

Draft

09/25/07

**ALAMEDA ALLIANCE FOR HEALTH AND  
ALAMEDA ALLIANCE JOINT POWERS  
AUTHORITY**

**INDEPENDENT AUDITOR'S REPORT  
AND  
COMBINED FINANCIAL STATEMENTS**

**JUNE 30, 2007 AND 2006**

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## INTRODUCTION

In accordance with the Governmental Accounting Standard's Board ("GASB") Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, Alameda Alliance for Health and Alameda Alliance Joint Powers Authority (collective the "Alliance") present comparative financial highlights as of and for the fiscal years ended June 30, 2007 and 2006. This discussion and analysis should be read in conjunction with the combined financial statements in this report.

Alameda Alliance for Health is a licensed health maintenance organization that operates in Alameda County (the "County"). The County's Board of Supervisors established Alameda Alliance for Health in March 1994 in accordance with State of California Welfare and Institutions Code (the "Code") Section 14087.54. This legislation provides that the Alliance is a public entity, separate and apart from the County and is not considered to be an agency, division or department of the County. Alameda Alliance for Health is not governed by, nor is it subject to, the Charter of the County and is not subject to the County's policies or operational rules. Alameda Alliance for Health received its Knox-Keene license in September 1995 and commenced operations in January 1996.

Alameda Alliance for Health operates the Alameda Alliance Joint Powers Authority (the "JPA"), a licensed health maintenance organization that operates in the County. The County's Board of Supervisors established the JPA in October 2005 in accordance with State of California Welfare and Institutions Code Section 14087.54. This legislation provides that the JPA is also a public entity, separate and apart from the County, and is not considered to be an agency, division, or department of the County. The JPA is not governed by, nor is it subject to, the Charter of the County and is not subject to the County's policies or operational rules. The JPA received its Knox-Keene license and commenced operations in December 2005. Alameda Alliance for Health and the JPA has a mutual guarantee agreement, insuring mutual solvency for the two organizations.

The mission and purpose of the Alliance is to develop, govern and administer a comprehensive health care delivery system that will provide quality health care to Medi-Cal eligible residents and other populations in the County. No individual or entity has any ownership interest in the Alliance and all accumulated net assets are available to invest in programs which support its mission.

Alameda Alliance for Health contracts with the California Department of Healthcare Services ("CDHCS") to provide health care services to the Medi-Cal eligible County residents who are enrolled as members of the Alliance "CDHCS Contract"). The current CDHCS Contract is effective through December 31, 2008. The CDHCS Contract specifies capitation rates which may be adjusted annually. CDHCS revenue is paid monthly and is based upon contracted rates and actual Medi-Cal enrollment. The Alliance, in turn, has contracted with hospitals and physicians whereby capitation payments (agreed-upon monthly payments per member) and fee-for-service payments are made in return for contracted health care services for its members. Provider contracts are typically evergreen and contact annual rate change and termination provisions.

## **INTRODUCTION (continued)**

Alameda Alliance for Health contracts with the California Managed Risk Medical Insurance Board's Healthy Families Program to provide health care benefits to certain children whose families do not qualify for Medi-Cal and cannot afford to purchase insurance out-of-pocket. The current contract is effective through June 30, 2008, and was assigned to the JPA effective December 1, 2005.

Alliance Group Care began accepting members on June 1, 2001 and offers health coverage to In Home Supportive Service ("IHSS") home care workers in the County. The current contract is automatically renewed on an annual basis, absent adequate written notice to terminate by either party. This contract was assigned to the JPA effective December 1, 2005. Alliance Healthy Kids began accepting members in October 2005 and offers medical coverage to children of parents not otherwise eligible for either the Medi-Cal or Healthy Families programs. This program was assigned to the JPA effective December 1, 2005. In November 2005, CDHCS implemented the Quality Improvement Fee ("QIF") program. This program imposes a 6% assessment on all non-Medicare revenue. CDHCS uses these assessments to obtain matching Federal funds, a portion of which is returned to the Alliance in the form of a Medi-Cal rate increase. In order to minimize the impact on the Alliance, the JPA was created. Effective December 1, 2006, all non-Med-Cal members were assigned to the JPA, thus reducing the resulting assessment levied on the Alliance.

In November 2005, CDHCS implemented the Quality Improvement Fee ("QIF") program. This program imposes a 6% assessment on all non-Medicare revenue. CDHCS uses this assessment to obtain matching Federal funds, of which a portion is returned to the Alliance in the form of a Medi-Cal rate increase. In order to minimize the impact on the Alliance, the JPA was created. Effective December 1, 2006, all non-Med-Cal members were assigned to the JPA, thus reducing the resulting assessment levied on the Alliance.

## **Using This Annual Report**

The Alliance's combined financial statements consist of three statements – a Balance Sheet; Statements of Revenues, Expenses and Changes in Net Assets; and a Statement of Cash Flows. These combined financial statements and related notes provide information about the activities of the Alliance, including resources held by the Alliance but restricted or designated for specific purposes. The combined financial statements include Alameda Alliance for Health and the JPA as they are under common management and control.

## **The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Assets**

The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Assets report information about the Alliance's resources and activities during the period. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All revenue and expenses are included regardless of when cash is received or paid.

These two combined financial statements report the Alliance's net assets and changes in net assets. Over time, increases and decreases in the Alliance's net asset are indicators of whether its financial health is improving or deteriorating. Other non-financial factors should also be considered, such as changes in the Alliance's membership, measures of quality service provided to members and local economic factors to assess the overall health of the Alliance.

### **The Statement of Cash Flows**

The final required statement is the Statement of Cash Flows. This statement reports cash receipts, cash payments and net changes in cash resulting from operations, investing and financing activities.

### **Overview of the Combined Financial Statements and Financial Analysis**

On June 30, 2007, the Alliance had assets of \$41,475,357 and liabilities of \$16,346,701. The resulting net assets, which represent the Alliance's assets after the liabilities are deducted, decreased \$1,153,774 to \$25,128,656 at June 30, 2007, compared to \$26,282,430 at June 30, 2006. The change in net assets is due to the net loss of sustained during the 2007 fiscal year.

