

In the opinion of Sidley Austin LLP, San Francisco, California ("Bond Counsel"), under existing statutes, regulations, rulings and judicial decisions and assuming compliance with certain covenants in the documents pertaining to the Bonds and certain requirements of the Internal Revenue Code of 1986, as amended (the "Code"), as described herein, interest on the Bonds is not includable in gross income of the owners of the Bonds for federal income tax purposes. In the further opinion of Bond Counsel, interest on the Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability. In the further opinion of Bond Counsel, interest on the Bonds is exempt from personal income taxes imposed by the State of California. See "TAX MATTERS" herein.

\$60,100,000
ABAG FINANCE AUTHORITY FOR NONPROFIT CORPORATIONS
REFUNDING REVENUE BONDS
(CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND)
SERIES 2007A

Dated Date: Date of Delivery

Due: December 1, as shown on inside cover

The ABAG Finance Authority for Nonprofit Corporations (the "Authority") will issue its Refunding Revenue Bonds (Children's Hospital & Research Center at Oakland) Series 2007A (the "Bonds"), which will be secured under the provisions of a Bond Indenture dated as of October 1, 2007 (the "Bond Indenture"), between the Authority and The Bank of New York Trust Company, N.A. (the "Trustee"), and a Loan Agreement dated as of October 1, 2007 (the "Loan Agreement"), between the Authority and Children's Hospital & Research Center at Oakland (the "Corporation"), as described herein. The Bonds are limited obligations of the Authority and will be payable from Loan Repayments made by the Corporation under the Loan Agreement and from certain funds held under the Bond Indenture. The obligation of the Corporation to make such payments is evidenced and secured by Obligation No. 1 issued under the Master Indenture, described herein, under which the Corporation and Children's Hospital & Research Center Foundation (together, the "Obligated Group") jointly and severally are obligated to pay the principal of, premium, if any, and interest on the Bonds, when due.

Interest on the Bonds will accrue from their date of delivery and will be payable on each June 1 and December 1, commencing December 1, 2007. The Bonds will be offered at the prices or yields, and will bear interest at the rates and mature on December 1 in the years and in the principal amounts set forth on the inside cover page.

The Bonds will be subject to optional, special and mandatory redemption prior to maturity and to mandatory purchase in lieu of redemption in certain circumstances, all as described herein.

The Bonds will be delivered in fully registered form in denominations of \$5,000 or any integral multiple thereof and, when delivered, will be registered in the name of Cede & Co., as nominee for The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the Bonds. Individual purchases of beneficial interests in the Bonds will be made in book-entry form (without bond certificates). For so long as DTC or its nominee, Cede & Co., is the registered Holder of the Bonds, payments of the principal of, premium, if any, and interest on the Bonds will be made directly to Cede & Co. for payment to its participants for subsequent disbursement to the beneficial owners. See APPENDIX F – "BOOK-ENTRY ONLY SYSTEM."

THE BONDS ARE SPECIAL LIMITED OBLIGATIONS OF THE AUTHORITY, PAYABLE SOLELY FROM AND SECURED BY THE REVENUES PLEDGED THEREFOR PURSUANT TO THE BOND INDENTURE AND OBLIGATION NO. 1. NEITHER THE AUTHORITY, THE ASSOCIATION OF BAY AREA GOVERNMENTS ("ABAG"), NOR THE MEMBERS OF THE AUTHORITY OR ABAG SHALL BE DIRECTLY OR INDIRECTLY OR CONTINGENTLY OR MORALLY OBLIGATED TO USE ANY OTHER MONEYS OR ASSETS OF THE AUTHORITY, ABAG OR ANY OF THEIR MEMBERS TO PAY ALL OR ANY PORTION OF DEBT SERVICE DUE ON THE BONDS. THE BONDS AND THE OBLIGATION TO PAY PRINCIPAL OF, PREMIUM, IF ANY, AND INTEREST THEREON, DO NOT CONSTITUTE AN INDEBTEDNESS OR AN OBLIGATION OF THE AUTHORITY OR ABAG, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF, WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION, OR A CHARGE AGAINST THE GENERAL CREDIT OR TAXING POWERS OF ANY OF THEM, BUT SHALL BE PAYABLE SOLELY FROM THE REVENUES DESCRIBED HEREIN. NO OWNER OF THE BONDS SHALL HAVE THE RIGHT TO COMPEL THE EXERCISE OF THE TAXING POWER OF THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF TO PAY ANY PRINCIPAL OF, PREMIUM, IF ANY, OR INTEREST ON THE BONDS. NEITHER THE AUTHORITY NOR ABAG HAS ANY TAXING POWER.

This cover page contains certain information for quick reference only. It is not intended to be a summary of the security or terms of this bond issue. Investors are instructed to read the entire Official Statement to obtain information essential to the making of an informed investment decision.

The Bonds are offered when, as and if received by the Underwriter, subject to prior sale, to withdrawal or modification of the offer without notice, and to the approval of legality by Sidley Austin LLP, San Francisco, Bond Counsel, the approval of certain matters for the Authority by its counsel Jones Hall, A Professional Law Corporation, and the approval of certain matters for the Obligated Group by its counsel, Hanson, Bridgett, Marcus, Vlahos & Rudy, LLP, San Francisco. Certain legal matters will be passed upon for the Underwriter by Holland & Knight LLP, San Francisco. It is expected that the Bonds in book-entry form will be available for delivery through the facilities of DTC on or about October 16, 2007.

Merrill Lynch & Co.

Date: October 4, 2007

MATURITY SCHEDULE

\$60,100,000

**ABAG FINANCE AUTHORITY FOR NONPROFIT CORPORATIONS
REFUNDING REVENUE BONDS
(CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND)
SERIES 2007 A**

<u>Due December 1</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP⁽¹⁾</u>
2010	\$1,085,000	4.00%	3.61%	00037CLY4
2011	1,130,000	4.00	3.75	00037CLZ1
2012	1,175,000	4.25	3.88	00037CMA5
2013	1,220,000	4.50	4.00	00037CMB3
2014	1,275,000	4.50	4.11	00037CMC1
2015	1,335,000	4.50	4.24	00037CMD9
2016	1,395,000	4.25	4.34	00037CME7
2017	1,455,000	4.75	4.43	00037CMF4
2018	1,525,000	4.50	4.54	00037CMG2
2019	1,590,000	4.50	4.63	00037CMH0

\$5,235,000 4.75% Term Bonds Due December 1, 2022, priced to yield 4.83%, CUSIP⁽¹⁾ 00037CMJ6
\$10,615,000 5.25% Term Bonds Due December 1, 2027, priced to yield 4.90%⁽²⁾, CUSIP⁽¹⁾ 00037CMK3
\$31,065,000 5.00% Term Bonds Due December 1, 2037, priced to yield 5.06%, CUSIP⁽¹⁾ 00037CML1

⁽¹⁾ Copyright 2007, American Bankers Association. CUSIP® is a registered trademark of the American Bankers Association. CUSIP data herein are provided by Standard & Poor's, CUSIP Service Bureau, a division of The McGraw-Hill Companies, Inc. CUSIP numbers have been assigned by an independent company not affiliated with the Authority and are included solely for the convenience of the holders of the Bonds. The Authority is not responsible for the selection or uses of these CUSIP numbers, and no representation is made as to their correctness on the Bonds or as indicated above. The CUSIP number for a specific maturity is subject to being changed after the issuance of the Bonds as a result of various subsequent actions including, but not limited to, a refunding in whole or in part of such maturity or as a result of the procurement of secondary market portfolio insurance or other similar enhancement by investors that is applicable to all or a portion of certain maturities of the Bonds.

