A Report
to the
Montana
Legislature

Financial-Compliance Audit

Montana Facility Finance Authority

For the Two Fiscal Years Ended June 30, 2010

December 2010

Legislative Audit
Division

10-12

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Financial-compliance audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2009, was issued March 1, 2010. The Single Audit Report for the two fiscal years ended June 30, 2011, will be issued by March 31, 2012. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
Room 277, State Capitol
P.O. Box 200802
Helena, MT 59620-0802

Legislative Audit Division
Room 160, State Capitol
P.O. Box 201705
Helena, MT 59620-1705

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LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel

Deputy Legislative Auditors
James Gillett
Angie Grove

December 2010

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit of the Montana Facility Finance Authority (Authority) for the two fiscal years ended June 30, 2010. We performed this audit of the Authority in compliance with §90-7-121, MCA. This report contains no recommendations.

The Authority's Executive Director reviewed and agreed with the contents of this report and chose not to respond in writing. We thank the members of the Montana Facility Finance Authority and their staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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Phone (406) 444-3122 • FAX (406) 444-9784 • E-Mail lad@mt.gov

Table of Contents

Appointed and Administrative Officials

			Profession	Term Expires
Board Members	Jon Marchi, Chair	Polson	Venture Capital/Ranching	2013
	Richard (Dick) King	Missoula	Missoula Area Economic Development	2013
	Larry Putnam	Helena	Hospital Administrator	2013
	James W. (Bill) Kearns	Townsend	Banker	2013
	Kim Rickard	Helena	Laborers Union Business Manager	2011
	Matthew B. Thiel	Missoula	Attorney	2011
	Joe Quilici	Butte	Former Business Owner Former State Legislator	2011

Administrative Staff

Michelle Barstad, Executive Director

Sandy Oitzinger, Associate Director

Nolan Brilz, Program Specialist

Teri Juneau, Accountant

For additional information concerning the Montana Facility Finance Authority, contact:

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Montana Facility Finance Authority
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MONTANA LEGISLATIVE AUDIT DIVISION

FINANCIAL-COMPLIANCE AUDIT

Montana Facility Finance Authority

For the Two Fiscal Years Ended June 30, 2010

DECEMBER 2010 10-12 REPORT SUMMARY

The Montana Facility Finance Authority (Authority) issued over $280 million in bonds and notes during fiscal years 2010 and 2009. At fiscal year-end 2010 and 2009, the Authority's outstanding bonds, notes, and loans exceeded $966 million and $879 million, respectively.

Context

The Authority provides access to various debt financing or refinancing instruments at reduced rates to Montana nonprofit private and public health care institutions or prerelease centers for purchases of capital equipment and buildings. The Authority administers six programs:

Direct Loan Program – provides short-term loans up to five years, in amounts of $200,000 or less, to eligible facilities for construction, renovation, acquisition, equipment purchases, and the refinancing of outstanding debt.

Equipment Revenue Note Program – provides financing for acquisition and installation of equipment. The notes are privately placed with investors for the useful life of the equipment.

Master Loan Program – loan proceeds from tax exempt bond issuances with negotiable terms and used to finance new construction projects with negotiable terms, refinance outstanding bonds, acquire real property, purchase equipment, or reimburse borrowers for prior capital expenditures.

Trust Fund Loan Program – provides loans to eligible facilities for capital projects. The legislature authorized the Authority to lend up to $15 million of the Permanent Coal Tax Trust funds. Loan terms are up to 20 years.

Stand-Alone Bond Program – issues tax-exempt bonds or notes for individual borrowers for terms up to 40 years.

Montana Capital Assistance Program – a grant program from Authority funds to help smaller hospitals deal with changing needs and services by providing funding for capital improvement plans, which are used to establish infrastructure priorities and to examine funding options for renovations and improvements.

Results

There are no findings or recommendations in this audit report.

Recommendation Concurrence	
Concur	0
Partially Concur	0
Do Not Concur	0
Source: Agency audit response included in final report.	

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Legislative Audit Division at 406-444-3122; e-mail to lad@mt.gov; or check the website at http://leg.mt.gov/audit.
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Call toll-free 1-800-222-4446, or e-mail lad@mt.gov.

Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Facility Finance Authority (Authority) for the two fiscal years ended June 30, 2010 and 2009. The objectives of the audit were to:

1. Determine whether the Authority complied with selected state laws and regulations.
2. Obtain an understanding of the Authority's control systems to the extent necessary to support an audit of the Authority's financial statements, and, if appropriate, make recommendations for improvement in management and the internal controls of the Authority.
3. Determine whether the Authority's financial statements present fairly the results of operations for the two fiscal years ended June 30, 2010, and 2009.

Background

The Authority is administratively attached to the Department of Commerce. The Authority provides access to various debt financing or refinancing instruments at reduced rates to Montana nonprofit private and public health care institutions or prerelease centers and to for-profit or nonprofit small manufacturing facilities for purchases of capital equipment and buildings.

The Authority administers six programs for the health care and prerelease sector and is developing a program for the small manufacturing facilities. Programs currently administered by the Authority include:

Direct Loan Program – provides short-term loans up to five years, in amounts of $200,000 or less, to eligible facilities for construction, renovation, acquisition, equipment purchases, and the refinancing of outstanding debt.

Equipment Revenue Note Program – provides financing for acquisition and installation of equipment. The notes are privately placed with investors for the useful life of the equipment.

Master Loan Program – loan proceeds from tax exempt bond issuances with negotiable terms and may be used to finance new construction projects with negotiable terms, refinance outstanding bonds, acquire real property, purchase equipment, or reimburse borrowers for prior capital expenditures.