### **ASSETS**

#### **Cash and Cash Equivalents**

Cash increased \$3,436,224 from \$1,464,575 at June 30, 2006 to \$4,900,799 at June 30, 2007. The increase is mainly due to cash generated by operating activities of \$1,196,975 offset by cash used in capital-related financing activities of \$573,445 and cash generated in investing activities of \$2,812,694.

#### **Investments**

Investments decreased \$1,519,048 from \$26,453,271 at June 30, 2006 to \$24,934,223 at June 30, 2007. The decrease is largely due to the timing of transfers to the cash accounts.

#### **Premiums Receivable**

Premiums receivable increased \$824,585 from \$2,216,690 at June 30, 2006 to \$3,041,275 at June 30, 2007, reflecting the timing of receipt of certain premium revenue due from the State of California and the County.

#### **Interest Receivable**

Interest receivable decreased \$55,195 from \$92,701 at June 30, 2006 to \$37,506 at June 30, 2007. The decrease is attributable to the timing of investment interest payments.

### **Reinsurance Recoveries Receivable**

Reinsurance recoveries receivable decreased \$434,572 from \$836,022 at June 30, 2006 to \$401,450 at June 30, 2007. The decrease results stems largely from declining premium rates paid.

### **Other Receivables**

Other receivables decreased \$409,174 from \$660,036 at June 30, 2006 to \$250,860 at June 30, 2007. The decrease results largely from the collection in 2007 of a provider overpayment outstanding at June 30, 2006.

### **Prepaid Expenses**

Prepaid expenses decreased \$29,172 from \$524,359 at June 30, 2006 to \$495,187 at June 30, 2007. The increase is attributable to the timing of payments for licenses, assessments, insurance, software support agreements and other costs to be charged to expense after June 30, 2007.

### **Restricted Assets**

Restricted assets consist of two components: restricted cash of not less than \$300,000 held in trust as required by the California Department of Managed Health Care and unexpended grant funds that must be used for specific purposes. Restricted cash increased \$7,512 from \$337,299 at June 30, 2006 to \$344,811 at June 30, 2007 due to an increase in investment market value. Unexpended temporarily-restricted grant funds increased \$222,982 from \$439,293 at June 30, 2006 to \$654,762 at June 30, 2007. The increase largely reflects the timing of grant funding received attributable to the Healthy Kids program.

### **Land, Building, Furniture and Equipment**

Net fixed assets increased by \$84,925 from \$6,984,321 at June 30, 2006, to \$7,069,246 at June 30, 2007. The overall increase reflects fixed asset acquisitions of \$573,445 less depreciation expense of \$488,520. Investments were made in additional furniture, computer hardware and computer software in fiscal year 2007.

## LIABILITIES

### Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses decreased \$112,797 from \$1,847,043 at June 30, 2006 to \$1,734,246 at June 30, 2007. The net decrease reflected a decrease in the payable to the California Department of Healthcare Services for the Quality Improvement Fee (QIF). Two months of QIF fee were payable at June 30, 2006 while only one month was payable at June 30, 2007. Partially offsetting the decrease in QIF payable is an increase in year-end trade payables and accrued expenses.

### Claims Payable

Claims payable represents the Alliance's estimated liability for healthcare and pharmacy expenses for which services have been performed but have not yet been paid by the Alliance. Claims payable includes the estimated value of claims that have been incurred but not yet reported to the Alliance as well as the estimated value of claims which have been received by the Alliance but not yet paid.

Total claims payable increased by \$4,075,931 from \$9,813,032 at June 30, 2006 to \$13,888,963 at June 30, 2007. Included in this change is an increase of \$4,368,209 in the liability for incurred-but-not-paid claims, and a decrease of \$292,278 in the liability for other medical payments. The change in the liability for incurred-but-not-paid claims from prior year is due to an increase in the cost of services and to an increase in both the quantity and magnitude of high-dollar inpatient expenses. The reduction in the liability for other medical payments is the result of timing of accruals.

### Other Current Liabilities

Other current liabilities comprise accrued payroll and any cash deficit. Other liabilities decreased \$903,277 from \$1,626,769 as of June 30, 2006 to \$723,492 as of June 30, 2007. Accrued payroll decreased \$219,099 because of the payment of staff bonuses accrued at June 30, 2006, in lieu of salary increases, and the cessation of that program in 2007. Included in the total is a cash deficit of \$684,179 at June 30, 2006 while no cash deficit existed at June 30, 2007.

**ALAMEDA ALLIANCE FOR HEALTH AND  
ALAMEDA ALLIANCE JOINT POWERS AUTHORITY  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
AS OF AND FOR THE YEARS ENDED JUNE 30, 2007 AND 2006**

Draft

**NET ASSETS**

Total net assets decreased \$1,153,744 to \$25,128,656 at June 30, 2007 compared to \$26,282,430 at June 30, 2006. The decrease is due to the following:

Net Operating Loss	(\$2,392,227)
Investment Income	<u>1,238,453</u>
Decrease in Net Assets	<u>(\$1,153,774)</u>

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

**Capitation and Premium Revenue and Membership**

Capitation and premium revenues of \$141,118,095 in fiscal year 2007 decreased \$2,089,607 or 1.5%, from \$143,207,300 in 2006. Medi-Cal enrollment decreased due to the CalWin redetermination process that disenrolled members who had not completed required certification paperwork. Partially offsetting this decrease was a 2% rate increase from CDHCS. Revenue in the Healthy Families plan decreased due to an 8% decline in enrollment. Group Care's revenue and membership increased 14% due to enrollment efforts made by the Public Authority. Healthy Kids premium revenue and enrollment increased during fiscal year 2007, the first full year of operations as the plan was launched during mid fiscal year 2006. The chart below summarizes member months:

	2007	2006	Increase (Decrease)	% Change
Medi-Cal	892,926	936,332	(43,506)	-5%
Healthy Families	90,729	98,557	(7,828)	-8%
Group Care	58,229	51,293	6,936	14%
Healthy Kids	12,417	5,283	7,134	135%
Total Member Months	<u>1,054,201</u>	<u>1,091,465</u>	<u>(37,264)</u>	<u>-3%</u>

**Health Care Expense**

Health care expense represents the Alliance's cost of providing physician, hospital, pharmacy, laboratory and other medical services to members. The Alliance has contracted with various health care providers whereby capitation payments (agreed-upon payments per member) and fee-for-service payments are made in return for contracted health care services for its members.

