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CERTIFIED PUBLIC ACCOUNTANTS | BUSINESS & FINANCIAL ADVISORS

Rehoboth McKinley Christian Health Care Services, Inc.

Consolidated Financial Statements, Supplementary Information and
Independent Auditors' Reports

August 31, 2008 and 2007

Rehoboth McKinley Christian Health Care Services, Inc.

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Rehoboth McKinley Christian Health Care Services, Inc.

Board of Trustees and Principal Employee
August 31, 2008

Independent Auditors' Report

Board of Trustees and Management of
Rehoboth McKinley Christian Health Care Services, Inc.
and
Mr. Hector H. Balderas, New Mexico State Auditor

We have audited the accompanying consolidated statements of financial position of Rehoboth McKinley Christian Health Care Services, Inc. (the "Hospital"), a not-for-profit corporation, and Rehoboth McKinley Christian Health Care Services Foundation, Inc., (the "Foundation") a wholly-owned not-for-profit subsidiary (collectively the "Organization"), as of August 31, 2008 and 2007, and the related consolidated statements of activities and cash flows for the years then ended, as listed in the table of contents. These consolidated financial statements are the responsibility of management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards established by the Auditing Standards Board (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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Organization as of August 31, 2008 and 2007, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 9, 2009, on our consideration of the Organization's internal control over financial reporting and 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.

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Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The accompanying information identified in the table of contents as Supplementary Information Required by New Mexico State Auditor is presented for purposes of additional analysis, and to meet the requirements of the New Mexico Office of the State Auditor, 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.

REDW LLC

January 9, 2009

Consolidated Financial Statements

Rehoboth McKinley Christian
Health Care Services, Inc.
Consolidated Statements of Financial Position
August 31,

	2008	2007
Assets		
Current assets		
Cash and cash equivalents	**$ 2,776,293**	$ 1,660,958
Patient accounts receivable, net of allowance for doubtful accounts of $10,900,000 in 2008 and $8,100,000 in 2007	**10,264,276**	7,460,591
Sole Community Provider and other receivables	**3,522,819**	832,187
Inventories	**875,307**	1,001,044
Prepaid expenses and deposits	**868,604**	787,987
Total current assets	**18,307,299**	11,742,767
Property, plant and equipment, net	**20,087,367**	21,019,804
Bond funds and other investments	**2,881,148**	4,479,279
Other assets, net	**1,364,435**	1,307,981
Total assets	**$ 42,640,249**	$ 38,549,831
Liabilities and Net Assets		
Current liabilities		
Accounts payable	**$ 4,838,825**	$ 3,063,784
Accrued salaries and related liabilities	**5,634,015**	4,672,190
Estimated third party payor settlements	**8,414,709**	6,852,197
Current portion of long-term debt	**1,246,289**	895,433
Total current liabilities	**20,133,838**	15,483,604
Long-term debt, less current portion	**8,089,783**	9,966,710
Total liabilities	**28,223,621**	25,450,314
Net assets		
Unrestricted	**13,809,236**	12,737,419
Temporarily restricted	**501,742**	262,988
Permanently restricted	**105,650**	99,110
Total net assets	**14,416,628**	13,099,517
Total liabilities and net assets	**$ 42,640,249**	$ 38,549,831

The accompanying notes are an integral part of these consolidated financial statements.

Rehoboth McKinley Christian
Health Care Services, Inc.
Consolidated Statements of Activities
For the Years Ended August 31,

	2008				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	2007 Total
Operating Revenue					
Net patient service revenue	$ 67,713,724	$ -	$ -	$ 67,713,724	$ 66,280,460
Other	9,254,275	248,385	6,540	9,509,200	6,246,709
Net assets released from restrictions	9,631	(9,631)	-	-	-
Total operating revenue	76,977,630	238,754	6,540	77,222,924	72,527,169
Operating Expenses					
Salaries and payroll taxes	37,454,862	-	-	37,454,862	35,797,333
Supplies and other	8,837,244	-	-	8,837,244	7,556,235
Provision for bad debts	7,402,698	-	-	7,402,698	6,809,216
Contract labor	3,369,910	-	-	3,369,910	1,409,989
Purchased services	3,293,280	-	-	3,293,280	3,780,299
Depreciation and amortization	2,975,213	-	-	2,975,213	2,890,929
Pharmaceuticals	2,524,252	-	-	2,524,252	3,125,010
Employee benefits	2,469,172	-	-	2,469,172	2,281,779
Professional fees	2,158,682	-	-	2,158,682	1,402,636
Utilities	1,517,912	-	-	1,517,912	1,401,995
Insurance	1,400,968	-	-	1,400,968	1,234,110
Repairs and maintenance	1,304,259	-	-	1,304,259	1,125,258
Rentals and leases	499,401	-	-	499,401	388,525
Advertising	272,435	-	-	272,435	248,349
Property taxes	105,186	-	-	105,186	65,348
Total operating expenses	75,585,474	-	-	75,585,474	69,517,011
Operating income	1,392,156	238,754	6,540	1,637,450	3,010,158
Nonoperating income (expense)					
Investment income	249,537	-	-	249,537	298,441
Other nonoperating income (expense)	121,397	-	-	121,397	(32,405)
Interest expense	(691,273)	-	-	(691,273)	(607,985)
Total nonoperating expense, net	(320,339)	-	-	(320,339)	(341,949)
Change in net assets	1,071,817	238,754	6,540	1,317,111	2,668,209
Net assets, beginning of year	12,737,419	262,988	99,110	13,099,517	10,431,308
Net assets, end of year	$ 13,809,236	$ 501,742	$ 105,650	$ 14,416,628	$ 13,099,517

The accompanying notes are an integral part of these consolidated financial statements.