Trust Fund Loan Program – provides loans to eligible facilities for capital projects. The legislature authorized the Authority to lend up to $15 million of the Permanent Coal Tax Trust funds. Loan terms are up to 20 years.

Stand-Alone Bond Program – issues tax-exempt bonds or notes for individual borrowers for terms up to 40 years.

Montana Capital Assistance Program – a grant program from Authority funds to help smaller hospitals deal with changing needs and services by providing funding for capital improvement plans, which are used to establish infrastructure priorities and to examine funding options for renovations and improvements.

There are no findings or recommendations in this audit report. There were no prior audit recommendations.

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel

Deputy Legislative Auditors
James Gillett
Angie Grove

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Assets of the Montana Facility Finance Authority as of June 30, 2010, and 2009, and the related Statement of Revenues, Expenses, and Changes in Fund Net Assets and Statement of Cash Flows for each of the fiscal years then ended. The information contained in these financial statements is the responsibility of the Authority's management. Our responsibility is to express an opinions on these financial statements based on our audit.

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 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 audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana Facility Finance Authority as of June 30, 2010, and 2009, and respective results of operation and its changes in cash flows for each of the fiscal years then ended, in conformity with accounting principles generally accepted in the United States of America.

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

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

November 3, 2010

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Montana Facility Finance Authority
Management's Discussion and Analysis, Financial Statements, and Notes

Montana Facility Finance Authority
Department of Commerce
A Component Unit of the State of Montana

Management's Discussion and Analysis

Years ended June 30, 2010 and 2009

The following represents Montana Facility Finance Authority (the "Authority") management's discussion and analysis of the Authority's financial performance during the fiscal years ended June 30, 2010 and 2009. Please read it in conjunction with the Authority's financial statements and accompanying notes.

Financial Highlights

- The Authority closed bonds/note issues:
  4 bond issues/8 series ($238,690,000) in FY 2010 and 4 ($44,220,000) in FY 2009
- The Authority made loans out of reserves designated for such purpose:
  3 loans ($447,325) in FY 2010 and 9 loans ($971,774) in FY 2009
- The Authority made loans from the Trust Fund Loan Program:
  3 loans ($2,862,695) in FY 2010 and 2 loans ($2,848,502) in FY 2009
- The Authority awarded (maximum of $60,000 per fiscal year) and expended funds for grants out of reserves designated for such purposes:
  During FY 2010, $0 was committed and $70,811 was expensed,
  During FY 2009, $56,380 was committed and $28,672 was expensed
- The Authority's total outstanding bonds/notes/loans increased to $974,394,182 in FY 2010 from $885,677,070 in FY 2009 and $896,837,597 in FY 2008

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the Authority's basic financial statements. The Montana Facility Finance Authority's basic financial statements comprise two components, basic financial statements, and notes to the financial statements. The Authority is a self-supporting entity and follows enterprise fund reporting. Accordingly, the financial statements are presented using the accrual basis of accounting.

Overall financial condition of the Authority improved from FY 2008 to FY 2009 and again in FY 2010 based on an increase in Net Assets and can be attributed to a larger portfolio that generates greater income. During the three fiscal years above, only two bond issues were publically marketed with the remainder being privately placed with banks or institutional investors. This can be attributed to two factors: 1) market turbulence causing unrest with investors willing to purchase bonds; and, 2) a provision included in the American Recovery and Reinvestment Act providing incentives for banks to purchase and hold tax-exempt bonds issued by the Authority.

Basic Financial Statements

The Statement of Net Assets presents information on all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Montana Facility Finance Authority is improving or deteriorating. The Statement of Revenues, Expenses, and Changes in Fund Net Assets presents revenues earned and expenses incurred during the year and classifies activities as either "operating" or "non-operating". The Statement of Cash Flows presents information related to cash inflows and outflows, categorized by operating and investing activities. The reconciliation of operating income to cash provided by operating activities explains the relationship between the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Fund Net Assets, showing that increases and decreases in operating assets often require the use or receipt of cash but do not result in recognition of revenue or an expense.

The basic financial statements can be found beginning on page A-6 of this report.

Notes to the financial statements

The notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the financial statements can be found beginning on page A-9 of this report.

Financial Analysis of the Authority

Condensed financial statements are presented below.

	2010	2009	2008
Total Assets	3,892,278	3,672,934	3,491,172
Total Current Liabilities	119,291	163,563	147,163
Total Non-current Liabilities	22,804	31,361	26,881
Total Liabilities	142,095	194,924	174,044
Invested in Capital Assets	45	45	45
Total unrestricted net assets	3,750,138	3,477,965	3,317,083
Total Net Assets	3,750,183	3,478,010	3,317,128
Total Net Assets and Liabilities	3,892,278	3,672,934	3,491,172
Total operating revenues	614,098	453,133	447,023
Operating expenses:			
Personal services	194,679	196,035	153,132
Contracted services	30,784	37,374	98,102
Other operating expenses	120,611	117,624	85,979
Grants	70,811	28,672	38,396
Total operating expenses	416,885	379,705	375,609
Operating income	197,213	73,428	71,414
Investment Earnings	74,960	87,454	133,438
Change in net assets	272,173	160,882	204,852