**ALAMEDA ALLIANCE FOR HEALTH AND  
ALAMEDA ALLIANCE JOINT POWERS AUTHORITY  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
AS OF AND FOR THE YEARS ENDED JUNE 30, 2007 AND 2006**

### Healthcare Expense (continued)

Health care expense increased \$5,507,433 or 4.4%, from \$124,369,242 in 2006 to \$129,876,676 in 2007. This change is largely due to a general increase in the cost of all services and an increase in both the frequency and acuity of high-dollar inpatient cases. The chart below shows the per-member-per-month (PMPM) effect of these costs:

	<u>2007</u>	<u>2006</u>	<u>2007 PMPM</u>	<u>2006 PMPM</u>	<u>PMPM % Change</u>
Physician Services	\$ 35,995,786	\$ 36,736,967	\$34.15	\$33.66	1 %
Inpatient Hospital and SNF	30,331,974	25,535,778	\$28.77	\$23.40	23 %
Ancillary Services	54,385,954	52,910,345	\$51.59	\$48.48	6 %
Emergency Services	5,571,338	5,162,914	\$5.28	\$4.73	12 %
Other Benefits	<u>3,705,455</u>	<u>3,666,262</u>	<u>\$3.51</u>	<u>\$3.36</u>	<u>5 %</u>
Subtotal	129,990,507	124,012,266	\$123.31	\$113.62	9 %
Reinsurance Expense (net)	<u>(113,831)</u>	<u>356,976</u>	<u>-\$0.11</u>	<u>\$0.33</u>	<u>(133)%</u>
Total Healthcare Expenses	<u>\$ 129,876,676</u>	<u>\$ 124,369,242</u>	<u>\$123.20</u>	<u>\$113.95</u>	<u>8 %</u>

### Medical Reinsurance

Medical reinsurance expense reflects reinsurance premium payments offset by refunds received. Net medical reinsurance expense decreased from \$356,976 in 2006 to a net recovery of \$113,831 in 2007. The change was attributable to significantly lower premiums based on prior year healthcare expenses, membership decreases and increased recoveries.

### Marketing, General and Administrative Expense

Marketing, general and administrative expense increased \$986,919 or 8% from \$13,133,051 in 2006 to \$14,119,970 in 2007. This reflects increased expenses in preparation for the launch of the Medicare SNP program, expected to commence operations in January 2008.

### Non-Operating Income

Non-operating income consists of investment income, rental income and gain/loss on disposal of fixed assets. Non-operating income increased \$232,718 from \$1,005,735 in 2006 to \$1,238,453 in 2007. The increase is primarily due to higher investment balances and yields. Rental income declined from \$395,672 in 2006 to \$0 in 2007 as the existing lease ended and no replacement tenant was secured. Loss on fixed asset disposals declined from \$111,799 in 2006 to \$0 in 2007 as no disposals occurred in 2007.

### Liquidity and Capital Reserves

Cash and investments increased \$1,701,706 from \$27,917,846 at June 30, 2006 to \$29,835,022 at June 30, 2007. Management of the Alliance believes it has adequate liquidity to meet its operating and cash flow needs for the foreseeable future.

To the Board of Governors of  
Alameda Alliance for Health and  
Alameda Alliance Joint Powers Authority

We have audited the accompanying combined balance sheets of Alameda Alliance for Health and the Alameda Alliance Joint Powers Authority (collectively the “Alliance”), both of which are under common management and control, as of June 30, 2007, and the related combined statements of revenues, expenses, and changes in net assets, and cash flows for the year then ended. These combined financial statements are the responsibility of the Alliance’s management. Our responsibility is to express an opinion on these combined financial statements based on our audit. The financial statements of the Alliance as of and for the year ended June 30, 2006 were audited by another auditor whose opinion dated September 15, 2006 expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined 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 Alliance’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 combined 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 audit provides a reasonable basis for our opinion.

In our opinion, such combined financial statements present fairly, in all material respects, the combined financial position of Alameda Alliance for Health and the Alameda Alliance Joint Powers Authority as of June 30, 2007, and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management’s Discussion and Analysis on pages 1 through 7 is not a required part of the basic combined financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Alliance’s management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

San Francisco, California  
September \_\_, 2007

**ALAMEDA ALLIANCE FOR HEALTH AND  
ALAMEDA ALLIANCE JOINT POWERS AUTHORITY  
COMBINED BALANCE SHEETS  
AS OF JUNE 30, 2007 AND 2006**

**Draft**

	<u>2007</u>	<u>2006</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 4,900,799	\$ 1,464,575
Investments	24,934,223	26,453,271
Premiums receivable	3,041,275	2,216,690
Interest receivable	37,506	92,701
Reinsurance recoveries receivable	401,450	836,022
Other receivables	250,860	660,036
Prepaid expenses	<u>495,187</u>	<u>524,359</u>
Total current assets	<u>34,061,300</u>	<u>32,247,654</u>
Noncurrent cash and investments		
Restricted cash	<u>344,811</u>	<u>337,299</u>
Capital assets		
Land	1,557,283	1,557,283
Depreciable capital assets, net of accumulated depreciation	<u>5,511,963</u>	<u>5,427,038</u>
Total capital assets	<u>7,069,246</u>	<u>6,984,321</u>
Total	<u>\$ 41,475,357</u>	<u>\$ 39,569,274</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable and accrued expenses	\$ 1,734,246	\$ 1,847,043
Claims payable	13,888,963	9,813,032
Other liabilities	<u>723,492</u>	<u>1,626,769</u>
Total current liabilities	<u>16,346,701</u>	<u>13,286,844</u>
Net assets		
Invested in capital assets	7,069,246	6,984,321
Restricted		
Grants for specific operating purposes	654,762	439,292
Required by legislative authority	344,811	337,299
Unrestricted	<u>17,059,837</u>	<u>18,521,518</u>
Total net assets	<u>25,128,656</u>	<u>26,282,430</u>
Total	<u>\$ 41,475,357</u>	<u>\$ 39,569,274</u>