Rehoboth McKinley Christian
Health Care Services, Inc.
Consolidated Statements of Cash Flows
For the Years Ended August 31,

	2008	2007
Cash flows from operating activities		
Cash received from patients and third-party payors	**$ 59,069,853**	$ 59,410,851
Other receipts from operations	**6,818,568**	6,646,901
Cash paid to employees and suppliers	**(62,232,494)**	(63,795,091)
Interest paid	**(691,273)**	(607,985)
Net cash provided by operating activities	**2,964,654**	1,654,676
Cash flows from investing activities		
Purchase of property and equipment	**(1,576,053)**	(721,364)
Proceeds from sale of property and equipment	**410,261**	-
Cash from (used for) bond funds and other investments	**1,529,210**	(2,976,285)
Net cash provided by (used for) investing activities	**363,418**	(3,697,649)
Cash flows from financing activities		
Proceeds from long-term debt	**-**	10,200,000
Cash paid for bond issue costs	**-**	(769,750)
Payment of long-term debt	**(2,212,737)**	(6,690,919)
Net cash provided by (used for) financing activities	**(2,212,737)**	2,739,331
Net increase in cash and cash equivalents	**1,115,335**	696,358
Cash and cash equivalents, beginning of year	**1,660,958**	1,202,445
Cash and cash equivalents, end of year	**$ 2,776,293**	$ 1,898,803
Reconciliation of change in net assets to net cash provided by operating activities		
Change in net assets	**$ 1,317,111**	$ 2,668,209
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation and amortization	**2,975,213**	2,890,929
Provision for bad debts	**7,402,698**	6,809,216
(Gain)/loss on sale of property and equipment	**(121,397)**	32,405
Net changes in operating assets and liabilities		
Patient accounts receivable	**(10,206,383)**	(6,843,001)
Other receivables	**(2,690,632)**	101,751
Inventories	**125,737**	(184,194)
Prepaid expenses and deposits	**(80,617)**	(6,114)
Other assets	**(56,454)**	42,398
Accounts payable	**1,775,041**	(3,285,188)
Accrued salaries and related liabilities	**961,825**	(545,127)
Estimated third-party payor settlements	**1,562,512**	(26,608)
Net cash provided by operating activities	**$ 2,964,654**	$ 1,654,676
Supplemental schedule of noncash investing and financing activities		
Equipment acquired through capital lease	**$ 686,666**	$ 1,119,118

The accompanying notes are an integral part of these consolidated financial statements.

1) Organization and Summary of Significant Accounting Policies

Organization

Rehoboth McKinley Christian Health Care Services, Inc. (the "Hospital") is a not-for-profit acute care hospital located in Gallup, New Mexico. The Hospital provides impatient, outpatient, and emergency care services to the residents of Gallup, McKinley County and the surrounding area.

These financial statements include the Hospital as well as Rehoboth McKinley Christian Health Care Services Foundation (RMCHCS Foundation or the "Foundation") (formerly "Western Health Foundation"), a wholly-owned not-for-profit subsidiary (see Note 12). The Hospital is the sole stated beneficiary of the Foundation. The Foundation is authorized by the Hospital to solicit contributions on its behalf. Intercompany balances and transactions have been eliminated in consolidation.

This summary of significant accounting policies of the Hospital is presented to assist in the understanding of the Hospital's financial statements. The financial statements and notes are the representations of the Hospital's management who is responsible for their integrity and objectivity. The financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) as applied to not-for-profit entities. The more significant of the Hospital's accounting policies are described below.

Basis of Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations.* Under SFAS No. 117, the Hospital is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Use of Estimates

Financial statement preparation in conformity with U.S. generally accepted accounting principles 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 financial statement date and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates contained in the Hospital's financial statements include the allowance for doubtful accounts, contractual allowance, estimated third party payor settlements and depreciation and amortization.

1) Organization and Summary of Significant Accounting Policies — continued

Fair Value of Financial Instruments
For financial statement purposes, receivables, bond funds and other investments, accounts payable, and debt are considered financial instruments. The Hospital estimates that the fair value of all financial instruments at August 31, 2008 and 2007, does not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying statements of financial position

Cash and Cash Equivalents
For purposes of reporting cash flows, the Hospital includes all highly liquid debt instruments with original maturities of three months or less to be cash equivalents, which at times may exceed the federally insured limits. The Hospital has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on its cash balances.

Accounts Receivable Allowances
Contractual allowances represent the amounts which reduce patient accounts receivable to amounts that are considered to be due from third-party payors based on existing contracts the Hospital has with these payors. The contractual allowance percentages are updated monthly by payor class and line of business and are based upon the accounts within that payor category that been adjusted over the previous six months if:

- The sum of the payments and adjustments recorded to the account over the previous six months were greater than 90% of charges; or
- The year-end accounts receivable balance equaled zero and the sum of payments made over the previous six months were greater than 90% of total payments posted to the patient's account.