⁽²⁾ Priced to the first par call. See "THE BONDS - Redemption - *Optimal Redemption*."

TABLE OF CONTENTS

	Page
INTRODUCTION	1
Purpose of this Official Statement.....	1
The Obligated Group and the Affiliated Entities.....	1
Plan of Finance.....	2
Security for the Bonds.....	2
Bondholders' Risks	3
Continuing Disclosure.....	3
Availability of Documents	4
PLAN OF FINANCE	4
Use of Proceeds.....	4
Refunded Securities.....	4
ESTIMATED SOURCES AND USES	5
THE AUTHORITY	5
DEBT SERVICE REQUIREMENTS	7
THE OBLIGATED GROUP	8
General	8
Outstanding Indebtedness.....	8
Interest Rate Agreements	9
THE BONDS.....	9
General	9
Redemption	10
SECURITY FOR THE BONDS.....	13
General	13
Limited Obligation of the Authority.....	13
Bond Reserve Fund.....	14
The Master Indenture	14
Limitations on Enforceability.....	16
BONDHOLDERS' RISKS.....	18
General	18
Significant Risk Areas Highlighted.....	18
Patient Service Revenues	21
Investments and Contributions.....	24
Limitations on Revenues for Research Programs.....	25
Nonprofit Health Care Environment	36
Regulatory Environment	38
Business Relationships and Other Business Matters.....	32
Tax-Exempt Status and Other Tax Matters.....	36
Interest Rate Swap and Other Hedge Risks.....	38
Secondary Market	38
Other Risk Factors.....	38
VERIFICATION OF MATHEMATICAL COMPUTATIONS.....	39
ABSENCE OF MATERIAL LITIGATION.....	39
The Authority	39
The Obligated Group.....	40

CONTINUING DISCLOSURE.....	40
RELATIONSHIPS AMONG PARTIES	40
TAX MATTERS	41
General	41
Backup Withholding	42
Premium Bonds	42
Discount Bonds	42
APPROVAL OF LEGALITY	43
UNDERWRITING	43
INDEPENDENT ACCOUNTANTS.....	43
RATING.....	43
MISCELLANEOUS.....	44
APPENDIX A	INFORMATION CONCERNING THE OBLIGATED GROUP
APPENDIX B	AUDITED CONSOLIDATED FINANCIAL STATEMENTS FOR FISCAL YEARS ENDED DECEMBER 31, 2006 AND 2005
APPENDIX C	SUMMARY OF PRINCIPAL DOCUMENTS
APPENDIX D	FORM OF OPINION OF BOND COUNSEL
APPENDIX E	FORM OF CONTINUING DISCLOSURE AGREEMENT
APPENDIX F	BOOK-ENTRY ONLY SYSTEM

OFFICIAL STATEMENT

\$60,100,000
ABAG FINANCE AUTHORITY FOR NONPROFIT CORPORATIONS
REFUNDING REVENUE BONDS
(CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND)
SERIES 2007A

INTRODUCTION

The following introductory statement is subject in all respects to the more complete information set forth in this Official Statement. The descriptions and summaries of various documents hereinafter set forth do not purport to be comprehensive or definitive and are qualified in their entirety by reference to each document. All capitalized terms used in this Official Statement and not otherwise defined herein or in APPENDIX C have the same meaning as in the Master Indenture or the Bond Indenture (each as defined below). See APPENDIX C - "SUMMARY OF PRINCIPAL DOCUMENTS."

Purpose of this Official Statement

This Official Statement is provided to furnish information in connection with the offering of the ABAG Finance Authority for Nonprofit Corporations Refunding Revenue Bonds (Children's Hospital & Research Center at Oakland), Series 2007A (the "Bonds"), in an aggregate principal amount of \$60,100,000. The Bonds will be issued pursuant to and secured by a Bond Indenture, dated as of October 1, 2007 (the "Bond Indenture"), between the ABAG Finance Authority for Nonprofit Corporations (the "Authority") and The Bank of New York Trust Company, N.A., as trustee (the "Trustee"). The Authority will lend the proceeds of the Bonds to Children's Hospital & Research Center at Oakland (the "Corporation"), which loan will be evidenced by a Loan Agreement, dated as of October 1, 2007 (the "Loan Agreement"), between the Authority and the Corporation. Under the Loan Agreement, the Corporation is required to make Loan Repayments sufficient to pay the principal of, premium, if any, and interest on the Bonds ("Debt Service"), when due. Under Obligation No. 1 issued under a Master Indenture (both described below), the Corporation and Children's Hospital & Research Center Foundation (the "Foundation") are jointly and severally obligated to make payments in an amount sufficient to pay Debt Service on the Bonds when due.

The Obligated Group and the Affiliated Entities

The Corporation is a California nonprofit public benefit corporation and is exempt from federal income taxation as an organization described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the "Code"). The Corporation owns and operates Children's Hospital & Research Center, a pediatric acute care hospital licensed for 170 beds and located in Oakland, California (the "Hospital"). In addition, the Corporation is licensed to operate and operates 20 beds that it leases from Alta Bates Summit Medical Center located in Oakland, California. The Foundation is a California nonprofit public benefit corporation and is exempt from federal income taxation as an organization described in Section 501(c)(3) of the Code. The Foundation engages in various fundraising activities on behalf of the Corporation. The Corporation and the Foundation collectively are referred to herein as the "Obligated Group" or "Members" of the Obligated Group, and each individually is sometimes referred to herein as a "Member." After issuance of the Bonds, the Obligated Group will have \$60,100,000 of long-term debt outstanding, consisting of the Bonds, and the Corporation, on its own, will have an additional \$30,000,000 of long-term debt outstanding, consisting of the 2005 Bonds. See "THE OBLIGATED GROUP—Outstanding Indebtedness" herein.

The Corporation is also affiliated with BayChildren's Physicians ("BCP"), Children First Healthcare Network, Inc. ("CFHN") and Children's Hospital Oakland Family House, Inc. ("Family House" and together with BCP and CFHN, the "Affiliated Entities"). None of the Affiliated Entities is a Member of the Obligated Group.

The Members of the Obligated Group are the sole obligors with respect to the Bonds. No Affiliated Entity is obligated to pay Debt Service on the Bonds.

The Corporation and the Foundation comprise the initial members of the Obligated Group formed under that certain Master Indenture of Trust, to be executed concurrently with the issuance of the Bonds and dated as of October 1, 2007 (the “Master Indenture”), among the Corporation, the Foundation and The Bank of New York Trust Company, N.A., as master trustee (the “Master Trustee”). The Master Indenture will provide that additional entities may become Members of the Obligated Group upon satisfying certain financial tests and meeting certain other conditions. See APPENDIX C – “SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE.”

See APPENDIX A—“INFORMATION CONCERNING THE OBLIGATED GROUP” for additional information about the Obligated Group, including its history, organization, and certain operating, utilization and financial information. The consolidated audited financial statements of the Obligated Group, CFHN and Family House for the years ended December 31, 2006 and 2005 are included as APPENDIX B. Management of the Corporation indicates that the net patient service revenue, the excess of revenues, gains and other support over expenses, and the total net assets of CFHN and Family House are not material to the financial performance of the Obligated Group. The consolidated audited financial statements of the Obligated Group, CFHN and Family House included as APPENDIX B, the consolidated audited financial data presented in Appendix A for the fiscal years ended December 31, 2004, 2005 and 2006 and the unaudited consolidated financial data for the five-month periods ended May 31, 2006 and 2007 presented in APPENDIX A also reflect the results of BCP. As of January 1, 2007, BCP commenced operations as a legal entity separate from the Corporation. For the fiscal years ended December 31, 2004, 2005 and 2006, the operations attributable to BCP generated approximately 4.28%, 5.05% and 5.35%, respectively, of the net patient service revenue of the Corporation, on a consolidated basis.