**ALAMEDA ALLIANCE FOR HEALTH AND  
ALAMEDA ALLIANCE JOINT POWERS AUTHORITY  
COMBINED STATEMENTS OF REVENUES, EXPENSES, AND  
CHANGES IN NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2007 AND 2006**

	2007	2006
Operating revenues		
Capitation and premium revenue	\$ 141,118,095	\$ 143,207,300
Grant contribution revenue	969,976	1,090,650
Other revenue	4,868	32,683
	142,092,939	144,330,633
Health care expenses		
Physician services	35,995,786	36,736,968
Hospital inpatient services	30,331,974	25,535,778
Ancillary services	54,385,954	52,910,345
Emergency services	5,571,338	5,162,913
Other member benefits	3,666,928	3,520,586
Medical reinsurance, net of recoveries	(113,831)	356,976
Other health care expenses	38,527	145,676
	129,876,676	124,369,242
Marketing, general, and administrative expenses	14,119,970	13,133,052
Depreciation expense	488,520	545,198
	144,485,166	138,047,492
Net income (loss) from operations	(2,392,227)	6,283,141
Non-operating income (loss)		
Investment income, net	1,238,453	721,862
Rental income	-	395,672
Loss on disposal of fixed assets	-	(111,799)
	1,238,453	1,005,735
Change in net assets	(1,153,774)	7,288,876
Net assets, beginning of year	26,282,430	18,993,554
Net assets, end of year	\$ 25,128,656	\$ 26,282,430

**ALAMEDA ALLIANCE FOR HEALTH AND  
ALAMEDA ALLIANCE JOINT POWERS AUTHORITY  
COMBINED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2007 AND 2006**

**Draft**

	<u>2007</u>	<u>2006</u>
Cash flows from operating activities		
Cash received from		
Capitation received from the State of California	\$ 128,557,777	\$ 131,975,892
Commercial premium revenue	11,950,475	10,321,222
Grants and restricted cash	1,040,808	1,357,802
Cash paid to providers for		
Medical and hospital expenses	(124,956,996)	(127,236,886)
Vendors and employees	(15,395,089)	(11,750,063)
	<u>1,196,975</u>	<u>4,667,967</u>
Cash flows used for capital and related financing activities		
Purchases of land, building, furniture, and equipment	(573,445)	(109,463)
Cash flows from investing activities		
Investment income	1,293,646	722,826
Purchases of investments	(478,103,507)	(319,408,256)
Proceeds from sale and maturities of investments	479,622,555	314,333,276
	<u>2,812,694</u>	<u>(4,352,154)</u>
Net increase in cash and cash equivalents	3,436,224	206,350
Cash and cash equivalents, beginning of year	<u>1,464,575</u>	<u>1,258,225</u>
Cash and cash equivalents, end of year	<u>\$ 4,900,799</u>	<u>\$ 1,464,575</u>
Reconciliation of change in net assets to net cash from operating activities		
Change in net assets	\$ (1,153,774)	\$ 7,288,876
Adjustments to reconcile change in net assets to net cash from operating activities		
Investment income, net	(1,238,453)	(721,862)
Depreciation	488,520	545,198
Net change in operating assets and liabilities		
Premiums receivable	(824,585)	(854,666)
Reinsurance recoveries receivable	434,572	282,099
Other receivables	409,176	954,708
Prepaid expenses	29,172	66,991
Restricted cash	(7,512)	12,701
Accounts payable and accrued expenses	(112,797)	1,373,261
Claims payable	4,075,931	(3,849,322)
Other liabilities	(903,275)	(541,816)
Loss on disposal of fixed assets	-	111,799
	<u>\$ 1,196,975</u>	<u>\$ 4,667,967</u>

**Note 1 – Organization**

Alameda Alliance for Health is a licensed health maintenance organization that operates in Alameda County (the “County”). The County’s Board of Supervisors established Alameda Alliance for Health in 1994 in accordance with State of California Welfare and Institutions Code (the “Code”) Section 14087.54. This legislation provides that Alameda Alliance for Health is a public entity, separate and apart from the County, and is not considered to be an agency, division, or department of the County. Further, Alameda Alliance for Health is not governed by, nor is it subject to, the Charter of the County and is not subject to the County’s policies or operational rules. Alameda Alliance for Health received its Knox-Keene license in December 1995 and commenced operations in January 1996.

The Alameda Alliance Joint Powers Authority (the “JPA”) is a licensed health maintenance organization that operates in the County. The County’s Board of Supervisors established the JPA in October 2005 in accordance with State of California Welfare and Institutions Code (the “Code”) Section 14087.54. This legislation provides that the JPA is a public entity, separate and apart from the County, and is not considered to be an agency, division, or department of the County. Further, the JPA is not governed by, nor is it subject to, the Charter of the County and is not subject to the County’s policies or operational rules. The JPA received its Knox-Keene license on December 1, 2005, and commenced operations in December 2005. Alameda Alliance for Health and the JPA have a mutual guarantee agreement, insuring mutual solvency for the two organizations

The mission and purpose of Alameda Alliance for Health and the JPA (collectively, the “Alliance”) is to develop, govern, and administer a comprehensive health care delivery system that will provide quality health care to Medi-Cal eligible residents of the County and other populations in the County. No individual or entity has any ownership interest in the Alliance, and all accumulated net assets are available to invest in programs which support its mission.