Contractual allowances are deducted from gross patient accounts receivable on the statements of financial position.

The allowance for doubtful patient accounts receivable is that amount which, in management's judgment, is considered adequate to reduce patient accounts receivable to an amount that is considered to be ultimately collectible. The Hospital calculates its allowance for doubtful accounts based on percentages of accounts receivable aging categories that consider historical write-offs by major payor categories over the past several years.

Management believes that the allowances for doubtful accounts and contractual allowances are adequate. Because of the uncertainty regarding the ultimate collectibility of patient accounts receivable, there is a possibility that recorded estimates of the allowance for doubtful accounts and contractual allowances will change by a material amount in the near term.

1) Organization and Summary of Significant Accounting Policies — continued

Accounts Receivable Allowances — continued
On a monthly basis, the Hospital evaluates patient accounts receivable balances older than six months to determine collectibility. Accounts are considered uncollectible when there has been no recent payment activity and no other indication that payment will be received. Those balances that are considered uncollectible are written off upon approval from the Director of Patient Financial Services, Chief Financial Officer and Chief Executive Officer depending on the balance of the account. In April 2008, the Hospital outsourced the collections of third-party accounts receivable (except for governmental payors) over 151 days old to a third-party collections company. Because of this company's success in collecting on these accounts, the Hospital reduced the calculated allowance for doubtful accounts by $1.7 million at August 31, 2008 based on the amounts expected to be collected on these accounts over the near term.

During 2008, the Hospital made various technical changes to the contractual model used to calculate these estimates. One of the changes included combining balances by account so that each account was only counted once in the model whereas these accounts were previously combined by third-party payor and bill status. This change reduced the amount of credits included in the model (for example, third-party overpayments). The other changes included updating contractual reserve percentages (which is described above) and aging the balances in the previously unbilled categories. In the aggregate, these changes reduced contractual allowances by approximately $1.1 million and reduced the allowance for doubtful accounts by approximately $88,000.

Inventories
Inventories are stated at lower of cost, (the first-in, first-out method) or market and consist primarily of medical supplies and medications.

Property, Plant, and Equipment
Property, plant and equipment are recorded at cost. Property and equipment donated for Hospital operations are recorded as additions to temporarily restricted net assets when the assets are placed in service. Assets held under capital leases are recorded at the lower of the net present value of the minimum lease payments or the fair value of the leased asset at the inception of the lease. Additions, improvements and other capital outlays that significantly extend the useful life of an asset and are greater than $1,000 are capitalized. Costs incurred for repair and maintenance are expensed as incurred.

In September 1995, the Hospital renewed its facility lease agreement with McKinley County, New Mexico for 25 additional years. The lease was extended in 2006 to a total of 33 years. The annual rent paid to the County for the use of the Hospital facility is $1 per year. Since the original lease agreement dates back to the 1970s and the original fair value of the building would be almost fully amortized at August 31, 2008 and 2007, the

1) Organization and Summary of Significant Accounting Policies — continued

Property, Plant, and Equipment — continued
net book value of the contribution receivable is considered insignificant to the financial statements. The fair market value of this lease and the offsetting donation income have not been recorded since the fair rental value of the hospital facility is not determinable, and management does not believe such amounts, if any, would be material to the financial statements.

Depreciation is computed using primarily the straight-line method over the assets' estimated useful lives ranging from 3 to 40 years. Leasehold improvements are amortized over their useful lives not to exceed the term of the related lease.

Bond Funds and Other Investments
Bond funds and other investments primarily include assets held by trustees under indenture agreements, and certain donor restricted assets.

The Hospital values its investments in equity securities with readily determinable fair values and all investments in debt securities at fair value in the accompanying statements of financial position. Unrealized gains and losses are included in investment income in the accompanying statements of activities.

Net Assets and Changes Therein
Net assets and income, expenses, gains and losses are classified based on the existence or absence or donor-imposed restrictions. Accordingly, the net assets of the Hospital and changes therein are classified and reported as follows:

Unrestricted—Unrestricted net assets represent those resources that are not restricted by donors, or for which donor-imposed restrictions have expired.

Temporarily Restricted—Temporarily restricted net assets reflect donor-imposed restrictions that require the Hospital to use or expend the related assets as specified. The restrictions are satisfied either by the passage of time or by the satisfaction of donor specified use.

The Hospital records contributions as temporarily restricted if they are received with donor stipulations that limit their use through either purpose or time restrictions. When donor restrictions expire, that is, when a time restriction ends or a purpose restriction is fulfilled, temporarily restricted net assets are reclassified to unrestricted net assets. Temporarily restricted contributions received and expended in the same accounting period are recorded in the unrestricted net asset category. Temporarily restricted revenues and reclassifications were not significant to the Hospital for the year ended August 31, 2007, and are therefore not presented separately in the accompanying 2007 statement of activities.

1) Organization and Summary of Significant Accounting Policies — continued

Net Assets and Changes Therein
Permanently Restricted—Permanently restricted net assets reflect donor-imposed restrictions which stipulate that the related resources be maintained in perpetuity, but which permit the Hospital to expend part or all of the income and capital appreciation derived from the donated assets for either specified or unspecified purposes. Permanently restricted revenues and reclassifications were not significant to the Hospital for the years ended August 31, 2008 and 2007, and are therefore not presented separately in the accompanying statements of activities.

