date. The Company does not accrue for unasserted claims or occurrences. In the opinion of management, any liability for such unasserted claims or occurrences would not materially affect the financial position of the Company.

Workers' Compensation

Under the Tennessee Workers' Compensation Law, governmental entities such as the District need not accept the workers' compensation system, thereby remaining subject to common law liability for work-related injuries and retaining all common law defenses to such claims. The limits of liability under the Tort Act are applicable to such claims. The District has not accepted the workers' compensation system. The Tennessee Supreme Court has ruled this exemption applicable to the District's affiliate nonprofit corporations as well.

10. Commitments and Contingencies (continued)

Employee Health

The Company is self-insured with respect to employee health insurance. Estimates of health insurance claims incurred but unpaid as of June 30, 2010 and 2009, are accrued based on estimates that incorporate the Company's past experience, as well as other considerations including the nature of claims and relevant trends. The Company had accrued a liability for incurred but unpaid claims of approximately $9,050,724 and $8,775,571, as of June 30, 2010 and 2009, respectively, which is included in accrued compensation and related expenses in the accompanying consolidated financial statements. The expenses related to claims paid during the years ended June 30, 2010 and 2009, are $27,206,537 and $29,178,267, respectively, and are included in salary and benefits expense.

Litigation

The Company 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 recorded in its consolidated financial statements, and will not have a material effect on the Company's results of operations or financial position.

11. Segment Information

As disclosed in Note 6, the Company has revenue bonds outstanding that are payable from the operating revenues of certain affiliates of the District (the Obligated Group). Summary financial information for the Obligated Group is as follows:

	June 30	
	2010	**2009**
Assets		
Current assets	**$ 127,269,577**	$ 143,137,048
Property, plant, and equipment, net	**389,810,055**	409,487,771
Other assets	**259,271,365**	207,131,326
	$ 776,350,997	$ 759,756,145
Liabilities and net assets		
Current liabilities	**$ 55,259,467**	$ 64,106,237
Long-term debt	**295,400,562**	300,035,676
Net assets:		
Unrestricted net assets	**288,582,985**	244,370,521
Invested in capital assets, net of related financing	**109,929,080**	124,037,494
Restricted net assets	**27,188,903**	27,206,217
	425,690,968	395,614,232
	$ 776,350,997	$ 759,756,145

11. Segment Information (continued)

	Year Ended June 30 2010	2009
Net patient service revenues	**$ 461,861,863**	$ 448,410,772
Other operating revenues	**25,611,304**	19,379,821
Total revenues	**487,473,167**	467,790,593
Operating expenses	**406,253,708**	411,844,868
Depreciation	**46,231,445**	42,881,960
Total expenses	**452,485,153**	454,726,828
Income from operations	**34,988,014**	13,063,765
Loss on swap termination	**–**	(18,912,223)
Income (loss) from operations after swap loss	**34,988,014**	(5,848,458)
Net nonoperating gains (losses)	**21,518,036**	(31,839,413)
Interest expense	**(18,364,589)**	(18,863,711)
Income (loss) before capital contributions and transfers	**38,141,461**	(56,551,582)
Transfers (to) from other affiliates	**(941,325)**	(922,784)
Contributions	**(1,123,400)**	(898,063)
Increase (decrease) in net assets	**36,076,736**	(58,372,429)
Net assets, beginning of year	**389,614,232**	447,986,661
Net assets, end of year	**$ 425,690,968**	$ 389,614,232
Net cash provided by (used in):		
Operating activities	**$ 86,193,884**	$ 24,636,077
Noncapital financing activities	**(2,064,725)**	(1,820,846)
Capital and related financing activities	**(55,966,212)**	(19,035,229)
Investing activities	**(29,390,691)**	8,311,636
Net decrease in cash and cash equivalents	**(1,227,744)**	12,091,638
Cash and cash equivalents, beginning of year	**14,284,292**	2,192,654
Cash and cash equivalents, end of year	**$ 13,056,548**	$ 14,284,292

12. Adjustments to prior year financial statements

In the Company's previously-issued consolidated balance sheet as of June 30, 2009, the Company incorrectly classified approximately $237,000,000 of outstanding indebtedness as a reduction of unrestricted net assets. Such debt should have been reflected as a reduction of invested in capital assets, net of related financing. This misclassification resulted in an understatement of unrestricted net assets and an overstatement of invested in capital assets, net of related financing. Such amounts have been corrected in the accompanying consolidated balance sheet as of June 30, 2009.