Alameda Alliance for Health has contracted with the California Department of Healthcare Services (“CDCHS”) to receive funding to provide health care services to the Medi-Cal eligible County residents who are enrolled as members of the Alliance (“CDHCS Contract”). The CDHCS Contract is effective January 1, 2004 through December 31, 2008. The CDHCS Contract specifies capitation rates which may be adjusted annually. CDHCS revenue is paid monthly and is based upon contracted rates and actual Medi-Cal enrollment. Alameda Alliance for Health, in turn, has contracted with hospitals and physicians whereby capitation payments (agreed-upon monthly payments per member) and fee-for-service payments are made in return for contracted health care services for its members. Provider contracts are typically evergreen and contain annual rate change provisions, termination clauses, and risk-sharing provisions.

Effective May 1, 1998, Alameda Alliance for Health contracted with the California Managed Risk Medical Insurance Board’s (“MRMIB”) Healthy Families Program (“Healthy Families”) to provide health care benefits to certain children whose families do not qualify for Medi-Cal and cannot afford to purchase insurance out-of-pocket. The current contract continues through June 30, 2008, and was assigned to the JPA effective December 1, 2005.

**Note 1 – Organization (continued)**

Alliance Group Care began accepting members on June 1, 2001, and offers health coverage to In Home Supportive Service (“IHSS”) home care workers in the County. The current contract is automatically renewed on an annual basis absent adequate written notice by either party. This contract was assigned to the JPA effective December 1, 2005.

On October 1, 2005, Alameda Alliance for Health launched its Healthy Kids program to provide medical coverage to children of parents not otherwise eligible for either the Medi-Cal or Healthy Families programs. This program was assigned to the JPA effective December 1, 2005.

In November 2005, CDHS implemented the Quality Improvement Fee (“QIF”) program. This program imposes an assessment on Alameda Alliance for Health’s revenue. CDHCS uses this assessment to obtain matching federal funds, of which a portion is returned to the Alliance in the form of a Medi-Cal rate increase. In order to minimize the impact on Alameda Alliance for Health, the JPA was created. Effective December 1, 2006, all non-Med-Cal programs were assigned to the JPA, thus reducing the resulting assessment levied on the Alliance.

**Note 2 – Summary of Significant Accounting Policies**

**Basis of Accounting and Accounting Standards** – Alameda Alliance for Health and the JPA are governmental health insuring organizations and, accordingly, follow governmental accounting standards and the provisions of the American Institute of Certified Public Accountants’ *Audit and Accounting Guide, Health Care Organizations*. The accrual basis of accounting is used in accordance with provisions for proprietary fund types.

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

**Basis of Combination** – The accompanying combined financial statements include the Alameda Alliance for Health and JPA. The operations of JPA are included from the date of its inception on December 1, 2005.

**Use of Estimates** – The preparation of combined financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the combined financial statements and the reported amounts of revenues and expenses during the reporting period. Capitation revenues, claims payable, and risk-sharing payable represent significant estimates. Actual results could differ from those estimates.

**Cash and Cash Equivalents** – The Alliance considers all highly liquid instruments with a maturity of three months or less at the time of purchase to be cash equivalents. Cash and Cash equivalents are carried at cost which approximates fair value.

**Note 2 – Summary of Significant Accounting Policies (continued)**

**Concentration of Credit Risk** - The Alliance is highly dependent upon the State of California for its revenues. Significant portion of accounts receivable and revenue are from the State of California.

**Investments** – Investments include debt obligations of the U.S. government and its agencies, mortgage-backed securities, corporate bonds, and money markets as permitted by the California Government Code for Investments. These investments are carried at fair market value. The fair values of investments are based on quoted market prices. Changes in the fair value of investments are included in investment income in the statements of revenues, expenses, and changes in net assets.

**Capital Assets** – Capital assets include land, building, furniture, equipment, and computer hardware and software. Capital assets are recorded at cost. Depreciation of building, furniture, and equipment is calculated using the straight-line method over 3 to 40 years which approximates the estimated useful lives of the assets. The Alliance capitalizes capital expenditures over \$1,000 which will have a useful life of three or more years.

**Restricted Cash** – The Alliance is required by the California Department of Managed Health Care to restrict cash having a fair value of at least \$300,000 for the payment of member claims in the event of its insolvency. The amounts recorded were \$344,811 and \$337,299 at June 30, 2007 and 2006, respectively. Restricted cash is comprised of money market funds and U.S. government securities and is stated at fair value.

**Net Assets** – Net assets are classified as invested in capital assets, restricted for specific operating activities or unrestricted. Invested in capital assets represents investments in land, building, furniture, and equipment, net of depreciation. Net assets restricted for specific operating activities represents the total cash balances that are restricted in their use as they represent grant monies received that must only be utilized for a specified purpose as agreed upon in the grant documents. Unrestricted net assets consist of net assets that do not meet the definition of restricted or invested in capital assets. Designated funds remain under the control of the Board of Governors, which may at its discretion later use the funds for other purposes.

Net assets restricted for specific operating activities are those whose use by the Alliance has been limited by donors for a specific purpose. During the year ended June 30, 2007, the Alliance was awarded grants in the amounts of \$629,794, \$300,000, \$31,935, \$5,000 and \$1,250 from the Tobacco Fund, the California Endowment Fund, Kaiser, First Five Alameda County and miscellaneous donations, respectively. During the year ended June 30, 2006, the Alliance was awarded grants in the amounts of \$400,000, \$334,605, \$280,001, and \$56,111 from the California Endowment Fund, Tobacco Fund, The California Healthcare Foundation, and First Five Alameda County, respectively. As of June 30, 2007 and 2006, \$654,762 and \$439,292, respectively, of these grants and other miscellaneous donations had not yet been used for the specified purposes. These amounts are classified as cash and cash equivalents.

**Note 2 – Summary of Significant Accounting Policies (continued)**

**Capitation and Premium Revenue** – Capitation revenue includes amounts received from the CDHS for Medi-Cal members and from MRMIB for Healthy Families members. Additional capitation revenue is received from the County for IHSS home care workers. Premium revenue is received from individual members for the Healthy Kids program.