Debt Issuance Costs
Deferred debt issuance costs are included with other long-term assets on the accompanying statements of financial position, and are amortized using the straight-line method over the term of the related debt. Amortization of deferred debt issuance costs is included with depreciation and amortization expense in the accompanying statements of activities. Total debt issuance costs were $789,449. Accumulated amortization of debt issuance costs totaled $66,975 and $19,699 at August 31, 2008 and 2007, respectively.

Charity Care
The Hospital provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, such amounts are not reported as revenue. The Hospital maintains records to identify and monitor the level of charity care provided. Those records include the amount of charges foregone for services and supplies furnished under the Hospital' charity care policy and aggregated approximately $3,360,749 and $1,801,063 in 2008 and 2007, respectively.

Tax Status
The Hospital and the Foundation are exempt from state and federal income taxes on related income under Section 501(a) of the Internal Revenue Code as organizations described in Section 501(c)(3). The Hospital and the Foundation are classified as other than private foundations.

Advertising Costs
Advertising costs are expensed as incurred. Advertising expense totaled $272,400 and $248,300 for the years ended August 31, 2008 and 2007, respectively.

Reclassifications
Certain reclassifications have been made to the 2007 financial information to conform to the 2008 financial statement presentation. Such reclassifications had no effect on the 2007 change in net assets.

2) Net Patient Service Revenue

Agreements with third-party payors provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on the estimated basis in the period the related services are rendered and adjusted in future periods as more information is available to improve estimates or final settlements are determined.

A summary of payment arrangements with major third-party payors follows:

Medicare—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. Inpatient nonacute services, behavioral inpatient services, certain outpatient services, and defined capital and medical education costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual costs reports by the Hospital and audits thereof by the Medicare fiscal intermediary.

Medicaid—The State of New Mexico (the “State”) administers its Medicaid program through contracts with Managed Care Organizations (MCOs). Medicaid beneficiaries are required to enroll with one of the MCOs. The State pays each MCO a per member, per month rate based on their current enrollment. These amounts are allocated by each MCO to separate pools for the hospital, physicians, and ancillary providers. As a result, the MCOs assume the financial risk of providing health care to its members. This arrangement is commonly referred to as “SALUD!.”

Through the Hospital’s contracts with MCOs, inpatient acute care services and outpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge and discounted fee schedules. These rates vary accordingly to a patient classification system that is based on clinical, diagnostic, and other factors. Behavioral and home health services rendered to Medicaid program beneficiaries are paid using a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicaid fiscal intermediary.

2) Net Patient Service Revenue — continued

Medicare and Medicaid cost report liabilities are as follows:

	August 31, 2008 Amount	August 31, 2008 Status	August 31, 2007 Amount
Medicare			
2006	$ -	Closed	$ 198,509
2007	-	Tentative Settlement	203,214
2008	194,026	Not filed	-
	194,026		401,723
Medicaid			
2002	265,947	Closed	484,198
2003	620,917	Closed	1,023,613
2004	1,391,986	Unaudited	1,391,986
2005	971,198	Unaudited	971,198
2006	1,187,519	Unaudited	1,187,519
2007	1,891,558	Unaudited	1,391,960
2008	1,891,558	Not filed	-
	8,220,683		6,450,474
Estimated third party payor settlements	$ 8,414,709		$ 6,852,197

Management believes that these estimates are adequate. Laws and regulations governing the Medicare and Medicaid programs are extremely 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. Estimates are continually monitored and reviewed, and as settlements are made or more information is available to improve estimates, differences are reflected in current operations.

Settlements of prior-year cost reports and changes in estimates resulted in increases to net patient service revenue of approximately $233,000 and $918,000 in the years ended August 31, 2008 and 2007, respectively.

Other Third-Party Payors—The Hospital has also entered into payment agreements with certain commercial insurance carriers. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established changes and prospectively determined daily rates.

2) Net Patient Service Revenue — continued

The following summary details the components of net patient service revenue for the years ended August 31:

	2008	2007
Gross charges		
Inpatient	**$ 46,837,577**	$ 44,778,585
Outpatient	**108,082,581**	105,020,989
	154,920,158	149,799,574
Third party contractual allowances	**(83,845,685)**	(81,718,051)
Charity care	**(3,360,749)**	(1,801,063)
Net patient service revenue	**$ 67,713,724**	$ 66,280,460

3) Bond Funds and Other Investments

The composition of bond funds and other investments at August 31, is as follows:

	2008	2007
Held by trustee under indenture agreement related to Series 2007 Revenue Bonds		
Cash and cash equivalents	**$ 2,318**	$ 1,707
Private debt obligations	**645,300**	645,300
	647,618	647,007
Series 2007 Revenue Bonds project fund		
Money market funds	**1,662,478**	2,789,363
Working capital loan fund held in escrow		
Money market funds	**286,366**	691,938
Irrevocable trust - 457(b) plan		
Money market funds	**10,662**	9,510
Equity securities	**78,620**	121,190
Fixed income securities	**56,640**	72,036
	145,922	202,736

3) Bond Funds and Other Investments — continued

	2008	2007
RMCHCS Foundation		
Certificate of deposit	**103,128**	98,712
Unexpended mill levy funds		
Cash	**-**	15,388
Other	**35,636**	34,135
	$ 2,881,148	$ 4,479,279

