Report of Independent Auditors
and Financial Statements

Marin Healthcare District

June 30, 2011 and 2010

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

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CONTENTS

Marin Healthcare District
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2011

This section of Marin Healthcare District's (the District) financial statements presents management's discussion and analysis of the financial activities of the District for the fiscal year ended June 30, 2011. We encourage the reader to consider the information presented here in conjunction with the financial statements as a whole.

Introduction to the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's audited financial statements, which are comprised of the financial statements. This annual report is prepared in accordance with the Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments.*

The required financial statements include the Statement of Net Assets; the Statement of Revenues, Expenses and Changes in Net Assets; and the Statement of Cash Flows. Notes to the financial statements, supplementary detail and/or statistical information, and this summary support these statements. All sections must be considered together to obtain a complete understanding of the financial picture of the District.

Statement of Net Assets

This statement includes all assets and liabilities using the accrual basis of accounting as of the statement date. The difference between the two classifications if represented as "Net Assets"; this section of the statement identifies major categories of restrictions on these assets and reflects the overall financial position of the District as a whole.

Statement of Revenues, Expenses, and Changes in Net Assets

This statement presents the revenues earned and the expenses incurred during the year using the accrual basis of accounting. Under the accrual basis, all increases or decreases in net assets are reported as soon as the underlying event occurs, regardless of the timing of the cash flow. Consequently revenues and/or expenditures reported during this fiscal year may result in changes to cash flows in a future period.

Statement of Cash Flow

This statement reflects inflows and outflows of cash, summarized by operating, capital, financing, and investing activities. The direct method was used to prepare this information, which means gross rather than net amounts were presented for the year's activities.

Notes to the Financial Statements

This additional information is essential to a full understanding of the data reported in the financial statements.

The District is a political sub-division of the state of California. It is the lessor of the Marin General Hospital facility and is governed by a Board of Directors.

Marin Healthcare District
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2011

Analytical Overview

The Statement of Net Assets and Statement of Revenues, Expenses, and Changes in Net Assets present a summary of the District's activities.

Table 1
Condensed Statement of Net Assets

	6/30/2011	6/30/2010
Current and other assets	$ 4,321,579	$ 6,844,550
Capital assets, net of accumulated depreciation	7,234,710	7,577,779
Total assets	11,556,289	14,422,329
Long-term debt and other long-term liabilities	3,750,843	4,892,439
Other liabilities	1,485,629	4,150,940
Total liabilities	5,236,472	9,043,379
Net assets:		
Invested in capital assets, net of related debt	7,234,710	7,577,779
Unrestricted deficit	(914,893)	(2,198,829)
Total net assets	$ 6,319,817	$ 5,378,950

Summary

Total assets of the District have decreased this year by $2,866,040, primarily related to the reduction in receivables from Marin General Hospital (MGH).

Liabilities have decreased this year by $3,806,907, as a result of the reduction of accounts payable and the transfer of employee-related liabilities to MGH. Effective July 1, 2011, the District's senior management team became employees of MGH.

The overall change to net assets is an increase of $940,867, resulting in a June 30, 2011 balance of $6,319,817.

Marin Healthcare District
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2011

Comparative Analysis of Current and Prior Year Activities and Balances

	6/30/2011	6/30/2010	Increase (Decrease)	
Operating revenues	$ 2,671,841	$ 3,142,792	$ (470,951)	Note 2
Operating expenses	1,732,727	1,257,478	475,249	Note 1
Net operating income	$ 939,114	$ 1,885,314	$ (946,200)	
Non-operating revenues	$ 1,753	$ 8,858	$ (7,105)	
Change in net assets	$ 940,867	$ 1,894,172	$ (953,305)	

Note 1 – The increase in operating expenses is related to net losses incurred from the expansion of the Clinics.

Note 2 – The decrease in operating revenue relates to a decrease in settlement funds, offset by increased revenues from the Clinics.

Capital Assets

At the end of fiscal year 2011, the cost of infrastructure and other capital assets recorded in the District's financial statements was as shown in Table 2 below.