Capitation and premium revenue is recorded as revenue in the month for which enrollees are entitled to health care service. A portion of revenues received from the CDHS is subject to possible retroactive adjustments. Provisions have been made for estimated retroactive adjustments.

**Grant Contribution Revenue** – From time to time, the Alliance receives grant contributions which are restricted as to their purpose by grantor organizations. Revenues from such grants are recognized as operating revenue when all requirements have been met, as they are restricted for specific operating purposes of the Alliance.

**Health Care Expense Recognition and Claims Payable** – The cost of health care services is recognized in the period provided and includes an estimate of the cost of services that have been incurred but not yet reported. The estimate for reserves for claims is based on actuarial projections of hospital and other costs using historical analysis of claims paid and authorization and admission data. Estimates are monitored and reviewed and, as settlements are made or estimates adjusted, differences are reflected in current operations. Such estimates are subject to the impact of changes in the regulatory environment and economic conditions.

**Operating Revenues and Expenses** – The Alliance’s statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. The primary operating revenue is derived from capitation and other sources in support of providing health care services to its members. Operating expenses are all expenses incurred to provide such health care services. Nonoperating revenues and expenses consist of those revenues and expenses that are related to financing and investing activities and result from net investment income and changes in the fair value of investments.

**Insurance Coverage** – The Alliance maintains its general liability insurance coverage through outside insurers in the form of “claims-made” policies. Should the “claims-made” policies not be renewed or replaced with equivalent insurance, claims related to the occurrences during the terms of the “claims-made” policies but reported subsequent to the termination of the insurance contract may be uninsured. These policies were renewed subsequent to year-end. Physicians and hospitals that the Alliance contracts with are required to maintain their own malpractice insurance coverage.

**Income Taxes** – The Alliance is a public entity established pursuant to Section 14087.54 of the Code and is further subject to the provisions of Ordinance No. 0-94-13 and related resolutions of the Board of Supervisors of the County. As a public entity defined by Internal Revenue Code Section 115, the Alliance is exempt from federal and state income taxes.

**Note 2 – Summary of Significant Accounting Policies (continued)**

**New Accounting Pronouncements** – In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets* effective for the fiscal periods beginning after June 15, 2009. Statement No. 51 requires the recognition of certain intangible assets. The Alliance is currently evaluating the effect, if any, that Statement No. 51 will have on its combined financial statements.

In July 2004, the GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, effective for the fiscal periods beginning after December 15, 2007, with an earlier adoption encouraged. Statement No. 45 requires accrual based measurement, recognition, and disclosure of other postemployment benefit (“OPEB”) expense, such as retiree medical and dental costs, over the employees’ years of service, along with the related liability, net of any plan assets. The Alliance is currently evaluating the effect, if any, that Statement No. 45 will have on its combined financial statements.

**Reclassifications** – Certain amounts in the 2006 combined financial statements have been reclassified to conform to the 2007 presentation. This reclassification has no effect on the 2006 operations or net assets.

**Note 3 – Cash and Investments**

Cash and investments as of June 30, 2007 and 2006, consist of the following:

	2007	2006
Cash on hand	\$ 1,500	\$ 1,500
Cash deposits	4,899,299	1,463,075
Investments	24,934,223	26,453,271
Total cash and investments	\$ 29,835,022	\$ 27,917,846

**Note 3 – Cash and Investments (continued)**

The Alliance’s Annual Investment Policy (“Policy”) sets forth the guidelines for the investment of all operating funds. The Policy conforms with the California Investment Code §53646 (“Investment Code”) as well as customary standards of prudent investment management. The objectives of the Alliance’s investment policy, in order of priority are safety of principal, maintenance of liquidity, and attainment of a market rate return that considers risk constraints and cash flow requirements. The table below identifies the investment types that are authorized for the Alliance. The table also identifies certain provisions that address interest rate risk, credit risk, and concentration of risk.

Authorized Investment Type	Maximum Maturity	Maximum Specified Percentage of Portfolio	Maximum Investment in One Issuer
U.S. Treasury Obligations	5 years	100 %	35 %
State of California Obligations	5 years	25	35
CA Local Agency Obligations	5 years	25	35
U.S. Agencies	5 years	100	35
Bankers' Acceptances	180 days	30	5
Comemrcial Paper	270 days	25	5
Negotiable Certificates of Deposit	1 year	30	5
Repurchase Agreemetns	30 days	100	5
Medium-Term Corporate Notes	5 years	30	5
Money Market Funds	N/A	20	5
Mortgage or Asset-Backed Securities	5 years	20	5
Variable and Floating Rate Securities	5 years	30	5

**Custodial Credit Risk** – Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the Alliance 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 Investment Code requires financial institutions to secure deposits made by public agencies by pledging securities in an undivided collateral pool held by a depository regulated under the state law. As of June 30, 2007 and 2006, the Alliance did not hold deposits exposed to custodial credit risk.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the Alliance will not be able to recover the value of its investment or collateral securities that are in the possession of another party. As of June 30, 2007 and 2006, the Alliance did not hold investments exposed to custodial credit risk.

**Note 3 – Cash and Investments (continued)**

**Interest Rate Risk** – Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. In accordance with its Policy, the Alliance manages the risk of market value fluctuations due to overall changes in the general level of interest rates by limiting the weighted-average maturity of its portfolio to no more than five years. The weighted-average maturity in years for the Alliance at June 30, 2007 and 2006, was as follows:

	2007	
	Fair Value	Weighted- Average Maturity (Years)
U.S. government agency obligations		
U.S. agency asset backed	\$ 996,250	0.21
Corporate obligations		
Domestic	276,645	0.08
Commercial paper	3,750,000	0.01
Repurchase agreement	10,313,000	0.00
Cash and money market fund	9,598,328	
Total fair value	\$ 24,934,223	
Portfolio weighted-average maturity		0.00
	2006	
	Fair Value	Weighted- Average Maturity (Years)
U.S. government agency obligations		
U.S. agency asset backed	\$ 4,239,594	0.60
Corporate obligations		
Domestic	1,728,226	0.55
Commercial paper	4,022,277	0.02
Repurchase agreement	1,478,998	0.00
Non-U.S. obligations	389,649	0.77
Asset-backed securities	321,658	0.44
Money market fund	14,272,869	
Total fair value	\$ 26,453,271	
Portfolio weighted-average maturity		0.15

Note 3 – Cash and Investments (continued)

**Credit Risk** – Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Per GASB Statement No. 40, *Deposit and Investment Risk disclosures—an amendment of GASB Statement No. 3*, unless there is information to the contrary, obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. Presented below is the minimum rating required by (where applicable) the California Government Code or the Alliance’s investment policy and the actual rating as of year-end for each investment type.