Investment income from cash and cash equivalents, short-term investments, bond funds and other investments consists of the following for the years ended August 31:

	2008	2007
Dividends and interest	**$ 248,026**	$ 295,249
Net unrealized gains and losses	**1,511**	3,192
Total	**$ 249,537**	$ 298,441

4) Property, Plant and Equipment

A summary of property, plant and equipment at August 31, follows:

	2008	2007
Equipment	**$ 30,043,217**	$ 28,808,623
Buildings and improvements	**29,298,836**	29,346,771
Land improvements	**1,458,701**	1,458,701
	60,800,754	59,614,095
Accumulated depreciation and amortization	**(41,827,620)**	(39,828,298)
	18,973,134	19,785,797
Land	**734,969**	898,921
Construction in progress	**379,264**	335,086
	$ 20,087,367	$ 21,019,804

5) Long-Term Debt

Long-term debt consists of the following at August 31:

	2008	2007
Series 2007A New Mexico Hospital Equipment Loan Council Hospital Facility Refunding and Improvement Bonds; issued under an Indenture of Trust; interest on the basis of a 360-day year at 5.00% until 2017 and 5.25% until maturity; principal payments range from $100,000 to $610,000; principal and interest payable annually on August 15 from 2009 through 2026; collateralized by the County Lease between the Hospital and the County of McKinley and buildings owned by the Hospital, secured by pledged revenues	**$ 7,245,000**	$ 7,245,000
Series 2007A-T New Mexico Hospital Equipment Loan Council Hospital Facility Refunding and Improvement Bonds; issued under an Indenture of Trust; interest on the basis of a 360-day year at 6.40%; principal payments range from $75,000 to $160,000; principal and interest payable annually on August 15 through 2009; collateralized by the County Lease between the Hospital and the County of McKinley and buildings owned by the Hospital	**150,000**	270,000
Working capital loan with Wells Fargo Bank; interest at 6.15% due monthly; principal payments due in the amount by which the outstanding principal balance exceeds $1,850,000 at January 15, 2008 and $1,100,000 at January 15, 2009; all outstanding principal and interest is due November 15, 2009; loan is collateralized by and payments are made from Mill Levy funds	**180,165**	1,431,579
Present value of capital leases that expire at various dates through February 2012; interest rates ranging from 3.6% to 20.5% secured by equipment	**1,760,907**	1,915,564
Total long-term debt	**9,336,072**	10,862,143
Less current portion	**(1,246,289)**	(895,433)
Long-term debt, less current portion	**$ 8,089,783**	$ 9,966,710

5) Long-Term Debt — continued

In March 2007, the Hospital issued the Series 2007A bonds to refund the outstanding Series 1996 and Series 2000 bonds, to finance the costs of the acquisition of certain equipment, to fund a project fund (see Note 3), and to pay certain costs of issuance for the Series 2007A bonds.

The Refunding and Improvement Bond Master Trust Indenture (the "Indenture") requires the Hospital to make monthly deposits with a trustee for payment on the bonds. Such deposits (see "Series 2008 Revenue Bonds" at Note 3) are included with bond funds and other investments in the accompanying statements of financial position. The bond agreement also places certain limits on the incurrence of additional debt and requires that the Hospital satisfy certain measures of financial performance as long as the bonds are outstanding. At August 31, 2008, the Hospital was in compliance with all applicable requirements and covenants of the bond agreement.

The cost of equipment under capital leases is included in property, plant and equipment in the statements of financial position and was $4,876,278 and $3,995,941 at August 31, 2008 and 2007, respectively. Accumulated amortization on the leased equipment at August 31, 2008 and 2007 was $2,431,531 and $1,597,294, respectively. Amortization of assets under capital leases is included in depreciation and amortization expense.

Required principal payments on long-term debt are as follows:

	Bonds and Loan Payable	Capital Leases
Year ending August 31,		
2009	$ 430,165	$ 924,508
2010	275,000	693,089
2011	290,000	246,612
2012	300,000	106,419
2013	320,000	-
Thereafter	5,960,000	-
	$ 7,575,165	1,970,628
Less amounts representing interest		(209,721)
		$ 1,760,907

6) Employee Benefits

The Hospital has established a Section 403(b) retirement plan (the "plan"). There is no minimum period of service or age in order to be eligible to participate; however, employees must make a minimum contribution to be eligible for a discretionary 100% employer match contribution of up to 3% of the employee's salary. Additionally, the Hospital will match 50% of additional contributions up to 5% of the employee's salary. At August 31, 2008, a total of $1,022,000 was accrued for employer contributions, of which $602,000 was applicable to calendar year 2007 and $420,000 to the first eight months of calendar year 2008. At August 31, 2007, a total of $773,000 was accrued for employer contributions, of which $430,000 was applicable to calendar year 2006 and $343,000 to the first eight months of calendar year 2007.

Effective January 1, 2003, the Hospital adopted a nonqualified deferred compensation plan under Section 457(b) of the Internal Revenue Code. The plan enables certain key employees to enhance their retirement security by deferring compensation in addition to 403(b) deferrals. An irrevocable trust was established to satisfy the financial obligations to provide benefits to participants under the plan. Participants do not have a secured interest in the assets held in the trust; as such assets remain the property of the Hospital and are subject to creditor claims. The funded amount of the trust for the years ended August 31, 2008 and 2007 was $145,922 and $202,736, respectively, and is included in bond funds and other investments in the statements of financial position. The related liabilities of $145,922 and $202,736 are included in accrued salaries and related liabilities in the statements of financial position.