In September 2001, the Company purchased certain property from the City of Jackson, TN. The value of the land, based on an independent appraisal, was approximately $2,000,000. The Company paid the City of Jackson $8,000,000 in connection with this transaction – $2,000,000 for the land and $6,000,000 as a contribution to the City of Jackson to be used toward the construction of a new elementary school. The Company erroneously recorded the entire amount paid as land at the time of purchase, while $6,000,000 should have been recorded as a reduction of net assets (specifically, invested in capital assets net of related financing) to reflect the contribution to the City of Jackson. The accompanying consolidated balance sheet as of June 30, 2009, has been adjusted to decrease land and net assets by $6,000,000. Additionally, beginning net assets as of July 1, 2008, in the accompanying consolidated statement of revenues and expenses and changes in net assets, has been decreased to reflect the adjustment.

A reconciliation between previously-reported balances and the as-adjusted amounts to reflect both of the aforementioned adjustments is shown below:

	Previously Reported	Adjustment	As Adjusted
Land and land improvements as of June 30, 2009	$ 48,616,153	$ (6,000,000)	$ 42,616,153
Invested in capital assets, net of related financing as of June 30, 2009	391,973,134	(243,145,277)	148,827,857
Unrestricted net assets as of June 30, 2009	12,030,049	237,145,277	249,175,326
Net assets as of July 1, 2008	493,353,250	(6,000,000)	487,353,250
Net assets as of June 30, 2009	431,209,400	(6,000,000)	425,209,400

Required Supplemental Information

West Tennessee Healthcare and Related Affiliates

Required Supplementary Information

Defined Benefit Retirement Plan
Schedule of Employer Contributions (Unaudited)

Year Ended December 31	Fiscal Year Ending	(a) Annual Required Contribution	Actual Contribution	Percentage Contributed
2002	June 30, 2003	$ 5,647,005	$ 5,647,005	100%
2003	June 30, 2004	6,456,714	6,456714	100%
2004	June 30, 2005	7,024,158	13,324,164	190%
2005	June 30, 2006	10,851,226	10,851,240	100%
2006	June 30, 2007	10,928,116	10,928,124	100%
2007	June 30, 2008	11,254,451	11,182,451	99%
2008	June 30, 2009	10,937,013	10,937,016	100%
2009	June 30, 2010	11,068,225	11,068,225	100%

(a) The actuarially determined contribution requirements for the Company's fiscal year ended June 30, 2010, are based on actuarial valuations as of January 1, 2009.

West Tennessee Healthcare and Related Affiliates

Required Supplementary Information

Defined Benefit Retirement Plan
Schedule of Funding Progress (Unaudited)

Defined Benefit Plan-Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Total Unfunded AAL (Funding Deficit) (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as % of Covered Payroll
January 1, 2008	$ 152,712,499	$ 175,027,485	$ 22,314,986	87%	$ 173,007,888	13%
January 1, 2009	160,897,049	192,825,950	31,928,901	83%	170,823,560	19%
January 1, 2010	168,453,833	205,375,259	36,921,426	82%	159,404,388	23%

West Tennessee Healthcare and Related Affiliates

Required Supplementary Information

Postemployment Benefits Other Than Pensions Schedule of Funding Progress (Unaudited)

Supplemental 415(m) Plan- Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Total Unfunded AAL (Funding Deficit) (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as % of Covered Payroll
July 1, 2008	$ –	$ 957,366	$ 957,366	0%	$ NA	0%
July 1, 2009	–	925,935	925,935	0%	NA	0%
July 1, 2010	–	923,632	923,632	0%	NA	0%

Grant Compliance

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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*

The Board of Trustees
Bobby Arnold, Chief Executive Officer
Jeff Blankenship, Chief Financial Officer
West Tennessee Healthcare

We have audited the financial statements of the business type activities of West Tennessee Healthcare and Related Affiliates (the Company) as of and for the year ended June 30, 2010, and have issued our report thereon dated October 25, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal control over financial reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified a certain deficiency in internal control that we consider to be a significant deficiency.

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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency, *Finding No. 2010-01*, described in the accompanying schedule of findings and questioned costs to be a significant deficiency.

Compliance and other matters

As part of obtaining reasonable assurance about whether the Company'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 *Governmental Auditing Standards.*

The Company's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the Company's response and accordingly, we express no opinion on it.