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
STATEMENT OF NET ASSETS - ENTERPRISE FUND
JUNE 30, 2010 AND 2009

ASSETS:		*2010*		*2009*
Current Assets:				
Cash & Cash Equivalents (Note 2)	$	2,136,426	$	1,922,397
Interest Receivable		612		1,218
Accounts Receivable		0		3,910
Short Term Notes Receivable (Note 4)		277,383		274,179
Securities Lending Collateral (Note 2)		87,367		133,997
Due From Primary Government		0		0
Prepaid Expenses		1,591		388
Total Current Assets		2,503,379		2,336,089
Noncurrent Assets:				
Long Term Notes Receivable (Note 4)		1,252,151		1,166,903
Investments (Note 2)		136,703		169,897
Capital Assets (Note 1)		45		45
Total NonCurrent Assets		1,388,899		1,336,845
Total Assets	$	3,892,278	$	3,672,934
LIABILITIES:				
Liabilities:				
Current Liabilities:				
Accounts Payable	$	10,800	$	13,258
Due to Primary Government		0		3,844
Secuities Lending Liability (Note 2)		87,367		133,997
Compensated Absences		21,124		12,464
Total Current Liabilities	$	119,291	$	163,563
Noncurrent Liabilities:				
Compensated Absences		9,915		25,385
OPEB Implicit Rate Subsidy		12,889		5,976
Total Noncurrent Liabilities		22,804		31,361
Total Liabilities		142,095		194,924
Net Assets				
Invested in Capital Assets Net of Related Debt	$	45	$	45
Total Unrestricted Net Assets		3,750,138		3,477,965
Total Net Assets (Note 6)	$	3,750,183	$	3,478,010
Total Net Assets and Liabilitites	$	3,892,278	$	3,672,934

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN FUND NET ASSETS
ENTERPRISE FUND
FOR FISCAL YEARS ENDED JUNE 30, 2010 AND 2009

	2010	*2009*
OPERATING REVENUES:		
Service Fees	$ 613,161	$ 448,835
Securities Lending Income	937	4,298
Total Operating Revenues	$ 614,098	$ 453,133
OPERATING EXPENSES:		
Personal Services	$ 194,679	$ 196,035
Contracted Services	30,784	37,374
Supplies and Materials	5,550	9,797
Communications	6,571	5,801
Benefits	6,913	3,050
Travel	13,565	16,536
Rent	23,575	23,118
Repairs and Maintenance	269	300
Other Expenses	41,552	31,650
OPEB	0	0
Securities Lending Expense	317	1,445
Grants	70,811	28,672
CU Expense to P Gov	22,299	25,927
Total Operating Expenses	$ 416,885	$ 379,705
Operating Income	$ 197,213	$ 73,428
NON OPERATING REVENUES (EXPENSES)		
Investment Earnings	74,960	87,454
Change in net assets	$ 272,173	$ 160,882
Net Assets Beginning of Period	$ 3,478,010	$ 3,317,128
Total Net Assets End of Period	$ 3,750,183	$ 3,478,010

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
STATEMENT OF CASH FLOWS
ENTERPRISE FUND
FOR FISCAL YEARS ENDED JUNE 30, 2010 AND 2009

		2010		*2009*
CASH FLOWS FROM OPERATING ACTIVITIES:				
Receipts for Sales and Services	$	617,071	$	555,346
Payments to Suppliers for Goods and Services		(201,125)		(197,777)
Payments to Employees		(222,845)		(184,723)
Net Cash Provided by (Used for) Operating Activities	$	193,101	$	172,846
CASH FLOWS FROM INVESTING ACTIVITIES:				
Cash Payments for Loans	$	(448,325)	$	(957,897)
Collection for Principal on Loans		359,873		261,080
Proceeds from Securities Lending Income		937		4,298
Payments of Securities Lending Costs		(317)		(1,445)
Cash Adjustment for STIP SIV's		33,194		61,812
Interest on Investments		75,566		91,418
Net Cash Provided by (Used for) Investing Activities:	**$**	20,928	$	(540,734)
Net Increase (Decrease) in Cash and Cash Equivalents	**$**	214,029	$	(367,888)
Cash & Cash Equivalents, July 1	$	1,922,397	$	2,290,285
Cash & Cash Equivalents, June 30	$	2,136,426	$	1,922,397
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:				
Operating Income (Loss)	$	197,213	$	73,428
ADJUSTMENTS TO RECONCILE OPERATING INCOME TO NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES:				
Depreciation		0		0
Securities Lending Expense		317		1,445
Securities Lending Income		(937)		(4,298)
Long Term Liability OPEB Implict Rate Subsidy		0		0
Change in Assets & Liabilities:				
Increase (Decrease) in Accounts Payable		(2,555)		(10,675)
Increase (Decrease) in Due to Primary Government		(3,747)		(1,834)
Increase (Decrease) in Compensated Absences Payable		(15,470)		1,430
Increase (Decrease) in OPEB		6,913		3,050
Increase (Decrease) in Compensated Absences Payable-Current		8,660		3,846
Decrease (Increase) in Accounts Receivable		3,908		106,511
Decrease (Increase) in Prepaid Expense		(1,202)		(57)
Decrease (Increase) in Due From Primary Government		0		0
Total Adjustments	$	(4,113)	$	99,418
Net Cash Provided by (Used for) Operating Activities	**$**	193,101	$	172,846

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

1. Summary of Significant Accounting Policies

Basis of Accounting

The Montana Facility Finance Authority (the "Authority") Enterprise Fund uses the accrual basis of accounting in accordance with Generally Accepted Accounting Principles. Under this basis, revenues are recognized in the accounting period when realizable, measurable, and earned. Expenses are recognized in the period incurred, when measurable.