Plan of Finance

Proceeds from the sale of the Bonds will be loaned to the Corporation pursuant to the Loan Agreement and will be used to prepay in advance of maturity and defease certain outstanding certificates of participation previously executed and delivered for the benefit of the Obligated Group, fund a Bond Reserve Fund for the Bonds, and pay certain costs related to the issuance of the Bonds. See “PLAN OF FINANCE” herein.

To secure its obligations under the Loan Agreement to pay the Debt Service on the Bonds, the Corporation, as Obligated Group Representative, will issue Obligation No. 1 under the Master indenture to the Master Trustee.

Security for the Bonds

The Bonds are limited obligations of the Authority and will be payable solely from payments made by the Corporation under the Loan Agreement (the “Loan Repayments”), from payments made by the Obligated Group on Obligation No. 1 and from certain funds held by the Trustee under the Bond Indenture. Pursuant to the Loan Agreement, the Corporation is required to make payments in an amount sufficient to pay in full, when due, the Debt Service on the Bonds. See “SECURITY FOR THE BONDS” herein.

In order to evidence and secure the obligation of the Corporation to make payments under the Loan Agreement sufficient to pay the Debt Service on the Bonds, the Corporation will deliver to the Trustee its Obligation No. 1 (“Obligation No.1”), dated the date of issuance of the Bonds, which will be issued pursuant to the Master Indenture, as supplemented and amended by the First Supplemental Master Indenture of Trust, dated as of October 1, 2007 (“Supplement No. 1”). Pursuant to Obligation No. 1, the Obligated Group jointly and severally agrees to make payments in an amount sufficient to pay, when due, the Debt Service on the Bonds. Obligation No. 1 will entitle the Trustee, as the holder thereof, to the benefit of the covenants, restrictions and other obligations imposed upon the Obligated Group under the Master Indenture.

The Master Indenture, as supplemented by Supplement No. 1 and as further supplemented from time to time, is hereinafter referred to collectively as the “Master Indenture.”

For a description of the Master Indenture and Supplement No. 1, see “SECURITY FOR THE BONDS—The Master Indenture” herein. See APPENDIX C—“SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE” for additional information regarding the Master Indenture and Obligation No. 1.

Except for the security interest granted to the Master Trustee by the Obligated Group in Collateral, which includes Gross Revenues and a deed of trust and is described below under “SECURITY FOR THE BONDS—The Master Indenture – Security Interest in Collateral,” the Bonds are not secured by any additional mortgage of, or security interest in, any real or personal property of the Corporation or the Foundation.

Upon issuance of the Bonds, the Bond Reserve Fund will be funded in an amount equal to the Bond Reserve Requirement. The Trustee is required to use moneys on deposit in the Bond Reserve Fund whenever moneys on deposit with the Interest Fund, the Principal Fund or the Sinking Fund, as appropriate, under the Bond Indenture are insufficient to pay in full the Debt Service on the Bonds, when due. See “SECURITY FOR THE BONDS—Bond Reserve Fund” herein and APPENDIX C—“SUMMARY OF PRINCIPAL DOCUMENTS—BOND INDENTURE—Bond Reserve Fund.”

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Bondholders’ Risks

There are risks associated with the purchase of the Bonds. See “BONDHOLDERS’ RISKS” herein for a discussion of certain of those risks.

Continuing Disclosure

The Corporation, on behalf of itself, the Foundation and any future Members of the Obligated Group, will enter into a Continuing Disclosure Agreement, dated as of October 1, 2007 (the “Continuing Disclosure Agreement”) for the benefit of the holders of the Bonds to provide certain information annually and quarterly and to provide notice of certain events to certain information repositories pursuant to the requirements of Rule 15c2-12 (the “Rule”) adopted by the Securities and Exchange Commission. See “CONTINUING DISCLOSURE” herein. A form of the Continuing Disclosure Agreement is set forth in APPENDIX E hereto.

Failure by the Corporation to comply with the Continuing Disclosure Agreement will not constitute an event of default under the Master Indenture, the Loan Agreement or the Bond Indenture, and holders of the Bonds are limited to the remedies described in the Continuing Disclosure Agreement. See APPENDIX E hereto for a form of the Continuing Disclosure Agreement. Failure by the Corporation to comply with the Continuing Disclosure Agreement must be reported in accordance with the Rule and must be considered by any broker, dealer or municipal securities dealer before recommending the purchase or sale of the Bonds in the secondary market. Consequently, any such failure may adversely affect the transferability and liquidity of the Bonds and their market price.

The Authority is not a party to, and has no responsibility under, the Continuing Disclosure Agreement and has no obligation to provide any information with respect to the Bonds under the Rule

Availability of Documents

The descriptions and summaries of various documents set forth in this Official Statement do not purport to be conclusive or definitive and reference is made to each such document for the complete details of all terms and conditions hereof. Further descriptions of the Master Indenture, the Bond Indenture and the Loan Agreement are set forth in APPENDIX C hereto. All references herein to the Bonds, Obligation No. 1, Supplement No. 1, the Swap Obligation, the Master Indenture, the Continuing Disclosure Agreement, the Bond Indenture and the Loan Agreement are qualified in their entirety by such documents, copies of which, are available from the Underwriter prior to the issuance of the Bonds, and thereafter may be examined or obtained at the expense of the person requesting the same at the designated corporate trust office of the Trustee in Los Angeles, California. Information relating to The Depository Trust Company (“DTC”) and the book-entry only system has been furnished by DTC.

PLAN OF FINANCE

Use of Proceeds

The proceeds of the Bonds will be used to: (i) advance prepay the outstanding balance of the Authority’s Insured Certificates of Participation, Series 1999, \$60,000,000 of which is currently outstanding (the “Refunded Securities”); (ii) fund the Bond Reserve Fund; and (iii) pay the costs of issuance of the Bonds. See “ESTIMATED SOURCES AND USES OF FUNDS” below.

Refunded Securities

To prepay the Refunded Securities, a portion of the proceeds of the Bonds will be deposited with The Bank of New York Trust Company, N.A., as escrow trustee (the “Escrow Agent”), under the Escrow Agreement, dated as of October 16, 2007 (the “Escrow Agreement”), between the Corporation and the Escrow Agent. Such proceeds will be used to purchase non-callable direct obligations of, or obligations that the principal of and interest on are unconditionally guaranteed by, the United States of America (the “Escrow Securities”), to be irrevocably deposited in trust for the benefit of the Holders of the Refunded Securities. The Escrow Securities will mature at such times and in such amounts and will bear interest payable at such times and in such amounts, together with any available cash in the escrow fund, such that sufficient moneys will be available in the escrow fund to provide for the payment of the debt service due with respect to the outstanding Refunded Securities on and before December 1, 2009, and the prepayment price of the Refunded Securities maturing on and after December 1, 2009, on December 1, 2009, which is the first optional prepayment date for such Refunded Securities, plus accrued interest, if any. Upon such irrevocable deposit, the Refunded Securities will be deemed paid and no longer outstanding. Neither the maturing principal of the Escrow Securities nor the interest income thereon will be available to make payments on the Bonds. The deposit of moneys and Escrow Securities into the escrow fund will constitute an irrevocable deposit for the benefit of the holders of the Refunded Securities. See “VERIFICATION OF MATHEMATICAL COMPUTATIONS” herein.

