

**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**
Auditor's Report and Financial Statements
June 30, 2014 and 2013



**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**
June 30, 2014 and 2013

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Independent Auditor's Report

Board of Directors
Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation
Tomball, Texas

We have audited the accompanying financial statements of Tomball Hospital Authority d/b/a Tomball Regional Health Foundation, which comprise the balance sheets as of June 30, 2014 and 2013, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Tomball Hospital Authority d/b/a Tomball Regional Health Foundation as of June 30, 2014 and 2013, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economical or historical context. Our opinion on the basic financial statements is not affected by this missing information.

BKD, LLP

Houston, Texas
November 18, 2014

**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**

**Balance Sheets
June 30, 2014 and 2013**

Assets

	2014	2013
Current Assets		
Cash and cash equivalents	\$ 2,260,526	\$ 2,342,641
Short-term investments	-	41,080,764
Restricted cash equivalents	-	124,926
Accrued interest receivable	202,557	403,082
Estimated amounts due from third-party payers	1,180,644	-
Prepaid expenses and other	103,464	120,901
Total current assets	3,747,191	44,072,314
Noncurrent Cash and Investments		
Long-term investments	86,538,728	40,432,890
Held by trustee under self-insurance trust	-	132,084
	86,538,728	40,564,974
Less amount required to meet current obligations	-	124,926
	86,538,728	40,440,048
Capital Assets, Net	631,470	650,398
Total assets	\$ 90,917,389	\$ 85,162,760

Liabilities and Net Position

	2014	2013
Current Liabilities		
Accounts payable	\$ 63,571	\$ 819,215
Estimated amounts due to third-party payers	-	270,676
Estimated self-insurance costs	83,866	124,926
	<hr/>	<hr/>
Total current liabilities	147,437	1,214,817
Estimated Self-insurance Costs	<hr/> 601,148	<hr/> 604,845
Total liabilities	<hr/> 748,585	<hr/> 1,819,662
Net Position		
Net investment in capital assets	631,470	650,398
Unrestricted	89,537,334	82,692,700
	<hr/>	<hr/>
Total net position	90,168,804	83,343,098
Total liabilities and net position	<hr/> <hr/> \$ 90,917,389	<hr/> <hr/> \$ 85,162,760

**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**
Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Operating Revenues	\$ 7,128	\$ 0
Operating Expenses		
Salaries and benefits	210,627	182,408
Purchased services and professional fees	361,535	1,577,883
Program fees	655,560	381,284
Supplies and other	242,098	392,256
Depreciation expense	18,928	7,054
Insurance	96,826	326,704
	<u>1,585,574</u>	<u>2,867,589</u>
Operating Loss	<u>(1,578,446)</u>	<u>(2,867,589)</u>
Nonoperating Revenue (Expenses)		
Investment income (loss)	8,399,990	(74,716)
Upper Payment Limit program expense	(646,331)	(3,713,644)
	<u>7,753,659</u>	<u>(3,788,360)</u>
Excess (Deficiency) of Revenues Over Expenses From Continuing Operations	6,175,213	(6,655,949)
Discontinued Operations		
Gain (loss) from discontinued operations	650,493	(1,225,546)
Increase (Decrease) in Net Position	6,825,706	(7,881,495)
Net Position, Beginning of Year	<u>83,343,098</u>	<u>91,224,593</u>
Net Position, End of Year	<u>\$ 90,168,804</u>	<u>\$ 83,343,098</u>

**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**

**Statements of Cash Flows
Years Ended June 30, 2014 and 2013**

	2014	2013
	<u> </u>	<u> </u>
Operating Activities		
Receipts (payments) on behalf of patients	\$ (800,827)	\$ 1,045,081
Payments to suppliers and contractors	(2,138,983)	(4,737,897)
Payments to employees	(210,627)	(182,408)
Other receipts, net	7,128	-
	<u> </u>	<u> </u>
Net cash used in operating activities	(3,143,309)	(3,875,224)
	<u> </u>	<u> </u>
Noncapital Financing Activity		
Upper Payment Limit program payments	(646,331)	(3,713,644)
	<u> </u>	<u> </u>
Net cash used in noncapital financing activity	(646,331)	(3,713,644)
	<u> </u>	<u> </u>
Capital and Related Financing Activity		
Purchase of capital assets	-	(94,642)
	<u> </u>	<u> </u>
Net cash used in capital and related financing activity	0	(94,642)
	<u> </u>	<u> </u>
Investing Activities		
Interest and dividends on investments	1,733,317	1,152,012
Purchases of investments	(94,737,507)	(120,214,157)
Proceeds from disposition of investments	96,579,631	40,263,298
Proceeds from sale of hospital operations	-	2,632,002
	<u> </u>	<u> </u>
Net cash provided by (used in) investing activities	3,575,441	(76,166,845)
	<u> </u>	<u> </u>
Decrease in Cash and Cash Equivalents	(214,199)	(83,850,355)
	<u> </u>	<u> </u>
Cash and Cash Equivalents, Beginning of Year	2,474,725	86,325,080
	<u> </u>	<u> </u>
Cash and Cash Equivalents, End of Year	<u>\$ 2,260,526</u>	<u>\$ 2,474,725</u>