Reporting Entity

The preceding financial statements are prepared from the Statewide Accounting Budgeting Human Resource System (SABHRS) and include the financial activity of the Authority's account in the Enterprise Fund. These statements are summaries of entries in the accounting records for the Authority and exclude any entries recorded for other agencies. Accordingly, these financial statements are not intended to fairly present the financial position, results of operations, or cash flow of the State of Montana. The Authority is a component unit of the State of Montana.

Nature of Fund

The fund maintained by the Authority, which conforms with authorizing legislation and Authority resolutions, is described as follows:

> The Enterprise Fund is used to account for operations financed and operated similar to private business enterprises, where the intent of the legislature is that costs are to be financed or recovered primarily through user charges.

Capital Assets

Capital assets are carried at cost less accumulated depreciation. Depreciation is provided for by using the straight-line method over the respective estimated useful lives of the assets.

Compensated Absences

Permanent employees are allowed to accumulate and carry over into a new calendar year a maximum of two times their annual accumulation of vacation leave. Upon termination, qualifying employees having unused accumulated vacation and sick leave receive 100 percent payment for vacation and 25 percent payment for sick leave. The accompanying financial statements reflect that liability.

2. Cash, Cash Equivalents, and Investments

Cash and Cash Equivalents

Cash and Cash Equivalents as presented on the accompanying Statement of Net Assets and Statement of Cash Flows represents the Authority's cash of $5,991 and $50,180 as of June 30, 2010 and 2009 respectively, and cash equivalents invested in the Board of Investments of the State of Montana Short-Term Investment Pool (STIP) of $2,267,138 and $2,042,114 for fiscal year 2010 and 2009, respectively. STIP balances include $136,703 for fiscal year 2010 and $169,897 for fiscal year 2009 of investments that are no longer liquid and classified as non-current assets (see last paragraph of Note 2 for further clarification). The Enterprise Fund invests its residual funds, by law, in STIP. STIP is considered an external investment pool. An external investment pool is defined as an arrangement that pools the monies of more than one legally separate entity and invests, on the participants behalf, in an investment portfolio. STIP is also classified as a 2a7-like pool. A 2a7-like pool is an external investment pool that

is not registered with the Securities and Exchange Commission (SEC) as an investment company, but has a policy that will, and does, operate in a manner consistent with the SEC Rule 2a7 of the Investment Company Act of 1940. If certain conditions are met, 2a7-like pools are allowed to use amortized cost rather than fair value to report net assets to compute unit values. The Board of Investments of the State of Montana (the "BOI") has adopted a policy to treat STIP as a 2a7-like pool. Cash and cash equivalents are defined as a short-term, highly liquid investment that is readily convertible to known amounts of cash.

Securities Lending

The BOI is authorized by law to lend its securities and has contracted with the custodial bank, State Street Bank and Trust "the Bank", to lend the BOI's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The custodial bank is required to maintain collateral equal to 102 percent of the fair value of domestic securities and 105 percent of the fair value of international securities while the securities are on loan. The Board and the bank split the earnings on security lending activities. The BOI retains all rights and risks of ownership during the loan period.

During fiscal years 2010 and 2009, the custodial bank lent BOI public securities and received as collateral: U.S. dollar cash; U.S. government and government sponsored agency securities; U.S. corporate debt securities and structured securities rated AA-/Aa3 or higher; sovereign debt securities of the G10 nations; and debt securities issued by certain supranational agencies. The Bank does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The BOI imposed no restrictions on the amount of securities available to lend during fiscal years 2010 and 2009. There were no failures by any borrowers to return loaned securities or pay distributions thereon during the period that resulted in a declaration and notice of Default of the Borrower (other than the default by Lehman Brothers Inc. which occurred in September 2008 and the BOI was made whole in the process). There were no losses resulting from a borrower default.

During fiscal years 2010 and 2009, the BOI and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received for each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool. The Securities Lending Quality Trust has a weighted average maturity of 20 and 31 days, respectively, as of June 30, 2010 and 2009. The relationship between the average maturities of the investment pool and the BOI's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the BOI could not determine. At year-end 2010 and 2009, the BOI had no credit risk exposure to borrowers because the collateral pledged by the borrowers exceeded the value of the securities borrowed.

As of June 30, 2010 and 2009, the Authority maintained security lending cash collateral of $87,367 and $133,997, respectively.

Investment Risk Disclosures

Effective June 30, 2007, the Authority implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40 – Deposit and Investment Risk Disclosures. The required GASB 40 risk disclosure for the authority is described below.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Credit Risk

Credit risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The Authority's investment is limited to STIP managed by the BOI. The Authority does not have a policy related to STIP investments. The BOI's policy requires that STIP securities have the highest investment grade rating in the short term category by at least one Nationally Recognized Statistical Rating Organizations (NRSRO). The five NRSRO's include Standard and Poors, Moody's, Duff and Phelps, Fitch, and Thompson's Bank Watch. Although the STIP investments have been rated by investment security type, STIP, as an external investment pool, has not been rated by the NRSRO.

At FYE 2010 and 2009 the STIP balance on SABHRS included $85,617,544 and $113,625,566, respectively, of investments in Structure Investment Vehicles, that were no longer liquid. As a result these are no longer considered cash equivalents and were reclassified from cash to investments based on a pro rata share of the State's investment in the pool. This will reflect the fact that this portion of STIP is not liquid enough to be considered a cash equivalent and the implicit backing of the pool with State cash. The Board of Investment believes the State will recover most, if not all, of the cash behind these investments. The Authority's portion is $136,703 for fiscal year 2010 and $169,897 for fiscal year 2009.