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

Ernst + Young LLP

October 25, 2010

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Report on Compliance with Requirements That Could Have A Direct and Material Effect on the Federal Program and on Internal Control Over Compliance in Accordance with the Program – Specific Audit Option Under OMB Circular A-133

The Board of Trustees
Bobby Arnold, Chief Executive Officer
Jeff Blankenship, Chief Financial Officer
West Tennessee Healthcare

Compliance

We have audited West Tennessee Healthcare and Related Affiliates (the Company) with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Company's major federal programs for the year ended June 30, 2010. The Company'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, contacts, and grants applicable to each of its major federal programs is the responsibility of the Company's management. Our responsibility is to express an opinion on the Company'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 the Company'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 the Company's compliance with those requirements.

In our opinion, the Company complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal programs for the year ended June 30, 2010.

As further described in Note 3 to the schedule of expenditures of federal awards and state financial assistance, this report replaces a previously-issued report dated December 13, 2010, due to the identification of an additional major federal program which has been included in the revised summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Internal control over compliance

Management of the Company is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Company's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the 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 the Company'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 management, the Board of Trustees, others within the entity, the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

December 13, 2010, except with respect to the Early Intervention Services (IDEA) Cluster in the accompanying schedule of findings and questioned costs and Note 3 on page 52, for which the date is January 14, 2011

West Tennessee Healthcare and Related Affiliates

Schedule of Expenditures of Federal Awards and State Financial Assistance

For the Year Ended June 30, 2010

Federal Grantor/Pass-Through Grantor	CFDA #	Contract Number	Expenditures
Federal Awards			
US Department of Justice			
TN Department of Finance and Administration	16.803	3836	$ 84,698
Total US Department of Justice			84,698
US Department of Education			
Tennessee Dept of Education			
Early Intervention Services (IDEA) Cluster			
Special Education Grants for Infants and Families with Disabilities	84.181	GG1028025	291,360
ARRA – Special Education Grants for Infants and Families, Recovery Act	84.393	GG1028025	17,860
Total Early Intervention Services (IDEA) Cluster			309,220
Total US Department of Education			309,220
US Department of Health and Human Services			
Tennessee Department of Human Services			
Child Care and Development Block Grant	93.575	N/A	501,982
Block Grant for Community Mental Health Services	93.958	GG1029797	305,966
	93.958	7387-GR1028225	120,047
Tennessee Department of Mental Health and Developmental Disabilities Division of Alcohol and Drug Abuse Services			
Block Grant for Prevention and Treatment of Substance Abuse	93.959	Z-09-216552-01	574,154
	93.959	Z-09-213832-01 &02 &03	114,459
	93.959	7653-GG1028753	208,422
	93.959	10300-GG1028871	79,950
Tennessee Department of Health			
Block Grant for Maternal and Child Health Services	93.994	GG-10-26109-00	9,574
Small Rural Hospital Improvement Grant Program	93.301	Z-09-214880-00	42,500
Cooperative Agreements for State-Based Comprehensive Breast and Cervical Cancer Early Detection Programs	93.919	GG-10-27790-00	42,434
National Bioterrorism Hospital Preparedness Program	93.889	GG-10-30428	394,626
	93.889	GG-10-30430	20,003
	93.889	GG-10-30427	20,003
	93.889	GG-10-30444	20,094
	93.889	GG-10-30429	20,060
	93.889	GG-10-30426	19,579
	93.889	Z-08-200412-01	509,612
	93.889	Z-08-200399-01	37,809
	93.889	Z-08-200438-01	46,385
	93.889	Z-08-200376-01	33,946
	93.889	Z-08-200378-01	23,861
	93.889	Z-08-200410-01	47,266

West Tennessee Healthcare and Related Affiliates

Schedule of Expenditures of Federal Awards and State Financial Assistance (continued)