The Refunded Securities consist of the following:

ABAG Finance Authority for Nonprofit Corporations Insured Certificates of Participation, Series 1999

<u>Maturity</u>	<u>Par Amount</u>	<u>Interest Rate</u>	<u>CUSIP</u>
12/1/2010	\$1,635,000	6.000%	00037EGQ3
12/1/2015	9,780,000	6.000%	00037EGR1
12/1/2019	10,140,000	5.875%	00037EGS9
12/1/2029	38,445,000	6.000%	00037EGT7

Defeasance of the 1988 Bonds and the 1994 Bonds

Concurrently with the issuance of the Bonds, the Corporation expects to use its own funds to defease the outstanding balance of (i) the City of Oakland, California, Weekly Adjustable/Fixed Rate Health Facility Revenue Bonds (Children’s Hospital Medical Center of Northern California), 1988 Series A (the “1988 Bonds”), currently outstanding in the aggregate principal amount of \$2,355,000, and (ii) the City of Oakland, California, Insured Refunding Revenue Bonds (Children’s Hospital Medical Center of Northern California), 1994 Series A (the “1994 Bonds”), currently outstanding in the aggregate principal amount of \$3,790,000. Upon such defeasance, the 1988 Bonds and the 1994 Bonds will be deemed paid and no longer outstanding. In connection with such defeasance, the Corporation expects to terminate certain interest rate swap transactions currently in place with respect to the 1988 Bonds and the 1994 Bonds.

ESTIMATED SOURCES AND USES

The following table sets forth the sources and uses of proceeds of the Bonds:

Sources of Funds

Principal Amount of the Bonds	\$60,100,000.00
Net Original Issue Premium	93,038.95
Funds Held in Connection with the Refunded Securities	9,242,404.07
TOTAL SOURCES	<u>\$69,435,443.02</u>

Uses of Funds

Deposit to defeasance escrow for Refunded Securities	\$64,278,377.01
Deposit to Bond Reserve Fund	4,025,262.50
Issuance Costs ⁽¹⁾	1,131,803.51
TOTAL USES	<u>\$69,435,443.02</u>

⁽¹⁾ Includes Underwriter’s discount, certain legal fees, printing costs, rating agency fees and miscellaneous expenses of issuance.

THE AUTHORITY

The ABAG Finance Authority for Nonprofit Corporations is duly organized and existing under the laws of the State of California (the “State”). The Authority was formed pursuant to the terms of a Joint Powers Agreement, dated as of April 1, 1990, as amended as of September 18, 1990 and June 9, 1992 (the “Joint Powers Agreement”), and the Joint Exercise of Powers Law of the State (constituting Chapter 5, commencing with Section 6500, of Division 7 of Title 1 of the California Government Code) (the “Act”), in order to assist nonprofit corporations and other entities to obtain financing for projects located within the several jurisdictions of Authority members with purposes serving the public interest.

THE BONDS ARE SPECIAL LIMITED OBLIGATIONS OF THE AUTHORITY, PAYABLE SOLELY FROM AND SECURED BY THE REVENUES PLEDGED THEREFOR PURSUANT TO THE BOND INDENTURE AND OBLIGATION NO. 1. NEITHER THE AUTHORITY, THE ASSOCIATION OF BAY AREA GOVERNMENTS (“ABAG”), NOR THE MEMBERS OF THE AUTHORITY OR ABAG SHALL BE DIRECTLY OR INDIRECTLY OR CONTINGENTLY OR MORALLY OBLIGATED TO USE ANY OTHER MONEYS OR ASSETS OF THE AUTHORITY, ABAG OR ANY OF THEIR MEMBERS TO PAY ALL OR ANY PORTION OF DEBT SERVICE DUE ON THE BONDS. THE BONDS AND THE OBLIGATION TO PAY PRINCIPAL OF, PREMIUM, IF ANY, AND INTEREST THEREON, DO NOT CONSTITUTE AN INDEBTEDNESS OR AN OBLIGATION OF THE AUTHORITY OR ABAG, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF, WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION, OR A CHARGE AGAINST THE GENERAL CREDIT OR TAXING POWERS OF ANY OF THEM, BUT SHALL BE PAYABLE SOLELY FROM THE REVENUES DESCRIBED

HEREIN. NO OWNER OF THE BONDS SHALL HAVE THE RIGHT TO COMPEL THE EXERCISE OF THE TAXING POWER OF THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF TO PAY ANY PRINCIPAL OF, PREMIUM, IF ANY, OR INTEREST ON THE BONDS. NEITHER THE AUTHORITY NOR ABAG HAS ANY TAXING POWER.

DEBT SERVICE REQUIREMENTS

The following table sets forth, for each fiscal year of the Obligated Group (currently ending December 31), the amounts required for payment of principal of, whether at maturity or by mandatory redemption, and interest on, all long-term indebtedness of Members of the Obligated Group after issuance of the Bonds, which will consist of the Bonds and the 2005 Bonds.

Fiscal Year Ending December 31,	The Bonds		The 2005 Bonds*		Total Debt Service
	Principal	Interest	Principal	Interest	
2007	-	\$367,332	-	\$62,875	\$430,207
2008	-	2,938,662	-	1,509,000	4,447,662
2009	-	2,938,662	-	1,509,000	4,447,662
2010	\$1,085,000	2,938,662	\$440,000	1,497,934	5,961,596
2011	1,130,000	2,895,262	460,000	1,475,299	5,960,561
2012	1,175,000	2,850,062	485,000	1,451,532	5,961,594
2013	1,220,000	2,800,125	510,000	1,426,508	5,956,633
2014	1,275,000	2,745,225	535,000	1,400,226	5,955,451
2015	1,335,000	2,687,850	565,000	1,372,561	5,960,411
2016	1,395,000	2,627,775	595,000	1,343,387	5,961,162
2017	1,455,000	2,568,487	625,000	1,312,704	5,961,191
2018	1,525,000	2,499,375	655,000	1,280,512	5,959,887
2019	1,590,000	2,430,750	690,000	1,246,686	5,957,436
2020	1,665,000	2,359,200	725,000	1,211,098	5,960,298
2021	1,745,000	2,280,112	765,000	1,173,625	5,963,737
2022	1,825,000	2,197,225	805,000	1,134,139	5,961,364
2023	1,910,000	2,110,537	845,000	1,092,642	5,958,179
2024	2,010,000	2,010,262	890,000	1,049,007	5,959,269
2025	2,120,000	1,904,737	935,000	1,003,108	5,962,845
2026	2,230,000	1,793,437	985,000	954,820	5,963,257
2027	2,345,000	1,676,362	1,035,000	904,017	5,960,379
2028	2,470,000	1,553,250	1,085,000	850,699	5,958,949
2029	2,595,000	1,429,750	1,145,000	794,614	5,964,364
2030	2,725,000	1,300,000	1,200,000	735,638	5,960,638
2031	2,860,000	1,163,750	1,265,000	673,643	5,962,393
2032	3,000,000	1,020,750	1,330,000	608,379	5,959,129
2033	3,150,000	870,750	1,395,000	539,845	5,955,595
2034	3,310,000	713,250	1,470,000	467,790	5,961,040
2035	3,475,000	547,750	1,545,000	391,963	5,959,713
2036	3,650,000	374,000	1,625,000	312,237	5,961,237
2037	3,830,000	191,500	1,710,000	228,362	5,959,862
2038	-	-	1,795,000	140,211	1,935,211
2039	-	-	1,890,000	47,534	1,937,534
	\$60,100,000	\$58,784,857	\$30,000,000	\$31,201,593	\$180,086,444

Note: Totals may not add due to rounding.