Table 2
Capital Assets at Year End

	Balance at June 30, 2011
Land and improvements	$ 2,243,596
Building	25,079,033
Construction in progress	-
Equipment	19,961,931
Less accumulated depreciation	(40,049,850)
Capital assets, net of accumulated depreciation	$ 7,234,710

Debt Administration

On June 30, 2010, the District transferred all of its long-term debt to MGH.

Economic Outlook and Major Initiatives

Economic factors do not have a direct influence on the District's budget. The current lease, effective for fiscal year 2012 and as amended by the Transfer Agreements, requires MGH to pay $98,784 of rent quarterly, irrespective of MGH's net earnings. In addition, the District recognizes $95,133 of deferred lease revenue on a monthly basis. Similarly, the Transfer Agreements require a set annual payment to support the District's expenses, irrespective of economic conditions.

Contacting the District's Financial Management

This financial report is intended to provide citizens, taxpayers, and creditors with a general overview of the District's finances. Questions about this report should be directed to Marin Healthcare District to the attention of the Executive Director or the Chair of Management, Finance and Audit Committee, at 415-464-2090.

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REPORT OF INDEPENDENT AUDITORS

To the Board of Directors
Marin Healthcare District

We have audited the accompanying statement of net assets of Marin Healthcare District (the District) as of June 30, 2011 and 2010 and the related statement of revenues, expenses, and changes in net assets and cash flows for the years then ended. The financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of June 30, 2011 and 2010, and the respective changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis on pages 1 through 4 is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures to this information, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and we express no opinion on it.

Moss Adams LLP

Stockton, California
September 29, 2011

MARIN HEALTHCARE DISTRICT

ASSETS

	JUNE 30, 2011	JUNE 30, 2010
CURRENT ASSETS		
Cash and cash equivalents	$ 2,973,655	$ 1,745,405
Patient accounts receivable, net of allowance for doubtful accounts of $19,547 in 2011	253,510	50,723
Other receivables	76,523	4,082,477
Total current assets	3,303,688	5,878,605
Deposits	107,200	42,500
Other long-term receivables	910,691	923,445
Capital assets, net of accumulated depreciation	7,234,710	7,577,779
	$ 11,556,289	$ 14,422,329

LIABILITIES AND NET ASSETS

	2011	2010
CURRENT LIABILITIES		
Accounts payable	$ 311,031	$ 2,459,278
Accrued expenses	1,800	487,728
Accrued election expense	31,200	62,336
Current portion of deferred lease revenue	1,141,598	1,141,598
Total current liabilities	1,485,629	4,150,940
Other long-term liabilities	3,750,843	4,892,439
Total liabilities	5,236,472	9,043,379
NET ASSETS (DEFICIT)		
Invested in capital assets net of related debt	7,234,710	7,577,779
Unrestricted	(914,893)	(2,198,829)
Total net assets	6,319,817	5,378,950
Total liabilities and net assets	$ 11,556,289	$ 14,422,329

	YEARS ENDED JUNE 30,	
	2011	2010
OPERATING REVENUE		
Lease income	$ 1,535,918	$ 1,520,337
Net patient service revenue	959,423	199,010
Settlement transition	176,500	1,423,445
Total operating revenues	2,671,841	3,142,792
OPERATING EXPENSES		
Depreciation	389,220	433,316
Administration	1,343,507	824,162
Total operating expenses	1,732,727	1,257,478
OPERATING INCOME	939,114	1,885,314
NON-OPERATING REVENUE		
Other revenue	1,753	8,858
Total non-operating revenue	1,753	8,858
NET INCOME	940,867	1,894,172
NET ASSETS, beginning of year	5,378,950	3,484,778
NET ASSETS, end of year	$ 6,319,817	$ 5,378,950