**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**

Statements of Cash Flows (Continued)

Years Ended June 30, 2014 and 2013

	2014	2013
Reconciliation of Cash and Cash Equivalents to the Balance Sheets		
Cash and cash equivalents in current assets	\$ 2,260,526	\$ 2,342,641
Cash and cash equivalents in noncurrent cash and investments	-	132,084
	<u>\$ 2,260,526</u>	<u>\$ 2,474,725</u>
 Reconciliation of Net Operating Loss to Net Cash Used in Operating Activities		
Operating loss	\$ (1,578,446)	\$ (2,867,589)
Gain (loss) from discontinued operations	650,493	(1,225,546)
Depreciation and amortization	18,928	7,054
Changes in operating assets and liabilities:		
Estimated amounts due from and to third-party payers	(1,451,320)	1,186,175
Accounts payable and accrued expenses	(800,401)	(1,135,491)
Other current assets and liabilities	17,437	160,173
	<u>\$ (3,143,309)</u>	<u>\$ (3,875,224)</u>

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements

June 30, 2014 and 2013

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Reporting Entity

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation (the Authority), was organized under the *Texas Hospital Authority Act* in 1973 as a body politic and corporate and political subdivision of the State of Texas. Five of the Authority's 11 Board of Directors (the Board) are appointed by Tomball's City Council. The remaining six members are appointed by the Board.

Prior to October 1, 2011, the Authority, formerly Tomball Hospital Authority d/b/a Tomball Regional Hospital, owned and operated Tomball Regional Hospital (the Hospital), an acute-care hospital located in Tomball, Texas. The Authority primarily earned revenues by providing inpatient, outpatient and emergency care services to patients in Tomball, Texas, and surrounding areas.

Effective October 1, 2011, the Authority sold the interest in its Hospital operations and substantially all of its assets, including its interests in Tomball Hospital Holdings (THH), Tomball Regional Medical Center Provider Network and an interest in Tomball Ambulatory Surgery Center d/b/a Medical Complex Surgical Center (TASC) to Tomball Texas Holdings, LLC (TTH), a subsidiary of Community Health Systems, Inc. (CHS). A portion of the proceeds were used to pay in full the outstanding long-term debt of the Authority. The Authority aims to use the remaining resources to improve the access to and quality of health care for residents of Tomball, Texas, and the surrounding areas.

Basis of Accounting and Presentation

The financial statements of the Authority have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally federal and state grants) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program-specific, such as investment income and Upper Payment Limit (UPL) program payments, are included in nonoperating revenues and expenses. The Authority first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position are available.

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements

June 30, 2014 and 2013

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Authority considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2014 and 2013, cash equivalents consisted primarily of money market accounts with brokers.

Risk Management

The Authority is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

The Authority is self-insured for its exposure to risk of loss from medical malpractice, general liability, workers' compensation claims and prior to October 1, 2011, employee health. Annual estimated provisions are accrued for these claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Investments and Investment Income

Investments in U.S. Treasury, agency and instrumentality obligations with a remaining maturity of one year or less at time of acquisition are carried at fair value. All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income, realized gains and losses on investments, and the net change for the year in the fair value of investments carried at fair value.

Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The estimated useful lives used by the Authority are as follows:

Equipment

3-20 years

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements

June 30, 2014 and 2013

Net Position

Net position of the Authority is classified in two components. Net investment in capital assets consists of capital assets net of accumulated depreciation. Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets.

Net Patient Service Revenue

Prior to October 1, 2011, the Authority had agreements with third-party payers that provided for payments to the Authority at amounts different from its established rates. Net patient service revenue was reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and included estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments were considered in the recognition of revenue on an estimated basis in the period the related services were rendered and such estimated amounts were revised in future periods as adjustments became known.

Income Taxes

As a political subdivision under the laws of the State of Texas, the Authority is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Authority may be subject to federal income tax on any unrelated business taxable income.

Note 2: Net Patient Service Revenue

Prior to the sale of the Hospital, the Authority had agreements with third-party payers that provided for payments to the Hospital at amounts different from its established rates. These payment arrangements included:

Medicare – Inpatient and substantially all outpatient services rendered to Medicare program beneficiaries were paid at prospectively determined rates. These rates varied according to a patient classification system that is based on clinical, diagnostic and other factors. The Authority was reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare fiscal intermediary.