* In accordance with the Master Indenture, debt service on the 2005 Bonds incorporates payments under the Preexisting Swap Agreement and certain guaranty payments made to the Foundation, and is calculated assuming an interest rate of 5.03% and level annual debt service over 30 years from 2009 forward.

THE OBLIGATED GROUP

General

The Obligated Group currently includes the Corporation and the Foundation. The Corporation owns and operates the Hospital, a pediatric acute care hospital located in Oakland, California, licensed for 170 acute care beds. In addition, the Corporation is licensed to operate and operates 20 beds that it leases from Alta Bates Summit Medical Center located in Oakland, California. The Foundation engages in various fundraising activities on behalf of the Corporation. See APPENDIX A—“INFORMATION CONCERNING THE OBLIGATED GROUP” for additional information about the Obligated Group, including its history, organization and certain operating, utilization and financial information. The consolidated audited financial statements of the Obligated Group, CFHN and Family House for the years ended December 31, 2006 and 2005 are included as APPENDIX B. Management of the Corporation indicates that the net patient service revenue, the excess of revenues, gains and other support over expenses, and the total net assets of CFHN and Family House are not material to the financial performance of the Obligated Group. The consolidated audited financial statements of the Obligated Group, CFHN and Family House included as APPENDIX B, the consolidated audited financial data presented in Appendix A for the fiscal years ended December 31, 2004, 2005 and 2006 and the unaudited consolidated financial data for the five-month periods ended May 31, 2006 and 2007 presented in APPENDIX A also reflect the results of BCP. As of January 1, 2007, BCP commenced operations as a legal entity separate from the Corporation. For the fiscal years ended December 31, 2004, 2005 and 2006, the operations attributable to BCP generated approximately 4.28%, 5.05% and 5.35%, respectively, of the net patient service revenue of the Corporation, on a consolidated basis.

In conjunction with the issuance of the Bonds, the refunding of the Refunded Securities, and the defeasance of the 1988 Bonds and the 1994 Bonds, the existing master indenture of the Obligated group will be released and the Obligated Group will execute the Master Indenture.

Pursuant to the Master Indenture, neither the Corporation nor the Foundation may withdraw from the Obligated Group, but certain other persons may enter into and thereafter withdraw from the Obligated Group, if certain conditions and financial tests are satisfied, as described in APPENDIX C — “SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE—Covenants of the Members—Withdrawal From Obligated Group.”

Outstanding Indebtedness

As Obligated Group Representative, the Corporation will issue Obligation No. 1 pursuant to the Master Indenture to secure payment of the Debt Service on the Bonds, when due. The Corporation is also required under the Loan Agreement to pay to the Trustee money sufficient to pay in the Debt Service on the Bonds, when due. See “SECURITY FOR THE BONDS—General” and “—The Master Indenture” herein.

On or before the delivery of the Bonds, the Corporation will provide funds for the defeasance of the 1988 Bonds and the 1994 Bonds. Upon issuance of the Bonds, the 1988 Bonds and the 1994 Bonds will no longer be deemed outstanding under the terms of the respective bond indentures pursuant to which such bonds were issued.

After issuance of the Bonds, the Obligated Group will have long-term indebtedness outstanding in the aggregate principal amount of \$60,100,000, which consists solely of its payment obligations with respect to the Bonds. In addition, after issuance of the Bonds, the Corporation will have long-term indebtedness outstanding in the aggregate principal amount of \$30,000,000, which consists solely of its payment obligations with respect to the ABAG Finance Authority for Nonprofit Corporations Revenue Bonds (Children’s Hospital & Research Center at Oakland) Series 2005 (the “2005 Bonds”). The Corporation’s payment obligations with respect to the 2005 Bonds will not be secured under the Master Indenture.

Interest Rate Agreements

The following describes the Obligated Group's Preexisting Swap Transaction that will remain outstanding after the issuance of the Bonds.

In conjunction with the execution of the Master Indenture, the Obligated Group and MLCS will amend and restate that certain existing interest rate swap transaction pursuant to which MLCS has agreed to pay the Obligated Group fixed amounts based on a fixed rate of 3.56% per annum and the Obligated Group has agreed to pay MLCS floating amounts based on a floating rate equal to the BMA Municipal Swap Index (now known as the SIFMA Municipal Swap Index), in each case based on a notional amount of \$30,000,000 (the "Preexisting Swap Agreement"). The Preexisting Swap Agreement will terminate pursuant to its terms on June 1, 2009.

The Preexisting Swap Agreement does not alter or affect any of the obligations of the Obligated Group with respect to the payment of Debt Service on the Bonds. MLCS has no obligation to make any payments with respect to the Debt Service on the Bonds. No persons other than the Obligated Group and MLCS will have any rights under the Preexisting Swap Agreement or against MLCS. Payments due under the Preexisting Swap Agreement will not be pledged to the payment of Debt Service on any of the Bonds.

The Preexisting Swap Agreement is subject to early termination upon the occurrence of certain specified events, including standard Termination Events and Events of Default (as defined therein). If an early termination occurs, a payment from the Obligated Group to MLCS or from MLCS to the Obligated Group may be required, and the amount of any such payment could be substantial and potentially materially adverse to the Obligated Group's financial condition. In the event of an early termination of the Preexisting Swap Agreement, there can be no assurance that (i) the Obligated Group will receive any termination payment payable to it by MLCS, (ii) the Obligated Group will have sufficient amounts to pay a termination payment payable by it to MLCS, or (iii) the Obligated Group will be able to obtain a replacement swap agreement with comparable terms. In addition, upon the occurrence of certain events, the Obligated Group may be required to collateralize its obligations under the Preexisting Swap Agreement by a deposit of cash and securities on a custodial basis. See "BONDHOLDERS' RISKS—Interest Rate Swap and Other Hedge Risk."

The Obligated Group's obligations under the Preexisting Swap Agreement will be secured by Obligation No. 2 (the "Swap Obligation") issued under the Master Indenture, which will be equally and ratably secured under the Master Indenture with all other Obligations, including Obligation No. 1. See "SECURITY FOR THE BONDS—General" and "—The Master Indenture" herein. The Swap Obligation will replace a similar obligation issued under the Obligated Group's existing master indenture, which will be released at the time of issuance of the Bonds.

THE BONDS

The following is a summary of certain provisions of the Bonds. Reference is made to the Bonds for the complete text thereof and to the Bond Indenture for all of the provisions relating to the Bonds. The discussion herein is qualified by such reference. See also APPENDIX C— "SUMMARY OF PRINCIPAL DOCUMENTS— BOND INDENTURE."

General

The Bonds will be issued only in book-entry form and, when issued, will be registered in the name of Cede & Co. or such other name as may be requested by an authorized representative of The Depository Trust Company ("DTC"), as nominee of DTC. The Bonds will be transferable and exchangeable as set forth in the Bond Indenture. DTC will act as securities depository for the Bonds. See APPENDIX F — "BOOK-ENTRY ONLY SYSTEM." So long as Cede & Co. is the registered owner of the Bonds, references herein to owners or registered owners of the Bonds shall mean Cede & Co. and will not mean the Beneficial Owners (as defined in APPENDIX E). Except as described in APPENDIX F, Beneficial Owners (as defined therein) of the Bonds will not receive or have the right to receive physical delivery of bond certificates representing their ownership interests in the Bonds. For so long as any purchaser is the Beneficial Owner of a Bond, such purchaser must maintain an account with a broker or dealer who

is or acts through a Direct Participant (as defined in APPENDIX F) to receive payment of the Debt Service on the Bonds.