7) Employee Health Insurance Benefit Program

The Hospital has retained liability for certain employee health claims up to $100,000 per claim and $1,500,000 in the aggregate and has purchased insurance for claims in excess of these amounts. Management believes that adequate reserves have been established as of August 31, 2008 and 2007, to cover claims which have been incurred but not reported. Such reserves are included in accrued salaries and related liabilities in the accompanying statements of financial position.

8) Other Operating Revenue

Other operating revenue includes the following:

<u>Ad Valorem Tax Levy</u>
A New Mexico state law adopted in 1980 and amended in 1981 allows for counties to provide tax support to qualifying hospitals. A property tax levy for two mills was approved by the county voters in fiscal year 2004. Revenue from the levy was $1,554,719

8) Other Operating Revenue — continued

Ad Valorem Tax Levy — continued
and $1,156,000 in the years ended August 31, 2008 and 2007, respectively. The current mill levy expires July 2012.

Sole Community Provider
The Hospital participates in a sole community provider indigent care program administered by the State of New Mexico. Revenue from this program in 2008 and 2007 totaled $6.3 million and $3.6 million, respectively. Approximately $2.7 million and $658,000 as of August 31, 2008 and 2007, respectively, is included in Sole Community Provider and other receivables in the consolidated statements of financial position.

Other
Other operating revenue also includes cafeteria, gift shop, donation and grant revenues.

9) Concentrations of Credit Risk

The Hospital provides credit, in the normal course of business, to patients located primarily in Gallup, McKinley County and the surrounding area and their respective insurance companies. The Hospital does not require collateral with the extension of credit. The Hospital maintains an allowance for doubtful accounts based on management's assessment of collectibility, current economic conditions, and prior experience. Because of the uncertainty regarding the ultimate collectibility of patient accounts receivable, there is at least a reasonable possibility that recorded estimates of the allowance for doubtful accounts and contractual allowances will change by a material amount in the near term.

The mix of gross accounts receivable from patients and third-party payors was as follows at August 31:

	2008	2007
Medicare	**34%**	34%
Medicaid	**20**	19
Other third-party payors	**25**	29
Patients	**21**	18
	100%	100%

10) Commitments and Contingencies

Healthcare Regulatory Environment—The healthcare industry is subject to laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs, the imposition of significant fines and penalties and significant repayments for patient services previously billed.

Management believes that the Hospital is in compliance with applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well a regulatory actions unknown or unasserted at this time.

The Health Insurance Portability and Accountability Act (HIPAA) was enacted August 21, 1996, to assure health insurance portability, guarantee security and privacy of health information, enforce standards for health information and establish administrative simplification provisions. Management believes that the Hospital is in the compliance with all applicable provisions of HIPAA.

Litigation—The Hospital is involved in litigation arising in the ordinary course of business. Claims alleging malpractice have been asserted against the Hospital and are currently in various stages of litigation. In management's opinion, upon consultation with legal counsel, malpractice coverage is adequate to cover adverse judgments, if any, made against the Hospital.

Malpractice Insurance—Effective March 1, 2003, pursuant to the Federal Risk Retention Act and under the captive insurance company provisions of Vermont law, the Hospital is insured under and is a founding subscriber in the VHA Mountain States Reciprocal Risk Retention Group for the purpose of providing insurance for malpractice and general liability coverage. The policy is on a claims made basis with a per occurrence deductible of $25,000 and maximum aggregate coverage of $5,000,000 for the Hospital and $10,000,000 aggregate for all sixteen member hospitals. The premiums are to accrue based on the ultimate experience of the group of health care entities. At August 31, 2008, the Hospital cannot estimate the additional premiums, if any, which may accrue as a result of the Group's experience to date.

Selected employed physicians are covered under the same risk retention group on a claims made basis with $1,000,000/$3,000,000. The Hospital maintains malpractice insurance for the remaining employed physicians through a commercial carrier.

10) Commitments and Contingencies — continued

Workers' Compensation Insurance—Pursuant to the New Mexico Self Insurance Act, the Hospital is insured under the New Mexico Hospital Workers Compensation Group for the purpose of providing insurance for workers' compensation coverage. The policy is a retrospectively rated policy whose premiums are to accrue based on the ultimate cost of the experience of a group of health care entities. At August 31, 2008, the Hospital cannot estimate the additional premiums or refunds, if any, which may accrue as a result of the Group's experience to date.