MARIN HEALTHCARE DISTRICT
STATEMENTS OF CASH FLOWS

	YEARS ENDED JUNE 30,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from tenants	$ 6,335,983	$ 291,680
Receipts from patients	755,954	150,626
Receipts from settlement	189,254	500,000
Payments to employees	(1,106,345)	(164,780)
Payments to suppliers and others	(4,902,198)	(2,061,687)
Net cash from operating activities	1,272,648	(1,284,161)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital asset purchases	(46,151)	(19,894,206)
Loan proceeds	-	21,370,802
Loan payments	-	(2,125,198)
Net cash from capital and related financing activities	(46,151)	(648,602)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest earned	1,753	8,858
Net cash from investing activities	1,753	8,858
NET CHANGE IN CASH AND CASH EQUIVALENTS	1,228,250	(1,923,905)
CASH AND CASH EQUIVALENTS, beginning of year	1,745,405	3,669,310
CASH AND CASH EQUIVALENTS, end of year	$ 2,973,655	$ 1,745,405

	YEARS ENDED JUNE 30,	
	2011	2010
RECONCILIATION OF OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Operating income	$ 939,114	$ 1,885,314
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation	389,220	433,316
Changes in certain assets and liabilities:		
Prepaid items	(64,700)	(31,500)
Patient accounts receivable	(202,787)	(50,723)
Other receivables	4,018,708	(4,077,271)
Accounts payable	(2,148,247)	1,484,912
Other long-term liabilities	(1,141,596)	(1,228,657)
Accrued expenses	(517,064)	300,448
Net cash from operating activities	$ 1,272,648	$ (1,284,161)

NON-CASH CAPITAL FINANCING ACTIVITY:

On June 30, 2010, the District transferred a total of $29,361,656 in long-term debt and $32,290,037 in construction in progress to Marin General Hospital (MGH), a California non-profit public benefit corporation, as part of the transfer of control (Note 6).

NOTE 1 – BASIS OF PRESENTATION AND ACCOUNTING POLICIES

Reporting entity – Marin Healthcare District (the District) is a political subdivision of the state of California. District directors are elected officials whose sole mission is to promote the health and welfare of the residents of the communities served by the District. The District operated the Marin General Hospital facility (the Hospital facility) until 1985, when it reorganized in compliance with local hospital district law of the state of California.

The District's principal asset is hospital property, plant, and equipment. The hospital is a general acute-care facility located in Marin County, California, and provides inpatient and outpatient healthcare services. Inpatient facilities consist of medical-surgical, pediatrics, maternity, nursery, intensive care, coronary, psychology, and radiology and laboratory services. The hospital facility is leased to MGH.

The District was the sole member of Marin General Hospital Foundation (the Foundation), a California not-for-profit public benefit corporation whose mission is to inspire philanthropy for the benefit of MGH, effective as of January 1, 2009. The Foundation's bylaws were amended such that MGH became the sole member of the Foundation effective as of June 30, 2010. The Foundation is consolidated with MGH for financial reporting purposes and correspondingly is not included in the District reporting entity for either period presented.

In addition to overseeing MGH's compliance with the lease agreement, the District is a forum for discussion of local healthcare issues, promotes healthcare services within the community, and acts on behalf of the public as an advocate of high quality, reasonably priced healthcare services.

The financial statements of the District include the accounts of the District and includes four healthcare clinics (the Clinics). The District formed the Clinics, pursuant to California Health and Safety Code Section 1206(b). The Clinics contract with physicians to provide health care services within the District's geographic boundaries. The Clinics' operations were not significant in 2010.

Proprietary fund accounting – The activities of the District are accounted for as an Enterprise Fund. Enterprise Funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under the method, revenues are recorded when earned and expenses are recorded at the time obligations are incurred.

NOTE 1 – BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

Accounting standards – In compliance with Governmental Accounting Standards Board (GASB) Statement No. 20, the District has chosen to apply all applicable GASB pronouncements and all Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins issued on or before November 30, 1989, unless they conflict with or contradict GASB pronouncements.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Non-operating revenues, such as subsidies and investment earnings, result from non-exchange transactions or ancillary activities.