The Bond Trustee will keep or cause to be kept sufficient books for the registration and transfer of the Bonds, which shall at all times (during regular business hours with prior notice at the location where such books are kept) be open to inspection by any Bondholder or his agent duly authorized in writing, the Authority or the Corporation; and, upon presentation for such purpose, the Bond Trustee shall, under such reasonable regulations as it may prescribe, register or transfer or cause to be registered or transferred, on such books, Bonds as hereinbefore provided.

So long as the Bonds are held in the book-entry system, the Debt Service on the Bonds will be paid through the facilities of DTC (or a successor securities depository). The Bonds shall be in denominations of \$5,000 or any integral multiple thereof. The principal or Redemption Price of the Bonds shall be payable in lawful money of the United States of America at the Principal Corporate Trust Office of the Bond Trustee. Payment of the interest on any Bond shall be made to the person whose name appears on the registration books of the Bond Trustee as the registered owner thereof as of the close of business on the Regular Record Date for such Interest Payment Date, except as provided in the Bond Indenture. Interest shall be paid in lawful money of the United States of America by check or draft mailed on the applicable Interest Payment Date to each Holder at the address shown on the registration books maintained by the Bond Trustee pursuant to the Bond Indenture, at the option of the Holder of at least \$1,000,000 in aggregate principal amount of the Bonds, by wire transfer to such address as may have been filed by the corresponding Record Date with the Bond Trustee for such purpose.

The Bonds shall bear interest payable on each respective Interest Payment Date; provided, however, that if, at the time of registration thereof, interest is in default on Outstanding Bonds, each such Bond shall bear interest from the Interest Payment Date to which interest has previously been paid or made available for payment of Outstanding Bonds. Any such interest not so punctually paid or duly provided for shall forthwith cease to be payable to the Bondholder on such Regular Record Date and shall be paid to the person in whose name the Bond is registered at the close of business on a Special Record Date for the payment of such defaulted interest to be fixed by the Bond Trustee, notice whereof being given to the Bondholders not less than ten days prior to such Special Record Date. The Trustee will not be required to register the transfer or exchange of (i) any Bonds during the fifteen days next preceding the date on which notice of redemption of such Bonds is given, or (ii) any Bonds that have been called for redemption. The Trustee shall require the Bondholder requesting such registration of transfer or exchange to pay any tax or other governmental charge required to be paid with respect to such registration of transfer or exchange.

The Bonds will be dated their date of delivery and will be issued in the aggregate principal amount, will mature (subject to prior redemption as described under “—Redemption” below) on the dates and will bear interest at the rates set forth on the inside cover page hereof payable on December 1, 2007 and semiannually thereafter on June 1 and December 1 of each year (each, an “Interest Payment Date”). Interest accruing on the Bonds will be computed on the basis of a 360-day year with twelve 30-day months.

Redemption

Mandatory Sinking Account Redemption. The 2022 Term Bonds, the 2027 Term Bonds and the 2037 Term Bonds are subject to redemption prior to their respective stated maturities, in part, from Mandatory Sinking Account Payments in the years and amounts set forth below, at a redemption price equal to the principal amount thereof, together with interest accrued thereon to the date fixed for redemption, without premium, as follows:

2022 Term Bonds

<u>Mandatory Sinking Account Payment Date December 1,</u>	<u>Mandatory Sinking Account Payment</u>
2020	\$1,665,000
2021	1,745,000
2022†	1,825,000

† Final Maturity.

2027 Term Bonds

<u>Mandatory Sinking Account Payment Date December 1,</u>	<u>Mandatory Sinking Account Payment</u>
2023	\$1,910,000
2024	2,010,000
2025	2,120,000
2026	2,230,000
2027†	2,345,000

† Final Maturity.

2037 Term Bonds

<u>Mandatory Sinking Account Payment Date December 1,</u>	<u>Mandatory Sinking Account Payment</u>
2028	\$2,470,000
2029	2,595,000
2030	2,725,000
2031	2,860,000
2032	3,000,000
2033	3,150,000
2034	3,310,000
2035	3,475,000
2036	3,650,000
2037†	3,830,000

† Final Maturity.

Special Redemption. The Bonds are subject to redemption prior to their respective stated maturities, at the option of the Authority (which option shall be exercised upon Request of the Corporation), in whole or in part on any date (from such maturities and in such amounts as may be specified by the Corporation, or, if the Corporation fails to designate such maturities, in inverse order of maturity and by lot within a maturity) from hazard insurance or condemnation proceeds received with respect to the facilities of any of the Members and deposited in the Special Redemption Account, at the principal amount thereof together with interest accrued thereon to the date fixed for redemption, without premium.

Optional Redemption. The Bonds maturing on or after December 1, 2018 are subject to redemption prior to their respective stated maturities, at the option of the Authority (which option shall be exercised upon request of the Corporation, delivered to the Trustee not less than forty-five days prior to the date fixed for such redemption or such shorter period as agreed to in writing by the Trustee in its sole discretion), in whole or in part on any date (and

if in part, in such amounts and from such maturities as may be specified by the Corporation or, if the Corporation fails to designate such maturities, in inverse order of maturity and within a maturity by lot) on or after December 1, 2017, at a Redemption Price equal to the principal amount of the Bonds called for redemption plus accrued interest to the date fixed for redemption, without premium.

Selection of Bonds for Redemption. Whenever provision is made in the Bond Indenture for the redemption of less than all of the Bonds, the Trustee shall select the Bonds to be redeemed from all Bonds subject to redemption or such given portion thereof not previously called for redemption, by lot in any manner which the Trustee in its sole discretion shall deem appropriate and fair.

Notice of Redemption. Notice of redemption will be mailed by the Trustee by first class mail, not more than 60 days and not fewer than 30 days prior to the redemption date to the respective Holder of each Bond subject to redemption, at the Holder's address appearing on the bond registration books of the Trustee. Failure by the Trustee to give any such notice of redemption to any one or more of the securities information services or depositories designated by the Corporation, or the insufficiency of any such notice shall not affect the sufficiency of the proceedings for redemption. Failure by the Trustee to mail any such notice of redemption to any one or more of the respective Holders of any Bonds designated for redemption shall not affect the sufficiency of the proceedings for redemption with respect to the Holders to whom such notice was mailed.

So long as the book-entry system is in effect with respect to the Bonds, the Trustee will send each notice of redemption of such Bonds to Cede & Co., as nominee of DTC, and not to the Beneficial Owners.

Rescission of Notice of Redemption. Any such notice of redemption may be rescinded by written notice given to the Trustee by the Corporation no later than five Business Days prior to the date specified for redemption. The Trustee shall give notice of such rescission as soon thereafter as practicable in the same manner, and to the same persons, as notice of such redemption was given.

Partial Redemption of Bonds. Upon surrender of any Bond redeemed in part only, the Authority shall execute and the Trustee shall authenticate and deliver to the Holder thereof, at the expense of the Corporation, a new Bond or Bonds of authorized denominations, equal in aggregate principal amount to the unredeemed portion of the Bond surrendered.

Effect of Redemption. Notice of redemption having been duly given as set forth in the Bond Indenture, and moneys for payment of the Redemption Price of, together with interest accrued to the redemption date on, the Bonds (or portions thereof) so called for redemption being held by the Trustee, on the redemption date designated in such notice, the Bonds (or portions thereof) so called for redemption shall become due and payable at the Redemption Price specified in such notice and interest accrued thereon to the redemption date, interest on the Bonds so called for redemption shall cease to accrue, said Bonds (or portions thereof) shall cease to be entitled to any benefit or security under the Bond Indenture, and the Holders of such Bonds shall have no rights in respect thereof except to receive payment of said Redemption Price and accrued interest to the date fixed for redemption from funds held by the Trustee for such payment.