11) Functional Expense Classification

In recording the activities of the Hospital, expenses are specifically tracked or allocated on the basis of periodic time and expense studies, and recorded in the following functional categories:

	2008	2007
Health care services	**$ 47,938,955**	$ 45,103,487
Management and general	**27,938,964**	24,840,458
Fundraising	**277,431**	213,456
	$ 76,155,350	$ 70,157,401

12) RMCHCS Foundation Summarized Financial Statements

Summarized financial statements for RMCHCS Foundation as of and for the years ended August 31, are as follows:

	2008	2007
Assets		
Current assets	**$ 416,877**	$ 288,461
Investments	**103,128**	98,712
Other assets	**3,179**	58,603
Total assets	**$ 523,184**	$ 445,776

12) RMCHCS Foundation Summarized Financial Statements — continued

	2008	2007
Liabilities and Net Assets		
Current liabilities	**$ 129,958**	$ 237
Total liabilities	**129,958**	237
Net assets (deficit)		
Unrestricted	**(214,166)**	83,441
Temporarily restricted	**501,742**	262,988
Permanently restricted	**105,650**	99,110
Total net assets	**393,226**	445,539
Total liabilities and net assets	**$ 523,184**	$ 445,776

	2008 Unrestricted	2008 Temporarily Restricted	2008 Permanently Restricted	2008 Total	2007 Total
Operating revenue	**$ 59,218**	**$ 238,754**	**$ 6,540**	**$ 304,512**	$ 287,829
Operating expenses	**277,431**	**-**	**-**	**277,431**	213,456
Operating income	**(218,213)**	**238,754**	**6,540**	**27,081**	74,373
Nonoperating income (expense)	**(79,394)**	**-**	**-**	**(79,394)**	97,411
Change in net assets	**(297,607)**	**238,754**	**6,540**	**(52,313)**	171,784
Net assets, beginning of year	**83,441**	**262,988**	**99,110**	**445,539**	273,755
Net assets, end of year	**$ (214,166)**	**$ 501,742**	**$ 105,650**	**$ 393,226**	$ 445,539

13) Subsequent Events

Effective September 1, 2008, the board of trustees approved the sale of RMCHCS' outpatient dialysis centers to Red Rocks Dialysis. However, a specific price has not yet been determined and the sale has not been finalized as of January 9, 2009. In the interim, RMCHCS has engaged Red Rocks Dialysis to provide certain management and administrative services for the dialysis centers until the closing date of the sale. This interim period is not expected to extend past one year.

As of August 31, 2008, RMCHCS was in the process of constructing a new dialysis center. This construction is ongoing and will be completed as scheduled. This building will remain an asset of RMCHCS upon completion, and it is expected that the building will be leased to Red Rocks Dialysis. The recorded amount of construction in progress related to this building as of August 31, 2008 was approximately $379,000.

Supplementary Information Required
by New Mexico State Auditor

Rehoboth McKinley Christian
Health Care Services, Inc.
Supplemental Schedule of Pledged Collateral
August 31, 2008

Financial Institution	Total Amount of Deposit in Bank	Insured Portion	Required Collateralization 50% of Uninsured Portion	Collateral Pledged	Over/ (Under) Collateralized
Bank of America	$ 118,532	$ 100,000	$ 9,266	$ -	$ (9,266)
Wells Fargo Bank	2,198,885	100,000	1,049,443	637,566	(411,877)
Gallup Federal Bank	398,287	100,000	149,144	-	(149,144)
Total	$ 2,715,704	$ 300,000	$ 1,207,853	$ 637,566	$ (570,287)

Pledged collateral

Custodian	Type of Security	CUSIP Number	Sequence Number	Maturity Date	Fair Value
Wells Fargo	FNCL	31412S4S1	012713	4/1/2038	$ 637,566

Rehoboth McKinley Christian
Health Care Services, Inc.
Supplemental Schedule of Deposits and Investments
August 31, 2008

Account Title	Account Type	Bank Balance	Reconciling Items	Book Balance
Cash and cash equivalents				
Wells Fargo Bank				
Operational	Checking	$ 1,663,527	$ 636,860	$ 2,300,387
Operational	Depository	-	15,823	15,823
Operational	Accounts payable zero balance account	-	(471,894)	(471,894)
Operational	Payroll zero balance account	-	(72,862)	(72,862)
Operational	Pension account	535,358	-	535,358
Gallup Federal Bank				
Foundation Operational	Checking	67,078	(4,893)	62,185
Foundation Restricted Checking	Checking	331,209	-	331,209
Bank of America				
Operational	Accounts payable zero balance account	-	(25,646)	(25,646)
Operational	Payroll zero balance account	-	(491)	(491)
Operational	Depository	118,532	(18,794)	99,738
Total deposits		2,715,704	58,103	2,773,807
Petty cash		3,650	-	3,650
Total cash		2,719,354	58,103	2,777,457
Short-term investments and other				
Flex comprehensive cash	Cash equivalent	-	(1,164)	(1,164)
Total short-term investments and other		-	(1,164)	(1,164)
Total cash and cash equivalents		$ 2,719,354	$ 56,939	$ 2,776,293
Bond funds and other investments				
Wells Fargo Bank				
Working Capital Fund	Cash equivalent	$ 286,366	$ -	$ 286,366
Project Fund	Cash equivalent	1,662,478	-	1,662,478
Series 2007 Bond Principal Fund	Cash equivalent	2,318	-	2,318
Series 2007 Bond Reserve Fund	Cash equivalent	645,300	-	645,300
Gallup Federal Bank				
RMCHCS Foundation certificate of deposit	Cash equivalent	103,128	-	103,128
Zia Trust				
Irrevocable trust - 457(b) plan	Cash equivalent	10,662	-	10,662
Irrevocable trust - 457(b) plan	Equity securities	78,620	-	78,620
Irrevocable trust - 457(b) plan	Fixed income securities	56,640	-	56,640
Merrill Lynch				
Hadden Trust Investment	Cash equivalent	1,352	7,592	8,944
Hadden Trust Investment	Equity securities	26,692	-	26,692
Total bond funds and other investments		$ 2,873,556	$ 7,592	$ 2,881,148