Medicaid – Inpatient services were paid based on a prospective payment system. Most outpatient services rendered to Medicaid program beneficiaries were reimbursed under a cost reimbursement methodology. The Authority was reimbursed for cost reimbursable services at tentative rates with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicaid fiscal intermediary.

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements

June 30, 2014 and 2013

On December 12, 2011, the United States Department of Health and Human Services approved a new Medicaid Section 1115(a) demonstration entitled "Texas Health Transformation and Quality Improvement Program" (the Waiver). The Waiver expands existing Medicaid managed-care programs and established two funding pools that will assist providers with uncompensated care costs and promote health system transformation. The Authority submits intergovernmental transfer payments to the federal government on behalf of the Hospital. During the years ended June 30, 2014 and 2013, the Authority submitted approximately \$646,000 and \$3,600,000, respectively, in inter-governmental transfers on behalf of the Hospital.

One of the funding pools established by the Waiver is the Delivery System Reform Incentive Program (DSRIP). Under this program, hospitals, through coordination with the Regional Healthcare Partnership to which they have been assigned, are charged with coordinating various projects to improve the delivery of health care in their service area and achieve specific goals associated with improving the health of the population served and reducing overall utilization. During 2013, in association with the DSRIP program, the Authority submitted approximately \$67,000 in inter-governmental transfers on behalf of the Hospital.

Note 3: Deposits, Investments and Investment Income

Deposits

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Authority's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State law generally requires collateralization of all deposits with federal depository insurance; bonds and other obligations of the U.S. Treasury; U.S. agencies or instrumentalities of the State of Texas; or bonds of any city, county, school district or special road district of the State of Texas having an aggregate value at least equal to the amount of the deposits.

At June 30, 2014 and 2013, approximately \$0 and \$2,171,000, respectively, of the Authority's deposits exceeded federally insured limits. No collateral was in place for the uninsured balance at June 30, 2013.

Investments

The Authority may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. Pursuant to the passing of Senate Bill 233 on September 1, 2013, a hospital authority that no longer owns or operates a hospital and is using the remaining assets to promote public health and general welfare initiatives can invest the remaining assets as provided by

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements June 30, 2014 and 2013

Chapter 2256 Government Code. The Authority modified their investment policy during the year ended June 30, 2014, as Senate Bill 233 allowed them to expand the investment portfolio to include U.S. and global equities and fixed income securities.

At June 30, 2014 and 2013, the Authority had the following investments and maturities:

Type	Fair Value	Maturities in Years			
		Less Than 1	1-5	6-10	More Than 10
June 30, 2014:					
Money market mutual funds	\$ 804,353	\$ 804,353	\$ -	\$ -	\$ -
Equity securities:					
U.S. equity securities	35,060,734	35,060,734	-	-	-
Global equity securities	14,573,258	14,573,258	-	-	-
Fixed income:					
U.S. fixed income non-government/agency	33,528,249	33,528,249	-	-	-
Global fixed income	2,572,134	2,572,134	-	-	-
	<u>\$ 86,538,728</u>	<u>\$ 86,538,728</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
June 30, 2013:					
Money market mutual funds	\$ 20,227,151	\$ 20,227,151	\$ -	\$ -	\$ -
U.S. Treasury or agency obligations	61,286,503	20,853,613	26,846,999	10,591,748	2,994,143
	<u>\$ 81,513,654</u>	<u>\$ 41,080,764</u>	<u>\$ 26,846,999</u>	<u>\$ 10,591,748</u>	<u>\$ 2,994,143</u>

Interest Rate Risk. As a means of limiting its exposure to fair value losses arising from rising interest rates, the Authority's investment policy limits the maximum weighted-average maturity of its investment portfolio to two years.

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. It is the Authority's policy to limit its investments in commercial bonds and equity securities to the top three ratings issued by nationally recognized statistical rating organizations (NRSROs). At June 30, 2014 and 2013, the Authority's investments in U.S. agencies' obligations not directly guaranteed by the U.S. Government were rated "AA+" by Standard & Poor's.

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements June 30, 2014 and 2013

Custodial Credit Risk. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Authority's investment policy requires all securities underlying repurchase agreements be pledged to the Authority, held in the Authority's name and deposited at the time the investment is made with the Authority or with a third party selected and approved by the Authority. The Authority held no securities under repurchase agreements as of June 30, 2014 and 2013.

Concentration of Credit Risk. The Authority places no limit on the amount that may be invested in any one issuer.