The District may fund programs with a combination of cost-reimbursement grants, categorical block grants, and general revenues. Thus, both restricted and unrestricted net assets may be available to finance program expenditures. The District's policy is to first apply restricted grant resources to such programs, followed by general revenues if necessary.

Use of estimates – The financial statements have been prepared in conformity with U.S. generally accepted accounting principles, and as such, include amounts based on informed estimates and judgments of management with consideration given to materiality. Actual results could differ from those estimates.

Net assets – Net assets is the excess of all the District's assets over all its liabilities, regardless of fund. Net assets are divided into captions under GASB Statement No. 34. These captions apply only to net assets, which is determined only at the government-wide level, and are described below:

Invested in capital, net of related debt: the portion of the net assets that is represented by the current net book value of the District's capital assets, less the outstanding balance of any debt issued to finance these assets.

Restricted: the portion of net assets that is restricted as to use by the terms and conditions of agreements with outside parties, governmental regulations, laws, or other restrictions which the District cannot unilaterally alter. The District has no restricted net assets.

Unrestricted: the portion of net assets that is not restricted to use.

Cash and cash equivalents – Cash and cash equivalents include cash in bank checking, money market funds and investments in highly liquid debt instruments with a maturity of three months or less when purchased.

Capital assets – Capital assets are recorded at cost. Depreciation is provided on the straight-line basis over the estimated useful lives of the assets. The capitalization threshold is $5,000.

Risk management – The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters for which the District carries commercial insurance.

The Clinics are insured under MGH's insurance policy. MGH is insured for professional and general liability. The professional and general liability coverage is for a claims-made policy, which limits coverage to claims that are reported to the insurance company during the policy year.

NOTE 1 – BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

Deferred revenue - lease – Deferred revenue represents capital expenditures by MGH in excess of the current commitment, which will be recognized as rental revenue in future years (Note 4).

Lease income – The District recognizes lease income and reimbursement of operating expenses when earned. The District derives substantially all of its lease income from MGH. The annual rent pursuant to the 30-year lease agreement with MGH, as amended by the Transfer Agreements, is $1,500,000, most of which MGH has prepaid in the form of capital expenditures on the Hospital facility, and MGH also reimburses the District for administrative expenses through quarterly cash payments, which are increased annually by 5% (Note 4).

Patient service revenue and credit concentrations – The District's patient service revenues is recognized when health care services are provided to patients at the Clinics. Net patient service revenue is reported at the estimated net realizable amount from patients, governmental programs, health maintenance, and preferred provider organizations and insurance contracts under applicable laws, regulations, and program instructions. Net realizable amounts are generally less than the District's established rates.

The District provides estimated losses on accounts receivable based on prior bad debt experience. No interest is charged on past due balances. Past due status is based on the date of services provided. Recoveries from previously charged-off accounts are recorded when received.

The mix of receivables from patients and third-party payors is as follows:

	June 30, 2011
Medicare	30%
Medi-Cal	10%
Other	60%
	100%

Operating revenues and expenses – The District's statement of revenues, expenses, and changes in net assets distinguishes between operating and non-operating revenues and expenses. Operating revenues result from leasing the hospital facility to MGH and providing health care services to patients at the Clinics. Non-exchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as non-operating revenues. Operating expenses are all expenses incurred in order to lease the hospital facility and to provide health care services, other than financing costs.

NOTE 1 – BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

New accounting pronouncements – In December 2010, GASB issued GASB Statement No. 62, *Codification of Accounting and Financial Reporting Contained in Pre-November 30, 1989 and AICPA Pronouncements*, which incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements. This pronouncement is effective for periods beginning after December 15, 2011.

Grants and contributions – The District may periodically receive grants and contributions from other governmental entities, individuals, or private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses.

NOTE 2 – CASH AND INVESTMENTS

Cash balances from all funds are combined and invested to the extent possible pursuant to the District Board approved Investment Policy and Guidelines and Statement Government Code. The District's investments are carried at fair value.

Authorized investments – In accordance with Section 53601 of the California Government Code, the District may invest in the following types of investments:

Securities of the U.S. government, or its agencies
Negotiable certificates of deposits
Local Agency Investment Fund (State Pool) deposits

Custodial credit risk – Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for deposits and investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party.