Mandatory Purchase in Lieu of Redemption. Each Holder or Beneficial Owner, by purchase and acceptance of any Bond, irrevocably grants to the Corporation the option to purchase such Bond at any time such Bond is subject to optional redemption as described under “–Optional Redemption” above, at a purchase price equal to then applicable Redemption Price thereof. In the event the Corporation determines to exercise such option, the Corporation shall deliver a Favorable Opinion of Bond Counsel to the Trustee, and shall direct the Trustee: (a) to provide notice of mandatory purchase, such notice to be provided, as and to the extent applicable, in accordance with the provisions of the Bond Indenture relating to notice of redemption; and (b) to select Bonds subject to mandatory purchase in the same manner as Bonds called for redemption pursuant to the Bond Indenture. On the date fixed for purchase of any Bond in lieu of optional redemption, the Corporation shall pay the purchase price of such Bond to the Trustee in immediately available funds, and the Trustee shall pay the same to the Holders of the Bonds being purchased against delivery thereof. No purchase of any Bond in lieu of optional redemption shall operate to extinguish the indebtedness of the Corporation evidenced by such Bond. No Holder or Beneficial Owner may elect to retain a Bond subject to mandatory purchase in lieu of optional redemption.

SECURITY FOR THE BONDS

General

The Bonds are limited obligations of the Authority. See “—Limited Obligation of the Authority” below. The Bonds are payable solely from the Revenues, being: payments made by the Corporation under the Loan Agreement (the “Loan Repayments”); payments made by the Obligated Group on Obligation No. 1; and certain funds held under the Bond Indenture pledged by the Authority under the Bond Indenture for such payment. Under the Loan Agreement, the Corporation is required to make Loan Repayments in amounts sufficient to pay the Debt Service on the Bonds when due. The obligation of the Corporation to make Loan Repayments under the Loan Agreement is evidenced and secured by Obligation No. 1 issued under the Master Indenture. See “—The Master Indenture” below. The Authority will assign its right, title, and interest in the Loan Agreement (except for its right to receive any administrative fees and expenses and to be indemnified) and Obligation No. 1 to the Trustee.

Pursuant to the Master Indenture, the Corporation, as Obligated Group Representative, will issue and deliver Obligation No. 1 to the Trustee in the aggregate principal amount of the Bonds. Simultaneously with the issuance and delivery of Obligation No. 1, pursuant to the Master Indenture, the Corporation, as Obligated Group Representative, will issue and deliver the Swap Obligation to the Swap Counterparty under the Preexisting Swap Agreement to secure its payment obligations thereunder. The Master Indenture provides that payments on any Obligations issued and outstanding thereunder, including Obligation No. 1, the Swap Obligation and any additional Obligations, are the joint and several obligations of each Member of the Obligated Group. Notwithstanding uncertainties (described below under “—Limitations on Enforceability”) with respect to the enforceability of the covenants in the Master Indenture of each Member of the Obligated Group to be jointly and severally liable for each Obligation, the accounts of the Members of the Obligated Group will be combined for financial reporting purposes and will be used in determining whether the covenants and financial tests contained in the Master Indenture are met.

Obligation No. 1 requires payments by the Obligated Group to the Trustee in amounts sufficient to pay the Debt Service on the Bonds, when due. The Obligated Group will make payments on Obligation No. 1 directly to Trustee. Obligation No. 1 will entitle the Trustee to the protection of the covenants, restrictions and other obligations imposed upon the Members of the Obligated Group by the Master Indenture.

The obligations of the Obligated Group to make payments on Obligation No. 1 are full and unlimited obligations of the Members of the Obligated Group and are secured by the lien of a deed of trust on certain of the Corporation's property. See “—The Master Indenture—Deed of Trust” herein below. The obligations are not secured by any other mortgage of, or security interest in, any real or personal property of the Corporation or the Foundation or any other future member of the Obligated Group, other than the security interest granted in Collateral by the Obligated Group to the Master Trustee. See “—The Master Indenture—Security Interest in Collateral” below.

Limited Obligation of the Authority

THE BONDS ARE SPECIAL LIMITED OBLIGATIONS OF THE AUTHORITY, PAYABLE SOLELY FROM AND SECURED BY THE REVENUES PLEDGED THEREFOR PURSUANT TO THE BOND INDENTURE AND OBLIGATION NO. 1. NEITHER THE AUTHORITY, THE ASSOCIATION OF BAY AREA GOVERNMENTS (“ABAG”) NOR THE MEMBERS OF THE AUTHORITY OR ABAG SHALL BE DIRECTLY OR INDIRECTLY OR CONTINGENTLY OR MORALLY OBLIGATED TO USE ANY OTHER MONEYS OR ASSETS OF THE AUTHORITY, ABAG OR ANY OF THEIR MEMBERS TO PAY ALL OR ANY PORTION OF DEBT SERVICE DUE ON THE BONDS. THE BONDS AND THE OBLIGATION TO PAY PRINCIPAL OF, PREMIUM, IF ANY, AND INTEREST THEREON, DO NOT CONSTITUTE AN INDEBTEDNESS OR AN OBLIGATION OF THE AUTHORITY OR ABAG, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF, WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION, OR A CHARGE AGAINST THE GENERAL CREDIT OR TAXING POWERS OF ANY OF THEM, BUT SHALL BE PAYABLE SOLELY FROM THE REVENUES DESCRIBED HEREIN. NO OWNER OF THE BONDS SHALL HAVE THE RIGHT TO COMPEL THE EXERCISE OF THE TAXING POWER OF THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF TO PAY ANY PRINCIPAL

OF, PREMIUM, IF ANY, OR INTEREST ON THE BONDS. NEITHER THE AUTHORITY NOR ABAG HAS ANY TAXING POWER.

Bond Reserve Fund

The Bond Reserve Fund for the Bonds will be established pursuant to the Bond Indenture. The Bond Reserve Fund will be funded in connection with the issuance of the Bonds, in an amount equal to the Bond Reserve Requirement. The “Bond Reserve Requirement” is equal to the least of: (i) 10% of the principal amount of Bonds at any time Outstanding; (ii) Maximum Annual Bond Service on the Bonds; and (iii) 125% of the average Annual Bond Service on all Bonds Outstanding to maturity or earlier mandatory redemption on the date on which such calculation is required in accordance with the terms of the Loan Agreement, calculated by the Corporation under the assumption that the principal amount of the Bonds are paid in accordance herewith. Moneys on deposit in the Bond Reserve Fund are required to be used by the Trustee, to the extent moneys on deposit in the Interest Fund, Principal Fund or the Sinking Fund established under the Bond Indenture are insufficient to pay Debt Service on the Bonds, as the same become due. The Bond Indenture provides that amounts required to be on deposit in the Bond Reserve Fund may be substituted by the Corporation with a letter of credit or a surety bond policy in an amount equal to the Bond Reserve Requirement. See APPENDIX C— “SUMMARY OF PRINCIPAL DOCUMENTS—BOND INDENTURE— Bond Reserve Fund.”

The Master Indenture

Obligation No. 1 and the Swap Obligation will entitle the holders thereof to the benefit of the covenants, restrictions and other obligations imposed on the Obligated Group under the Master Indenture, as described in APPENDIX C— “SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE.” Certain of those covenants and restrictions are described below.