Rating, based on S&P, as of June 30, 2007:

Investment Type	Fair Value	AAA	AA	A	Unrated
U.S. government agency obligations					
U.S. agency asset backed	\$ 996,250	\$ -	\$ -	\$ -	\$ 996,250
Corporate obligations					
Domestic	276,645	-	276,645	-	-
Commercial paper	3,750,000	-	-	3,750,000	-
Repurchase agreement	10,313,000	-	-	-	10,313,000
Cash and money market fund	9,598,328	-	-	-	9,598,328
Total fair value	<u>\$ 24,934,223</u>	<u>\$ -</u>	<u>\$ 276,645</u>	<u>\$ 3,750,000</u>	<u>\$ 20,907,578</u>

Rating, based on S&P, as of June 30, 2006:

Investment Type	Fair Value	AAA	AA	A	Unrated
U.S. government agency obligations					
U.S. agency asset backed	\$ 4,239,594	\$ -	\$ -	\$ -	\$ 4,239,594
Corporate obligations					
Domestic	1,728,226	489,574	1,238,652	-	-
Commercial paper	4,022,277	-	-	4,022,277	-
Repurchase agreement	1,478,998	-	-	-	1,478,998
Non-U.S. obligations	389,649	-	389,649	-	-
Asset-backed securities	321,658	321,658	-	-	-
Money market fund	14,272,869	-	-	-	14,272,869
Total fair value	<u>\$ 26,453,271</u>	<u>\$ 811,232</u>	<u>\$ 1,628,301</u>	<u>\$ 4,022,277</u>	<u>\$ 19,991,461</u>

**Note 3 – Cash and Investments (continued)**

**Concentration of Credit Risk** – The investment policy of the Alliance contains certain limitations on the amount that can be invested in any one issuer and is listed in the table above. Investments in any one issuer (other than U.S. Treasury securities, mutual funds, and external investment pools) that represent 5% or more of the total Alliance’s investments for the years ended June 30, 2007 and 2006, are as follows:

Issuer	2007	
	Investment Type	Reported Amount
Federal Home Loan Mortgage Corporation	U.S. Agency	\$ 996,250
First Boston	Repurchase Agreement	9,079,000
Morgan Stanley	Repurchase Agreement	1,234,000
	2006	
Issuer	Investment Type	Reported Amount
Federal Home Loan Mortgage Corporation	U.S. Agency	\$ 2,947,813
Morgan Stanley	Repurchase Agreement	1,479,000

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NOTES TO COMBINED FINANCIAL STATEMENTS  
JUNE 30, 2007 AND 2006

Draft

Note 4 – Capital Assets

Capital asset additions, retirements, and balances for the years ended June 30, 2007 and 2006, were as follows:

	Balance July 1, 2006	Additions	Retirements	Balance June 30, 2007
Capital assets				
Land	\$ 1,557,283	\$ -	\$ -	\$ 1,557,283
Building and improvements	5,773,293	5,833	-	5,779,126
Furniture and equipment	988,838	2,323	-	991,161
Computer hardware	1,461,923	117,840	-	1,579,763
Computer software	1,124,767	285,650	-	1,410,417
Construction in process	-	161,799	-	161,799
Total capital assets	<u>10,906,104</u>	<u>573,445</u>	<u>-</u>	<u>11,479,549</u>
Less accumulated depreciation for				
Building and improvements	(852,827)	(184,014)	-	(1,036,841)
Furniture and equipment	(814,654)	(90,085)	-	(904,739)
Computer hardware	(1,264,661)	(89,408)	-	(1,354,069)
Computer software	(989,641)	(125,013)	-	(1,114,654)
Total accumulated depreciation	<u>(3,921,783)</u>	<u>(488,520)</u>	<u>-</u>	<u>(4,410,303)</u>
Net capital assets	<u>\$ 6,984,321</u>	<u>\$ 84,925</u>	<u>\$ -</u>	<u>\$ 7,069,246</u>
	Balance July 1, 2005	Additions	Retirements	Balance June 30, 2006
Capital assets				
Land	\$ 1,557,283	\$ -	\$ -	\$ 1,557,283
Building and improvements	5,773,293	-	-	5,773,293
Furniture and equipment	1,139,621	49,526	(200,309)	988,838
Computer hardware	1,776,391	42,864	(357,332)	1,461,923
Computer software	1,107,694	17,073	-	1,124,767
Construction in process	56,087	-	(56,087)	-
Total capital assets	<u>11,410,369</u>	<u>109,463</u>	<u>(613,728)</u>	<u>10,906,104</u>
Less accumulated depreciation for				
Building and improvements	(660,103)	(192,724)	-	(852,827)
Furniture and equipment	(826,441)	(132,819)	144,606	(814,654)
Computer hardware	(1,493,641)	(128,242)	357,222	(1,264,661)
Computer software	(898,228)	(91,413)	-	(989,641)
Total accumulated depreciation	<u>(3,878,413)</u>	<u>(545,198)</u>	<u>501,828</u>	<u>(3,921,783)</u>
Net capital assets	<u>\$ 7,531,956</u>	<u>\$ (435,735)</u>	<u>\$ (111,900)</u>	<u>\$ 6,984,321</u>

Depreciation expense for 2007 and 2006 was \$488,520 and \$545,198, respectively.