Custodial Credit Risk

STIP is managed by the BOI. STIP securities are registered in the nominee name for the BOI and held in the possession of its custodial bank, State Street Bank and Trust.

3. Revenue Bonds Outstanding

Resolutions adopted by the Authority have provided for trust and other agreements that establish specific funds to account for the proceeds of the various bond and note issues, mortgage and revenue notes receivable, debt service payments, payments by Borrowers, construction costs, and issuance costs. Specific funds established by agreements are held by trustees, or other participating financial institutions for the purpose of security and liquidity. Revenues are collected and disbursements made only in accordance with the provisions of applicable bond and note documents.

Most loans financed with bond proceeds are secured by first mortgages or security interests in the land, buildings, and related facilities and equipment financed by the Authority and utilized by the Borrower. Other loan payments are secured by a Master Note issued under a Master Trust Indenture of an Obligated Group or by standby letters of credit from financial institutions rated "A" or better. These liabilities do not constitute a general obligation debt or liability to the state of Montana, or any political subdivision thereof and accordingly, do not appear on the Statement of Net Assets.

The Health Care Revenue Bonds (Montana State Hospital Project) Series 1997[1] are special obligations of the state, payable solely from the facility revenue of the Montana State Hospital and the Montana Mental Health Nursing Center, both owned by the state and operated by the Montana Department of Public Health and Human Services. The Health Care Revenue Refunding Bonds (Montana Developmental Center Project) Series 2003[2] (which refunded the Health Care Revenue Bonds (Montana Developmental Center Project) Series 1994) are special obligations of the state, payable solely from the facility revenue of the Montana Developmental Center, which is owned by the state and operated by the Montana Department of Public Health and Human Services. The Health Care Revenue Bonds (Montana State Hospital Project) Series 1997[1] and the Health Care Revenue Refunding Bonds (Montana Developmental Center Project) Series 2003[2] do not constitute a general obligation debt of the state or obligate the state to appropriate or apply any funds or revenue of the state, other than the respective facility revenue and each of such bond issues are reflected in the State of Montana Basic Financial Statements.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Revenue Bonds Outstanding:

Issue	Period Outstanding	Type of Interest Rate	Outstanding June 30, 2010	Outstanding June 30, 2009
Health Care Variable Rate Revenue Bonds (Pooled Loan Program) Series 1985A	1985-2020	Variable	0	0
Hospital Facilities Revenue Bonds (Billings Deaconess Medical Center) Series 1991 A&B	1991-2016	Variable	17,800,000	20,200,000
Hospital Facilities Revenue Bonds (Billings Deaconess Medical Center) Series 1991 C	1991-2017	Variable	15,500,000	16,800,000
Health Care Revenue Bonds (Richland Opportunities, Inc. Project) Series 1993	1993-2013	Fixed	0	58,820
Hospital Revenue Bonds (Deaconess-Billings Clinic Health System Project) Series 1994	1994-2025	Variable	58,515,000	58,515,000
Health Care Facilities Revenue Bonds (Master Loan Program Marcus Daly Memorial Hospital Project) Series 1996B	1996-2011	Fixed	335,000	490,000
Health Care Facilities Revenue Bonds (Master Loan Program Glendive Medical Center Project) Series 1996C	1996-2011	Fixed	285,000	415,000
Health Care Revenue Bonds (Community Medical Center, Inc.) Series 1996	1996-2018	Fixed	12,400,000	13,325,000
Development Disability Facility Revenue Bonds (Beartooth Industries Project) Series 1997	1997-2024	Fixed	175,533	184,091
Prerelease Center Revenue Bonds (Alternatives, Inc. Project) Series 1997	1997-2017	Fixed	1,515,000	1,665,000
Health Care Revenue Bonds (Montana State Hospital) Project) Series 1997[1]	1997-2022	Fixed	16,930,000	17,945,000
Health Care Facilities Revenue Bonds (Master Loan Program-Big Horn Hospital Association Project) Series 1998A	1998-2018	Fixed	730,000	805,000
Health Care Facilities Revenue Bonds (Master Loan Program-Lewis & Clark County Nursing Home Project) Series 1998B	1998-2018	Fixed	885,000	975,000
Health Care Facilities Revenue Bonds (Master Loan Program-Lewis & Clark County Office Project) Series 1998D	1998-2018	Fixed	440,000	485,000
Revenue Bonds (Sisters of Charity of Leavenworth Health Services Corp.) Series 1998	1998-2024	Fixed	0	114,940,000
Developmental Disability Facilities Revenue Bonds (Opportunity Resources, Inc. Project) Series 1998	1998-2018	Fixed	100,194	111,760
Hospital Facilities Revenue Bonds (Kalispell Regional Hospital Project) Series 1998	1998-2018	Fixed	5,710,000	7,275,000
Hospital Facilities Revenue Bonds (Bozeman Deaconess Health Services Project) Series 1998	1998-2018	Fixed	0	7,655,000
Prerelease Center Revenue Bonds (Missoula Correctional Services Project) Series 1998A	1998-2018	Fixed	3,205,000	3,485,000
Prerelease Center Revenue Bonds (Great Falls Prerelease Services, Inc. Project) Series 1998B	1998-2013	Fixed	0	520,000
Health Care Facilities Revenue Bonds (Master Loan Program-Marcus Daly Memorial Hospital Corporation Project) Series 2000	2000-2020	Fixed	2,285,000	2,430,000
Prerelease Center Revenue Bonds (Boyd Andrew Prerelease) Series 2000	2000-2020	Fixed	1,540,000	1,635,000
Hospital Facilities Revenue Bonds (Kalispell Regional Medical Center) Series 2001	2001-2016	Fixed	12,670,000	13,935,000
Health Care Facilities Revenue Bonds (Master Loan Program-Community Medical Center Project) Series 2001 A&B	2001-2021	Fixed	4,015,000	4,230,000
Variable Rate Demand Revenue Bonds (Mission Ridge Project) – Series 2002	2002-2027	Variable	11,345,000	11,725,000
Health Care Revenue Refunding Bonds (Montana Developmental Center Project) Series 2003[2]	2003-2019	Fixed	7,365,000	8,030,000
Variable Rate Demand Revenue Bonds (Sisters of Charity of Leavenworth Health System Project) Series 2003	2003-2035	Variable	39,210,000	39,210,000