REDW LLC
The Rogoff Firm
CERTIFIED PUBLIC ACCOUNTANTS | BUSINESS & FINANCIAL ADVISORS

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*

Board of Trustees and Management of
Rehoboth McKinley Christian Health Care Services, Inc.
and
Mr. Hector H. Balderas, New Mexico State Auditor

We have audited the consolidated financial statements of Rehoboth McKinley Christian Health Care Services, Inc. (the "Hospital") as of and for the year ended August 31, 2008, as listed in the table of contents, and have issued our report thereon dated January 9, 2009. We conducted our audit in accordance with generally accepted auditing standards established by the Auditing Standards Board (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 Hospital'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 Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over financial reporting.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

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

Compliance and Other Matters

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

We noted certain other matters that are required to be reported under *Government Auditing Standards* paragraphs 5.14 and 5.16, and Section 12-6-5 NMSA 1978, which are described in the accompanying schedule of findings and responses as items SA 08-1 and SA 08-2.

The Hospital's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the Hospital's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the boards of trustees, management, others within the Hospital, the New Mexico Office of the State Auditor, and the New Mexico Legislature, and is not intended to be and should not be used by anyone other than these specified parties.

REDW LLC

January 9, 2009

Rehoboth McKinley Christian Health Care Services, Inc.
Schedule of Findings and Responses
For the Year Ended August 31, 2008

The following findings are reported in accordance with the New Mexico State Audit Rule 2 NMAC 2.2., *Requirements for Contracting and Conducting Audits of Agencies*.

SA 08-1 — Cash Collateralization (Prior Year Finding 07-1)

Criteria or Specific Requirement: In accordance with Section 6-10-17, NMSA, 1978 Compilation, the Hospital is required to collateralize an amount equal to one-half of the public money in excess of $100,000 at each financial institution.

Condition: At August 31, 2008, the Hospital had uninsured bank deposits of $2,415,704 in separate financial institutions. State law requires that $1,207,852 be collateralized. The Hospital did not have adequate collateral in place to cover this balance.

Cause: The Hospital's bank did not maintain adequate collateral over the Hospital's deposits.

Effect: The deposits were not collateralized appropriately, and the Hospital was not in compliance with the cash collateralization requirements.

Recommendation: Consider either obtaining collateralization for bank deposits in excess of $100,000 or moving the deposits to multiple banks with less than $100,000 in each.

Management Response:

Based on correspondence with Wells Fargo, we are currently in compliance with the collateralization requirements and based on changes FDIC has made, (see below) we will maintain compliance through the end of the next fiscal year.

On October 14, 2008 the FDIC announced its temporary Transaction Account Guarantee Program, which provides full coverage for non-interest bearing transaction deposit accounts at FDIC-insured institutions that agree to participate in the program. The transaction account guarantee applies to all personal and business checking deposit accounts that do not earn interest at participating institutions. This unlimited insurance coverage is temporary and will remain in effect for participating institutions until December 31, 2009.

SA 08-2 — Mileage Reimbursement

Criteria or Specific Requirement: In accordance with the Per Diem and Mileage Act, Section 10-8-2 (D), NMSA, 1978 Compilation, the Hospital is required to reimburse every employee at the Internal Revenue Service (IRS) standard mileage rate for the use of privately owned vehicles for each mile traveled if the travel is necessary to the discharge of official duties.

Condition: Three of three employees tested were reimbursed at rates below the IRS standard mileage rate.

Cause: The Hospital has not updated its travel policies and procedures or its travel reimbursement forms.

Effect: These employees were not fully reimbursed for their business-related travel, and the Hospital was not in compliance with the Per Diem and Mileage Act.

Recommendation: Update policies and procedures within the Hospital to include travel policies and procedures. At a minimum, update the travel reimbursement forms to reflect current IRS standard mileage rates and periodically review the IRS website for any changes to this rate.

Management Response: Upon receiving notice that we were not in compliance with this Act, management updated its mileage reimbursement practice to pay at the IRS standard mileage rate.

Rehoboth McKinley Christian
Health Care Services, Inc.
Current Status Schedule of 2007 Audit Findings
For the Year Ended August 31, 2008

Prior-Year Number	Description	Current Status
07-1	Cash Collateralization	Not resolved. Repeated as SA 08-1

Rehoboth McKinley Christian
Health Care Services, Inc.
Other Disclosures
For the Year Ended August 31, 2008

Exit Conference
A closed meeting exit conference was held on January 13, 2009, with the following attending:

Rehoboth McKinley Christian Health Care Services, Inc.:

Board Members
Claudia Klesert
Dr. Alan Beamsley
Tony Gonzales
Eric D. Begay (also a board member of RMCHCS Foundation)
Priscilla Smith
Michelle Stam-Maclaren

Staff
Mark Hall, CFO
Mary Poel, CMO
Teresa Lopez, Administrative Assistant
Pat Wolfram, Interim CEO – ex-officio

REDW LLC
Chris Tyhurst, Principal
Angie Olvera, Manager

Financial Statement Preparation
The Hospital's independent public accountants prepared the accompanying financial statements; however, the Hospital is responsible for the financial statement and footnote content.