For the Year Ended June 30, 2010

Federal Grantor/Pass-Through Grantor	CFDA #	Contract Number	Expenditures
Federal Awards (continued)			
US Department of Health and Human Services (continued)			
Tennessee Department Mental Health Development Disabilities			
Substance Abuse and Mental Health Services			
Projects for Assistance in Transition from Homelessness	93.150	10255-GG1028845-01	58,500
Total US Department of Health and Human Services			3,251,232
Total Federal Awards			3,645,150
State Financial Assistance			
Tennessee Department of Education			
Special Education Grants for Infants and Families With Disabilities	84.181	GG1028025	315,640
Total Tennessee Department of Education			315,640
Tennessee Department of Mental Health and Developmental Disabilities Division of Alcohol and Drug Abuse Services			
Block Grant for Prevention and Treatment of Substance Abuse	93.959	Z-09-213832-01, 02 & 03	48,156
	93.959	Z-09-216552-01	44,147
	93.959	10300-GG1028871	49,969
	N/A	11197-GG1029366	400,000
	N/A	GG1030968	30,000
	N/A	7344-GR1028127	190,240
Block Grant for Maternal and Child Health Services	93.994	GG-10-26109-00	279,889
	N/A	GG-10-27787-00	56,512
	N/A	7506-GR1028450	1,461,017
	N/A	GG-1030831	51,000
Block Grant for Community Mental Health Services	93.958	GG1029797	29,176
	N/A	7457-GG1028551	32,450
	N/A	7685-GG1028775	36,000
	N/A	7648-GG1028670	52,500
	N/A	GG1029094-01	63,876
	N/A	GG1029415	279,999
	N/A	GG1029415	645,600
Substance Abuse and Mental Health Services			
Projects for Assistance in Transition from Homelessness	93.150	10255-GG1028845-01	27,359
	N/A	GG1029672	32,073
	N/A	10959-GG1029093	131,850
	N/A	17335-GG1030042	63,438
Total Tennessee Department of Mental Health and Developmental Disabilities Division of Alcohol and Drug Abuse Services			4,005,251
Tennessee Department of Finance and Administration			
Physician Connectivity	N/A	GG-09-26521-00	41,606
	N/A	GR-3636	57,973
Total Tennessee Department of Finance and Administration			99,579
Total State Awards			4,420,470
Total Federal and State Awards			$ 8,065,620

West Tennessee Healthcare and Related Affiliates

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

June 30, 2010

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards and state financial assistance includes the federal grant activity of West Tennessee Healthcare and Related Affiliates and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

2. Contingencies

The Company'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 Company'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 Company expects such amounts, if any, to be immaterial.

3. Reissuance of the Compliance Report

The schedule of expenditures of federal awards and state financial assistance has been revised to properly identify two federal programs (CFDA Numbers 84.181 and 84.393) as comprising a cluster. OMB Circular A133, *Audits of States, Local Governments, and Non-Profit Organizations,* requires expenditures under such programs to be aggregated for the purpose of determining major federal programs.

West Tennessee Healthcare and Related Affiliates

Schedule of Findings and Questioned Costs

Year Ended June 30, 2010

Part I – Summary of Auditor's Results

Financial Statement Section

Type of auditor's report issued:	Unqualified	
	Yes	**No**
Internal control over financial reporting:		
Material weakness(es) identified?		X
Significant deficiencies identified not considered to be material weaknesses?	X	
Noncompliance material to financial statements noted?		X

Federal Awards Section

	Yes	**No**
Internal control over major programs:		
Material weakness(es) identified?		X
Significant deficiencies identified not considered to be material weaknesses?		X
Type of auditor's report on compliance for major programs:	Unqualified	
	Yes	**No**
Any audit findings disclosed that are required to be reported in accordance with Circular A-133 (section .510(a))?		X

Part I – Summary of Auditor's Results (continued)

Identification of programs tested as major:

CFDA Number(s)	Name of Federal Program or Cluster
93.889	US Department of Health and Human Services – National Bioterrorism Hospital Preparedness Program
93.959	US Department of Health and Human Services – Block Grants for Prevention and Treatment of Substance Abuse
84.181, 84.393	US Department of Education – Early Intervention Services (IDEA) Cluster

Dollar threshold used to determine Type A programs: $ 300,000

	Yes	No
Auditee qualified as low-risk auditee?	X	

Part II – Financial Statement Findings Section

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.

Finding No. 2010-01

Misclassification within net assets

Observation

In the Company's previously-issued consolidated balance sheet as of June 30, 2009, the Company incorrectly classified approximately $237 million of outstanding indebtedness as a reduction of unrestricted net assets. Such debt should have been reflected as a reduction of invested in capital assets, net of related debt. This misclassification resulted in an understatement of unrestricted net assets and an overstatement of invested in capital assets, net of related debt. Such amounts have been corrected in the 2010 financial statements with a footnote disclosing the correction of the prior year misclassification.

Recommendation

Management should implement a process to more thoroughly review the determination of invested in capital assets, net of related debt, to ensure the propriety of classification within the Company's net assets.

Management's response

Management has remediated its internal control process to ensure that the net assets calculation is reviewed on a monthly basis such that that the classification within the Company's net assets is correctly stated.

Part III – Federal Award Findings and Questioned Costs Section

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

No findings required to be reported.

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