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Issue	Period Outstanding	Type of Interest Rate	Outstanding June 30, 2010	Outstanding June 30, 2009
Hospital Facilities Revenue Bonds (Bozeman Deaconess Health Services Project) Series 2004	2004-2029	Fixed	7,045,000	7,290,000
Hospital Facilities Revenue Bonds (St. Peter's Hospital Project) Series 2004	2004-2024	Fixed	26,985,000	27,755,000
Prerelease Center Revenue Bond (Boyd Andrew Community Services) Series 2004	2004-2014	Fixed	113,094	138,347
Health Care Facilities Revenue Bonds (Master Loan Program – Marias Medical Center Project) Series 2005A	2005-2028	Fixed	2,950,000	3,180,000
Health Care Facilities Revenue Bonds (Master Loan Program – Montana Children's Home and Hospital Project) Series 2005B	2005-2024	Fixed	7,640,000	8,065,000
Prerelease Center Revenue Bond (Boyd Andrew Community Services Project) Series 2005	2005-2021	Fixed	934,902	1,001,230
Revenue Refunding Bond (Mission Ridge Project) Series 2007	2005-2016	Fixed	1,316,199	1,522,932
Health Facilities Revenue Bonds (Bozeman Deaconess Health Services Obligated Group) Series 2005	2005-2035	Fixed	25,330,000	26,060,000
Developmental Disability Facility Revenue Bond (Spring Meadow Resources, Inc. Project) Series 2005	2005-2021	Fixed	467,002	499,362
Prerelease Center Revenue Bond (Great Falls Pre-Release Services, Inc. Project) Series 2005	2005-2021	Fixed	3,608,985	3,848,770
Health Care Facilities Revenue Refunding Bonds (Master Loan Program – Northern Montana Obligated Group Project) Series 2006A	2006-2016	Fixed	4,455,000	5,150,000
Variable Rate Demand Revenue Bonds (Sisters of Charity of Leavenworth Health System) Series 2006A	2006-2026	Variable	30,125,000	31,470,000
Revenue Bonds (Providence Health & Services) Series 2006B	2006-2026	Fixed	68,430,000	68,430,000
Prerelease Center Revenue Bonds (Alternatives, Inc.) Series 2006	2006-2026	Fixed	7,075,000	7,370,000
Revenue Bonds (Community, Counseling, and Correctional Services, Inc. Project) Series 2006A	2006-2026	Fixed	8,360,000	8,690,000
Revenue Bonds (Boyd Andrew Community Services Project) Series 2006B	2006-2026	Fixed	4,595,000	4,775,000
Senior Living Revenue Bonds (St. John's Lutheran Ministries Project) Series 2006A	2006-2036	Fixed	26,600,000	27,000,000
Senior Living Revenue Bonds (St. John's Lutheran Ministries Project) Series 2006B	2006-2036	Variable	2,870,000	2,950,000
Health Care Facilities Revenue Bonds (Master Loan Program - Marcus Daly Memorial Hospital) Series 2007A	2007-2027	Fixed	6,645,000	6,895,000
Hospital Facilities Revenue Bonds (St. Peter's Hospital Project) Series 2007	2007-2036	Fixed	16,855,000	18,620,000
Hospital Revenue Bonds (Benefis Healthcare System) Series 2007	2007-2037	Fixed	120,595,000	123,285,000
Health Care Facilities Revenue Bonds (Master Loan Program – Northeast Montana Health Services, Inc. Project) Series 2007B	2007-2032	Fixed	12,055,000	12,375,000
Health Care Facilities Revenue Bonds (Master Loan Program – St. Luke Community Healthcare Network Project) Series 2007C	2007-2032	Fixed	22,095,000	22,670,000
Hospital Revenue Bonds (Billings Clinic) Series 2008A	2008-2028	Fixed	18,895,000	20,000,000
Hospital Revenue Bonds (Billings Clinic) Series 2008B	2008-2028	Fixed	38,905,000	40,000,000
Health Care Facilities Revenue Bonds (Master Loan Program – Glendive Medical Center Series 2008A	2008-2034	Fixed	29,730,000	30,000,000
Revenue Bonds (Boyd Andrew Community Services Project) Series 2008	2009-2029	5-year Fixed	1,434,653	1,478,799