**Note 5 – Claims Payable**

The Alliance estimated claims payable based on historical claims payment and other relevant information. For the years ended June 30, 2007 and 2006, the following is a reconciliation of the claims payable liability:

	<u>2007</u>	<u>2006</u>
Balance, July 1	\$ 9,813,032	\$ 13,662,354
Incurred - current	68,500,460	57,873,633
Paid		
Current	(56,548,930)	(53,442,209)
Prior	(7,742,508)	(8,413,030)
Adjustment	<u>(133,091)</u>	<u>132,284</u>
Balance, June 30	<u>\$ 13,888,963</u>	<u>\$ 9,813,032</u>

**Note 6 – Operating Leases**

The Alliance leases parking space and equipment under noncancelable operating leases. Rent expense under these leases was \$22,624 and \$22,184 for the years ended June 30, 2007 and 2006, respectively. The total future minimum lease commitments under noncancelable leases at June 30, 2007, were as follows:

<u>Years Ending June 30,</u>	
2008	\$ 87,128
2009	87,813
2010	32,119
2011	31,463
2012	-
Thereafter	-
	<u>\$ 238,523</u>

The Alliance leased a portion of its owned building to a third party under a noncancelable operating lease that expired in May 2006. Total rental income under the lease for the years ended June 30, 2007 and 2006, was \$0 and \$395,672 and is included in rental income in the statements of revenues, expenses, and changes in net assets.

On July 30, 2007 the Alliance entered into a sublease for satellite office space in Oakland. The site is expected to provide better access for members than the current location. The lease is effective August 1, 2007 and monthly rent expense in the amount of \$4,700 is included in the future minimum lease commitments schedule.

#### Note 7 – Medical Reinsurance (Stop-Loss Insurance)

The Alliance has entered into certain reinsurance (stop-loss) agreements with third parties in order to limit its losses on individual claims. Under the terms of these agreements, the third parties will reimburse the Alliance certain proportions of the cost of each member's hospital, professional, and out-of-area services, excluding those that are capitated, in excess of specified deductibles ranging from \$7,500 to \$100,000 per contract, up to a maximum of \$1,000,000 per member per contract year. Reinsurance premiums are recorded as health care operating expenses and recoveries are recorded as a reduction of these expenses. Stop-loss recoveries exceeded premiums by \$113,831 in 2007. Stop-loss premiums exceeded recoveries by \$356,976 in 2006.

#### Note 8 – Employee Benefit Plans

##### Pension Plan

The Alliance has a defined contribution employee benefit plan (the "Plan"). The Plan is named the Alameda Alliance for Health Money Purchase Pension Plan and is administered by the Alliance. The Board of Governors has the authority to establish and amend benefit provisions and contribution requirements. All employees who have met certain service requirements are eligible to participate. During the years ended June 30, 2007 and 2006, the Alliance contributed 5% of each eligible employee's gross compensation to certain investment vehicles chosen by the employee. Contributions are subject to limitations on annual compensation and annual contributions. The annual compensation limit was \$225,000 and \$220,000 in 2007 and 2006, respectively. The maximum annual contribution limit was \$15,500 and \$15,000 in 2007 and 2006, respectively. Contributions to the Plan are made by the Alliance at the discretion of the Board of Governors. Employees do not contribute to this Plan. Employees become vested with respect to the Alliance's contributions ratably over five years. Total contributions by the Alliance were \$363,000 and \$382,176 for the years ended June 30, 2007 and 2006, respectively.

##### CalPERS Plan

**Plan Description** – Effective January 1, 1999, the Plan joined the California Public Employees Retirement System (PERS), an agent multiple-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by state statute. Copies of the PERS annual financial report may be obtained from their Executive Office: 400 P Street, Sacramento, CA 95814.

**Funding Policy** – Participating employees are required to contribute 7.0% of their monthly salaries to PERS. The Plan deducts the contributions from employees' wages and remits to PERS on their behalf and for their account. The Plan is required to contribute an actuarially determined rate. The employer contribution rates were 7.15% and 7.37% of annual covered payroll for the years ended June 30, 2007 and 2006, respectively. The contribution requirements of the plan members and the Plan are established and may be amended by PERS. With the election to participate in PERS, participation in Social Security is discontinued, and contributions to PERS are in lieu of contributions to Social Security.

**Note 8 – Employee Benefit Plans (continued)**

**Annual Pension Cost** – The Plan’s annual pension cost for PERS was equal to the Plan’s required and actual contributions which were determined as part of the actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions included (a) 7.75 % investment rate of return (net of administrative expenses); (b) projected salary increases of 3.25% varying by duration of services, and (c) 2.0% cost-of-living adjustment. Both (a) and (b) included an inflation component of 3.0%. These assumptions are expected to change in the subsequent valuation.

Historical trend information:

Fiscal Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
June 30, 2005	\$ 461,690	100%	\$ -
June 30, 2006	\$ 499,157	100%	\$ -
June 30, 2007	\$ 515,350	100%	\$ -

**Deferred Compensation Plan**

The Plan offers its employees a deferred compensation plan with ING created in accordance with Internal Revenue Code Section 457. The deferred compensation plan is available to all employees and permits them to defer a portion of their salary. No employer contribution to the plan is required. Deferred compensation is not available to employees until termination, retirement, death, or an unforeseeable emergency.

**Note 9 – Professional Liability Insurance**

The Alliance maintains insurance coverage for professional liability and errors and omissions insurance. The policy is an occurrence-based policy and designed specifically for health maintenance organizations to provide comprehensive professional liability insurance and errors and omissions insurance for the Alliance employees. There have been no reductions in coverage or any claims that have exceeded coverage in any of the past three years.

**Note 10 – Commitments and Contingencies**

In the ordinary course of business, the Alliance is a party to claims and legal actions by enrollees, providers, and others. After consulting with legal counsel, the Alliance’s management is of the opinion that any liability that may ultimately be incurred as a result of claims or legal actions will not have a material effect on the combined financial position or results of operations of the Alliance.