California law requires banks and savings and loan associations to pledge government securities with a market value of 110% of the District's cash on deposit or first trust deed mortgage notes with a value of 150% of the deposit as collateral for these deposits. Under California law, this collateral is held in the District's name and places the District ahead of general creditors of the institution.

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

The District places certain funds with the state of California's Local Agency Investment Fund (LAIF). The District is a voluntary participant in LAIF, which is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the state of California and the Pooled Money Investment Board. The state Treasurer's office pools these funds with those of other governmental agencies in the state and invests the cash. The fair value of the District's investment in this pool is reported in the accompanying financial statements based upon the District's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The monies held in the pooled investment funds are not subject to categorization by risk category. The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on the amortized cost basis. Funds are accessible and transferable to the master account with 24 hours notice. Financial statements for LAIF can be obtained from the California State Treasurer's Office, 915 Capitol Mall, Suite 110, Sacramento, California, 95814.

The management of the state of California Pooled Money Investment Account has indicated to the District that as of June 30, 2011 and 2010 the estimated market value of the pool (including accrued interest) was $26,990,453 and $26,853,337, respectively. The District's proportionate share of that value is $297,007 and $295,563 as of June 30, 2011 and 2010, respectively.

NOTE 3 – CAPITAL ASSETS

The following is a summary of changes in capital assets during the years ended June 30:

	Life (Years)	Balance, June 30, 2010	Additions	Deletions	Balance, June 30, 2011
Equipment	3 – 20	$ 18,784,416	$ -	$ -	$ 18,784,416
Hospital buildings	40	24,974,084	-	-	24,974,084
Construction in progress (not depreciated)	N/A	-	-	-	-
Parking structure	40	2,324	-	-	2,324
Phase 1 building	40	102,625	-	-	102,625
Land (not depreciated)	N/A	865,701	-	-	865,701
Other improvements	40	596,491	-	-	596,491
Parking improvements	40	781,404	-	-	781,404
Moveable equipment	3 – 20	1,131,364	46,151	-	1,177,515
Subtotal		47,238,409	46,151	-	47,284,560
Less accumulated depreciation		(39,660,630)	(389,220)	-	(40,049,850)
Capital assets, net of accumulated depreciation		$ 7,577,779	$ (343,069)	$ -	$ 7,234,710

NOTE 3 – CAPITAL ASSETS (CONTINUED)

	Life (Years)	Balance, June 30, 2009	Additions	Deletions	Balance, June 30, 2010
Equipment	3 – 20	$ 18,784,416	$ -	$ -	$ 18,784,416
Hospital buildings	40	24,974,084	-	-	24,974,084
Construction in progress (not depreciated)	N/A	12,436,467	19,853,570	(32,290,037)	-
Parking structure	40	2,324	-	-	2,324
Phase 1 building	40	102,625	-	-	102,625
Land (not depreciated)	N/A	865,701	-	-	865,701
Other improvements	40	596,491	-	-	596,491
Parking improvements	40	781,404	-	-	781,404
Moveable equipment	3 – 20	1,090,728	40,636	-	1,131,364
Subtotal		59,634,240	19,894,206	(32,290,037)	47,238,409
Less accumulated depreciation		(39,227,314)	(433,316)	-	(39,660,630)
Capital assets, net of accumulated depreciation		$ 20,406,926	$ 19,460,890	$ (32,290,037)	$ 7,577,779

The District's property, plant, and equipment are leased to and used exclusively by MGH. Depreciation expense for the years ended June 30, 2011 and 2010, was $389,220 and $433,316, respectively.

NOTE 4 – LEASE OF MARIN HEALTHCARE DISTRICT FACILITY

Annual rental payments – Effective December 1, 1985, the District leased the Marin General Hospital facility to MGH for a term of 30 years pursuant to Section 32126 of the Local Hospital District Law. Per the amended lease agreement dated August 25, 1987, as further amended by the Transfer Agreements (Note 5), the annual rent payments comprise capital expenditures made by MGH and quarterly payments of approximately $94,000 for 2011. The minimum cash payment, which is payable in quarterly installments, increases annually by 5% throughout the lease term.