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Issue	Period Outstanding	Type of Interest Rate	Outstanding June 30, 2010	Outstanding June 30, 2009
Hospital Revenue Bonds (Billings Clinic) Series 2009A	2009-2020	3-year Fixed	9,306,092	10,000,000
Hospital Revenue Bonds (Billings Clinic) Series 2009B	2009-2020	5-year Fixed	2,629,091	2,720,000
Revenue Bonds (Rimrock Foundation Project) Series 2009	2009-2030	5-year Fixed	593,018	0
Health Care Facilities Revenue Bonds (Sisters of Charity of Leavenworth Health System) Series 2010A	2010-2024	Fixed	106,060,000	0
Health Care Facilities Revenue Bonds (Sisters of Charity of Leavenworth Health System) Series 2010B	2010-2040	Fixed	110,355,000	0
Total Revenue Bonds Outstanding			**$938,008,763**	**$870,284,111**

Stated maturities on Revenue Bonds Outstanding are as follows:

Maturing in Year Ended June 30	Bond Principal Payment (in thousands)
2011	$ 48,183
2012	31,192
2013	36,185
2014	37,908
2015-2040	784,541
Total	**$938,009**

The bonds are payable solely from loan repayments to be made by eligible facilities pursuant to loan agreements and, further, from the funds created by the indentures and investment earnings thereon.

Revenue Notes Outstanding:

Issue	Period Outstanding	Interest Rate	Outstanding June 30, 2010	Outstanding June 30, 2009
St. Patrick Hospital- Private Placement Revenue Note	1999-2010	6.06%	$459,326	$961,557
Community Medical Center- Private Placement Revenue Note	2001-2007	5.48%	0	0
St. Peter's Hospital-Private Placement Revenue Note	2001-2007	4.25%	0	0
St. Patrick Hospital-Private Placement Revenue Note	2002-2007	4.33%	0	0
St. Patrick Hospital-Private Placement Revenue Note	2002-2007	4.33%	0	0
Kalispell Regional Medical Center–Private Placement Revenue Note	2002-2010	4.65%	0	591,390
Kalispell Regional Medical Center–Private Placement Revenue Note	2007-2013	5.08%	827,272	1,119,526
Community Medical Center, Inc.–Private Placement Revenue Note	2003-2008	4.26%	0	0
Billings Clinic–Private Placement Revenue Note	2006-2011	3.99%	1,338,727	1,999,355
Kalispell Regional Medical Ctr.–Private Placement Revenue Note	2007-2017	4.22%	1,823,524	2,321,160
Community Medical Center-Private Placement Revenue Note	2007-2012	4.71%	0	137,201
Bozeman Deaconess-Private Placement Revenue Note 2010A	2010-2015	1.75%	3,505,000	0
Bozeman Deaconess-Private Placement Revenue Note 2010B	2010-2015	3.14%	3,140,000	0
Community Medical Center-Private Placement Revenue Note 2010A	2010-2014	2.66%	5,135,000	0
Community Medical Center-Private Placement Revenue Note 2010B	2010-2022	5.10%	9,390,000	0

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Community Medical Center-Private Placement Revenue Note 2010C	2010-2011	3.55%	495,000	0
Total Revenue Notes Outstanding			**$26,113,849**	**$7,130,189**

The notes are payable solely from loan repayments to be made by health institutions pursuant to loan agreements.

4. Notes Receivable

The Notes Receivable include loans made under the Authority's Direct Loan Program. The Short-Term Notes Receivable represents the portion of the loans that are due within the year following the balance sheet date.

Revenue Notes Receivable:
(MFFA Direct Loans)

Issue	Period Outstanding	Interest Rate	Outstanding June 30, 2010	Outstanding June 30, 2009
BSW, Inc.	2004-2009	3.53%	0	5,974
Ravalli Services	2004-2009	3.53%	0	3,294
Quality Life Concepts	2004-2009	3.53%	0	2,908
Eastern MT Community Mental Health Center	2005-2010	3.90%	0	4,907
Phillips County Hospital	2007-2010	3.90%	1,831	23,348
Liberty County Hospital and Nursing Home	2006-2011	4.50%	5,423	14,395
Beartooth Hospital and Health Center	2006-2011	4.48%	1,635	3,997
Northern Rockies Medical Center	2006-2009	4.60%	0	0
Boyd Andrew Community Services	2006-2011	4.62%	0	88,967
Northern Rockies Medical Center	2006-2011	4.60%	7,836	14,197
Broadwater Health Center	2007-2011	4.66%	5,498	13,432
Gateway Community Services	2007-2010	6.28%	73,592	76,041
Gateway Community Services	2007-2010	4.36%	1,176	5,752
Central Montana Medical Center	2007-2012	4.33%	32,061	44,842
Western Montana Mental Health	2008-2013	2.95%	81,514	107,123
Eastern MT Community Mental Health Center	2008-2013	2.83%	45,606	59,969
Big Sandy Medical Center	2008-2013	3.24%	38,620	50,682
Broadwater Heath Center	2008-2013	3.47%	34,564	45,003
Northern Rockies Medical Center	2008-2013	3.47%	17,431	22,621
Broadwater Heath Center	2008-2013	3.39%	37,010	47,603
Rimrock Foundation	2008-2020	5.93%	174,339	186,355
Spring Meadow Resources	2008-2020	5.93%	259,067	276,922
Residential Support Services	2008-2020	5.93%	196,272	209,803
Western Montana Mental Health	2009-2014	1.73%	50,129	63,259
Mineral Community Hospital	2009-2014	3.00%	25,661	31,745
Eastern MT Community Mental Health Ctr.	2009-2014	3.00%	30,831	37,943
Opportunity Resources, Inc.	2009-2014	3.00%	115,725	0
Marias Medical Center	2010-2015	3.00%	180,447	0
Eastern MT Community Mental Health Ctr.	2010-2015	3.00%	113,266	0
Total Revenue Notes Receivable			**$1,529,534**	**$1,441,082**

5. Employee Benefit Plans

The Authority participates in the Public Employees' Retirement System (PERS), a cost sharing, multiple employer, defined benefit pension plan which covers all employees. The plan is established under State law and is administered by the State of Montana. The plan provides retirement, disability and death benefits to plan members and beneficiaries.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

The plan issues publicly available annual reports that include financial statements and required supplemental information for the plans. Those reports may be obtained from:

Public Employees Retirement Division
PO Box 200131
100 South Park, Suite 220
Helena, MT 59620-0131
406-444-3154

The Authority and its employees were each required to contribute 7.035 percent and 6.9 percent of annual compensation respectively for both fiscal years 2010 and 2009.