Summary of Carrying Values

The carrying values of deposits and investments are included in the balance sheets as follows:

	2014	2013
Carrying value:		
Deposits	\$ 2,260,526	\$ 2,474,725
Investments	86,538,728	81,513,654
	\$ 88,799,254	\$ 83,988,379
Included in the following balance sheet captions:		
Cash and cash equivalents	\$ 2,260,526	\$ 2,342,641
Short-term investments	-	41,080,764
Noncurrent cash and investments	86,538,728	40,564,974
	\$ 88,799,254	\$ 83,988,379

Investment Income (Loss)

Investment income (loss) for the years ended June 30, 2014 and 2013, consisted of the following items:

	2014	2013
Interest and dividend income	\$ 1,532,792	\$ 1,555,094
Net realized and unrealized gains (losses)	6,867,198	(1,629,810)
	\$ 8,399,990	\$ (74,716)

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements June 30, 2014 and 2013

Note 4: Capital Assets

Capital assets activity for the years ended June 30 was as follows:

	2014			
	Beginning Balance	Additions	Disposals	Ending Balance
Land	\$ 562,810	\$ -	\$ -	\$ 562,810
Equipment	94,642	-	-	94,642
	657,452	0	0	657,452
Less accumulated depreciation:				
Equipment	7,054	18,928	-	25,982
Capital assets, net	\$ 650,398	\$ (18,928)	\$ 0	\$ 631,470
	2013			
	Beginning Balance	Additions	Disposals	Ending Balance
Land	\$ 562,810	\$ -	\$ -	\$ 562,810
Equipment	-	94,642	-	94,642
	562,810	94,642	0	657,452
Less accumulated depreciation:				
Equipment	-	7,054	-	7,054
Capital assets, net	\$ 562,810	\$ 87,588	\$ 0	\$ 650,398

Note 5: Risk Management

As a unit of government covered by the *Texas Tort Claims Act* (the Act), the Authority's liability for general and malpractice claims is limited to \$100,000 per person and \$300,000 per occurrence, with no annual limit. The Authority is self-insured for amounts not limited by the Act. Losses from asserted and unasserted claims identified under the Authority's incident reporting system are accrued based on estimates that incorporate the Authority's past experience, as well as other considerations, including the nature of each claim or incident and relevant trend factors. Accrued malpractice and general liability losses have been estimated by professional insurance consultants. It is reasonably possible that the Authority's estimate of losses will change by a material amount in the near term.

Tomball Hospital Authority d/b/a Tomball Regional Health Foundation

Notes to Financial Statements June 30, 2014 and 2013

The Authority is self-insured for workers' compensation claims costs. A provision is accrued for workers' compensation claims including both claims reported and claims incurred, but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims, and other economic and social factors. It is reasonably possible that the Authority's estimate will change by a material amount in the near term.

Activity in the Authority's accrued liabilities during 2014 and 2013 is summarized as follows:

	2014	
	General and Professional Liability	Workers' Compensation
Balance, beginning of year	\$ 100,000	\$ 629,771
Changes in estimates for claims incurred in prior years	-	43,012
Claims and expenses paid	-	(87,769)
Balance, end of year	\$ 100,000	\$ 585,014
	2013	
	General and Professional Liability	Workers' Compensation
Balance, beginning of year	\$ 500,992	\$ 72,831
Current year claims incurred and changes in estimates for claims incurred in prior years	(400,992)	651,290
Claims and expenses paid	-	(94,350)
Balance, end of year	\$ 100,000	\$ 629,771

Note 6: Operating Lease

A noncancellable operating lease for the Authority's office expires in 2017. Rental payments include base rent plus additional items.

**Tomball Hospital Authority d/b/a
Tomball Regional Health Foundation**

**Notes to Financial Statements
June 30, 2014 and 2013**

Future minimum lease payments at June 30, 2014, were as follows:

2015	\$ 48,000
2016	48,000
2017	<u>40,000</u>
Future minimum lease payments	<u><u>\$ 136,000</u></u>

Note 7: Commitments and Contingencies

Purchase Indemnification

Under the asset purchase agreement between the Authority and TTH, the Authority is liable for any misrepresentation or breach of warranty made in the agreement if total losses to TTH exceed \$1,000,000. The Authority is liable for any single claim in excess of \$15,000 up to an overall limit equal to 15 percent of the purchase price. At June 30, 2014 and 2013, no liability has been recorded.

Litigation

In the normal course of business, the Authority is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Authority's self-insurance program (discussed elsewhere in these notes) or by commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Authority evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

Note 8: Discontinued Operations

During the year ended June 30, 2012, as part of the asset purchase agreement, the Authority sold the operations of its medical center provider and ambulatory surgery center. During the years ended June 30, 2014 and 2013, there were additional amounts related to the sale of the Hospital that were recognized.