Due to the significant capital investment required for the hospital modernization program completed in June 1989, MGH's rental payment commitment for capital expenditures due under the entire lease has been satisfied. The advanced capital commitment (including the excess capital commitment) has been recorded as deferred revenue. The total deferred lease revenue was $4,892,441 and $6,034,037 as of June 30, 2011 and 2010, respectively.

NOTE 4 – LEASE OF MARIN HEALTHCARE DISTRICT FACILITY (CONTINUED)

The deferred lease revenue will be amortized over the remaining term of the lease, which ends on December 1, 2015. Future amortization of deferred lease revenue is as follows:

Fiscal Year End	Amortization	Cash Payment	Total
2012	$ 1,141,598	$ 395,138	$ 1,536,736
2013	1,141,598	414,895	1,556,493
2014	1,141,598	435,640	1,577,238
2015	1,141,598	457,422	1,599,020
2016	326,049	200,122	526,171
Total	$ 4,892,441	$ 1,903,217	$ 6,795,658

Capital improvement payments – In addition to the capital obligation described under annual rental payments, the lease agreement, as amended by the Transfer Agreements, required MGH to make minimum annual capital expenditures (buildings and equipment) during the settlement period. The obligation was approximately $2.90 million for the year ended June 30, 2010. The District did not have a capital obligation for the year ended June 30, 2011.

Effective June 30, 2010, the lease agreement between the District and MGH was amended. The amended lease agreement requires that MGH provide financial support to the District relating to the operation of the Clinics. MGH provided $453,538 to the District for the operation of the Clinics in 2011.

NOTE 5 – SETTLEMENT

In June 2005, MGH, which was operated by and under the control of Sutter Health, a northern California-based not-for-profit integrated health care system (Sutter), filed a lawsuit for declaratory relief against the District. At issue was whether the lessor or the lessee was responsible for the seismic upgrade of the Hospital facility as required by California Senate Bill 1953, enacted in 1994 (the Hospital Seismic Upgrade Act).

The parties signed a settlement agreement (Settlement Agreement) dated October 4, 2006. The Settlement Agreement incorporates a transfer agreement and an interim funding agreement (collectively, Transfer Agreements) that describe contractual rights and obligations of the parties with respect to the Transfer through which the District became the sole corporate member of MGH on June 30, 2010 (the Transfer). Under the Transfer Agreements, the District assumed full responsibility and all financial liability associated with pre-transfer compliance with the Hospital Seismic Upgrade Act (SB 1953), including necessary extensions for compliance. The deadline for compliance with SB 1953 is January 1, 2015. As part of that transfer of control, MGH assumed all liabilities of the District related to the Transfer Agreements. As part of the transfer of control, the District and MGH were required to replace the hospital's information technology system and other programs and contracts such as major purchasing agreements, managed care agreements, and insurance. These items were purchased and installed in 2010.

NOTE 5 – SETTLEMENT (CONTINUED)

In 2010, the District made a loan of $1,081,405 to a Medical Foundation that was formed by MGH and a local physician's group. The Medical Foundation's purpose is establishing, operating and maintaining multi-specialty medical clinics. As of June 30, 2010, the District transferred the note receivable due from the Medical Foundation to MGH who has recorded the investment as a beneficial interest asset.

As of June 30, 2010, the District had a receivable due from MGH of $4,057,181 relating to the Transfer and the formation of the Medical Foundation.

The Transfer Agreements allow, and the District has created, an appointed subsidiary operating Board of Directors (Board) to provide oversight and run the day to day operations of MGH after the District becomes the sole corporate member of MGH. The Board has the sole authority to operate the hospital.