The Authority's PERS contributions were $10,796 and $10,117 in fiscal years 2010 and 2009, respectively.

Deferred Compensation Plan

The Authority's permanent employees are eligible to participate in the State of Montana's deferred compensation plan. The compensation deferred is not available to employees until separation from State service, retirement, death, or upon an unforeseeable emergency, when still employed and meeting IRS specified criteria. The plan is governed by Internal
Revenue Service Code (IRC) Section 457 and Title 19, chapter 50, Montana Code Annotated (MCA). The Small Business Job Protection Act of 1996 resulted in changes to IRC Section 457 and Title 19, chapter 50, MCA. Assets of the deferred compensation plan are required to be held in trust, custodial accounts or insurance company contracts for the exclusive benefit of participants and their beneficiaries.

6. Net Assets

Capital Reserve Accounts

Net Assets	Funded 2010	Requirement 2010	Funded 2009	Requirement 2009
Capital Reserve Account A	$ 957,831	$10,111,968	$ 862,189	$10,954,502
Capital Reserve Account B	122,588	874,204	112,479	682,169
Direct Loan Program	1,754,708	1,754,708	1,685,178	1,685,178
Working Capital Fund	915,056	915,056	818,164	818,164
Total	$3,750,183	$13,655,936	$3,478,010	$14,140,013

The Montana Legislature approved the creation of Capital Reserve Accounts in section 90-7-317, MCA, as security for the payment of loans in connection with certain bonds or loans issued by the Authority. The Capital Reserve Account A is security that applies to all bonds issued under the Master Loan Program (13 series of bonds), one Stand Alone bond issue for the Montana Developmental Center, and surety bonds issued for Prerelease Revenue Bonds (9 series of bonds). These bonds and loans are enhanced by the BOI through the BOI's contract with the Authority to replenish the debt service reserve fund if necessary. The Authority designates certain funds equal to 10% of the par amount of the enhancements provided by the BOI to be deposited to Capital Reserve Account A. Therefore the Authority has designated a certain portion of the Total Net Assets for loan repayments to the BOI, upon demand, under the Capital Reserve Agreements. The table below shows enhancements provided by the BOI, the Capital Reserve Account requirement and the amount of the Capital Reserve Account requirement that was funded.

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

	BOI Enhancements	Capital Reserve Account Requirement	Capital Reserve Account Funded
2010	101,119,677	10,111,968	957,831
2009	109,545,022	10,954,502	862,189

Effective July 1, 1999, the Montana Legislature required the BOI to allow the Authority to make loans totaling up to $15,000,000 of the Permanent Coal Tax Trust Fund for capital projects in section 17-6-308, MCA. Until the Authority makes a loan pursuant to Title 90, Chapter 7, MCA, the funds under its administration must be invested by the BOI. The BOI and the Authority calculate the interest rate on each loan. Three new loans were originated under this program during fiscal years 2010 and two in 2009. The Authority has issued a total of 18 loans under this authority, twelve of which are currently outstanding. The outstanding loan amount of approximately $8,742,035 as of June 30, 2010 and $6,821,687 as of June 30, 2009 is reported as investments in the financial statements of the BOI. The Authority designates certain funds up to 10% of the par amount of outstanding loans made from this program as a loan repayment, in the event of a borrower default, in the Capital Reserve Account B. These funds are represented in the Total Net Assets as Capital Reserve Account B. As of June 30, 2010, the total Capital Reserve Account B requirement was $874,204 and was funded at $122,588. As of June 30, 2009, the total Capital Reserve Account B requirement was $682,169 and was funded at $112,479.

Direct Loan Program

The Legislature authorized the Authority to create and fund a revolving Direct Loan Program that provides short-term loans to its non-investment grade clients to finance small capital projects. The Authority has designated a certain portion of the Total Net Assets for this revolving loan program. Deposits to the Direct Loan Program include applicable loan repayments, annual fees, and investment earnings. On June 30, 2010 the funding requirement for the program was $1,754,708, had loans outstanding of $1,529,535 leaving $225,173 available for additional loans. As of June 30, 2009 the funding requirement for the program was $1,685,178, had loans outstanding of $1,441,082 leaving $244,096 available for additional loans.

Working Capital Fund

The Authority has designated a working capital fund equal to twice its annual budget. For fiscal years 2010 and 2009 the fund requirement equaled $915,056 and $818,164, respectively and were fully funded. These funds are part of the Total Net Assets balance.

7. Subsequent Events

On August 11, 2010 two bond issues totaling $17,855,000 were closed for Powell Community Memorial Hospital. Proceeds will be used to construct a replacement hospital in Deer Lodge.

On October 28, 2010 two series of bonds totaling $$33,080,000 were issued for Barrett Hospital Development Corporation. Proceeds were used to finance the construction of a new hospital in Dillon.