NOTE 6 – LOANS PAYABLE AND PURCHASE OBLIGATION

Pursuant to the Interim Funding Agreement executed along with the Transfer Agreements on October 4, 2006, the District has received funding from Sutter for the establishment of a transition team to implement the Transfer Agreements. These agreements relate to the resolution of legal proceedings from June 30, 2005. Under the Interim Funding Agreement, the District has received $500,000 on July 1 and January 1 of each year January 2007 through 2010. In addition, as of the Transfer, the District was responsible for executing a promissory note to pay back one half of all amounts provided under the Interim Funding Agreement plus interest at the prime rate plus two percent. The District had accrued $1,525,938 in principal and interest due under this arrangement at June 30, 2009. Total principal and interest payments of $2,125,198 were made under this arrangement in June 2010 upon transfer, and the obligation is considered satisfied in full.

On November 8, 2008, the District entered into a loan agreement with the County of Marin for an amount up to $20,000,000. The funds were needed to make preparation for the Transfer. The interest rate is prime plus one percent. The term of the loan will end no later than 75 days after the Transfer date, or no later than September 13, 2010. The District had $4.5 million outstanding under this arrangement at June 30, 2009 and borrowed another $8,000,000 during 2010. That amount outstanding ($12.5 million), along with accrued interest, was transferred to MGH as a hospital obligation upon transfer of control. As of June 30, 2010, the District did not have any amounts outstanding under this arrangement.

The District entered into a loan agreement with ACS Healthcare Solutions for the implementation of information technology upgrades to Marin General Hospital. The District is contractually committed for up to $14,000,000, which may be increased through change orders prior to the Hospital transfer date. As of June 30, 2010 and 2009, the outstanding balance of the loan is $0 and $6,053,177, respectively. This obligation was transferred to MGH as a hospital obligation upon transfer of control.

In June 2010, the District borrowed $2,000,000 from the Foundation. The loan bears an interest rate of 6% per annum. The outstanding balance of $2,000,000, along with accrued interest, was transferred to MGH as a hospital obligation upon transfer of control and was included in the District's receivable due from MGH as of June 30, 2010. As of June 30, 2010, the District did not have any amounts outstanding under this arrangement. In July 2010, MGH remitted the balance due to the Foundation to the District who then remitted payment to the Foundation.

NOTE 7 – COMMITMENTS

Compliance with the Hospital Seismic Upgrade Act – Pursuant to settlement, the District became the sole corporate member of MGH as of June 30, 2010. Pursuant to the Transfer Agreements, the District has assumed full responsibility and all financial liability for compliance SB 1953. The District estimates seismic architectural and engineering costs of approximately $35,000,000.

NOTE 8 – CONTINGENT LIABILITIES

Pending litigation – The District and MGH have alleged that Sutter has breached its fiduciary duty to MGH, as well as other breaches of the Transfer Agreements (Note 5). Sutter has filed certain counterclaims against the District and MGH. The parties are currently in arbitration relating to the claims and counterclaims. The likelihood of adverse outcome related to these matters at this time cannot be estimated; however, management believes that the ultimate resolution will not have a materially adverse effect on the District's financial position. As of June 30, 2011 and 2010, the District has $910,691and $923,445 due from Sutter, respectively.

NOTE 9 – OPERATING LEASES

The District and the Clinics lease office facilities under a non-cancelable operating lease. The total cost for the leases were $223,833 for the fiscal year ended June 30, 2011. The future minimum lease payments were as follows:

Years Ending June 30,	Amount
2012	$ 180,346
2013	173,485
2014	117,311
2015	123,539
2016	123,539
Thereafter	92,654
	$ 810,874

NOTE 10 – MANAGEMENT SERVICES AGREEMENT AND SUBSEQUENT EVENTS

The District entered into a management services agreement with MGH effective June 30, 2010. The agreement requires that the District's senior management team, legal counsel, and consultants provide MGH with services. In consideration of the service provided, MGH would reimburse the District for costs incurred. The agreement terminates on June 30, 2011. As of June 30, 2011, the District has $76,523 due from MGH relating to this agreement. Effective July 1, 2011, the District's senior management team became employees of MGH and will provide management services to the District on a contract basis.