Security Interest in Collateral. Pursuant to the Master Indenture, to secure payment of all Obligations, each Member of the Obligated Group grants to the Master Trustee, for so long as such Member remains a Member of the Obligated Group, a security interest (subject to Permitted Encumbrances) in Collateral. The Master Indenture defines “Collateral” as including, among other things, “Gross Revenues,” which is defined as all revenues, income, receipts and money now existing or hereafter received by each Member, including (a) gross revenues collected from its operations and possession of and pertaining to its properties, (b) gifts, grants, bequests, donations and contributions, (c) proceeds derived from (i) condemnation, (ii) insurance, (iii) accounts and accounts receivable, including health-care-insurance receivables, (iv) payment intangibles, (v) securities and other investment property, (vi) inventory and other tangible and intangible property, (vii) medical reimbursement programs and agreements, (viii) contract rights and other rights and assets now or hereafter owned, held or possessed by or on behalf of any Member, and (d) rentals received from the lease of real estate. Pursuant to the Master Indenture, each Member of the Obligated Group, so long as any of the Obligations remain outstanding, shall deposit all of the Gross Revenues of the Obligated Group with a depository bank or banks in one or more funds designated as the “Gross Revenue Accounts” and, subject to the provisions of the Master Indenture permitting application of the Gross Revenues for the purposes and upon the terms and conditions set forth therein, shall grant a security interest (to the extent permitted by law) to the Master Trustee in all Gross Revenue Accounts and all of the Gross Revenues of the Obligated Group to secure the required payments and the performance by the Members of the Obligated Group of their obligations under the Master Indenture

The security interest in Collateral does not include Restricted Assets owned by the Obligated Group. See APPENDIX C “SUMMARY OF PRINCIPAL DOCUMENTS—DEFINITIONS OF CERTAIN TERMS.” In addition, the enforceability, priority and perfection of the security interest in the Collateral may be limited by a number of factors, or may be subordinated to the interests and claims of others in certain circumstances, as discussed under “– Limitations on Enforceability” below.

Third party payments and other revenues derived from physician services (“Physician Revenues”) will not be included in the Collateral pledged by the Obligated Group to secure Obligations. Although Physician Revenues are included in the historical financial information contained in APPENDIX A describing the Obligated Group, after January 1, 2007, Physician Revenues have been owned by BCP, which is not a Member of the Obligated Group. For the fiscal years ended December 31, 2004, 2005 and 2006, the operations attributable to Physician Revenues

was approximately 4.28%, 5.05% and 5.35%, respectively, of the net patient service revenue of the Corporation. Bondholders will not have a security interest in Physician Revenues and will not have any right, if there were an event of default under the Loan Agreement or Obligation No. 1, to Physician Revenues as a source of payment of the Bonds.

The Deed of Trust required by the First Supplemental Master Indenture. Pursuant to the First Supplemental Master Indenture, the Corporation will execute a Deed of Trust on certain of its properties to secure all of the Obligations issued under the Master Indenture. When Obligation No. 1 is satisfied and the First Supplemental Master Indenture is terminated, the Master Indenture will no longer require the Deed of Trust (unless required by a future supplement, including any supplement that may be executed in connection with the Swap Obligation) and it will be reconveyed. The Deed of Trust will create a first mortgage lien on all such real property and fixtures of the Corporation. In the event that there is a default under the Master Indenture, the Master Trustee has the right to foreclose on such facilities under certain circumstances. All amounts collected upon foreclosure of the facilities pursuant to the Deed of Trust will be used to pay certain costs and expenses incurred by, or otherwise related to, the foreclosure, the performance of the Master Trustee and/or the beneficiary under the Deed of Trust, and then to pay amounts owing under the Master Indenture. For a summary of certain provisions of the Deed of Trust, see APPENDIX C –“SUMMARY OF PRINCIPAL DOCUMENTS – DEED OF TRUST.”

Additional Obligations. Obligation No. 1, the Swap Obligation and any additional Obligations issued by any Member of the Obligated Group under the Master Indenture are collectively referred to herein as the “Obligations.” Additional Obligations may be issued under the Master Indenture to secure additional Indebtedness or for other purposes. Additional Obligations will be equally and ratably secured with Obligation No. 1 and the Swap Obligation.

If an Event of Default occurs under the Master Indenture, it is uncertain whether the Master Trustee could obtain a remedy on behalf of the holders of the Obligations adequate to provide full and timely payment of the Bonds. See “—Limitations on Enforceability” below.

Additional Indebtedness and Liens. Subject to certain requirements set forth in the Master Indenture, Members of the Obligated Group may incur Additional Indebtedness and other obligations under certain circumstances, which may, but need not, be evidenced or secured by additional Obligations under the Master Indenture. See the information in APPENDIX C “SUMMARY OF PRINCIPAL DOCUMENTS - MASTER INDENTURE—Covenants of the Members—Limitations on Additional Indebtedness.”

Members of the Obligated Group may not create, assume or suffer to exist any Lien upon their Property, except Permitted Encumbrances. In addition to other Permitted Encumbrances not subject to an aggregate limitation, the Master Indenture contains provisions permitting the Members of the Obligated Group to create Liens on Property subject to an aggregate limitation, provided that the value of Property (calculated as provided in the Master Indenture) of the Obligated Group that is encumbered by such Liens may not exceed 10% of the value (calculated on the same basis as the value of the encumbered property) of the Property of the Obligated Group. See the information in APPENDIX C-- “SUMMARY OF PRINCIPAL DOCUMENTS—FIRST SUPPLEMENTAL MASTER INDENTURE—Additional Covenants.”

Disposition of Assets The Master Indenture limits the ability of the Obligated Group to sell, lease or otherwise dispose of cash or property. For a description of the conditions under which cash or property, including property secured by the Deed of Trust, may be sold, leased or otherwise disposed of, see APPENDIX C—“SUMMARY OF PRINCIPAL DOCUMENTS – MASTER INDENTURE – Sale, Lease or Other Disposition of Property ” and “– FIRST SUPPLEMENTAL MASTER INDENTURE – Additional Covenants.”

Merger, Consolidation, Sale or Conveyance. Under the Master Indenture, a Member of the Obligated Group may merge into, or consolidate with, or sell, transfer, assign or otherwise convey all or substantially all of its Property to another Member or any Person who is not a Member upon compliance with the provisions of the Master Indenture summarized under the caption APPENDIX C—“SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE—Covenants of the Members—Consolidation, Merger, Acquisition, Sale or Conveyance.” This could, under certain circumstances, lead to substantial changes to the current covenant restrictions on the Obligated Group in connection with the Bonds or the substitution of different security for the Bonds. The new

obligor could have substantial debt outstanding that is entitled to security in addition to that provided for the benefit of the Bonds.

Financial Information. The audited financial information contained in APPENDIX A and APPENDIX B hereto includes, in accordance with accounting principles generally accepted in the United States, certain financial information of the Corporation and the Foundation, each Members of the Obligated Group, as well as the financial information concerning BCP, CFHN and Family House, which are not Members of the Obligated Group, and which are not obligated to pay Debt Service on the Bonds or make payments with respect to Obligation No. 1. Financial information of Members of the Obligated Group could in the future include revenues and assets of additional Persons who are not Members of the Obligated Group, who would not be obligated to pay Debt Service on the Bonds or make payments with respect to Obligations issued under the Master Indenture and whose revenues and assets would not be available to be applied to payment of the Debt Service on the Bonds or Obligations. See APPENDIX A — “INFORMATION CONCERNING THE OBLIGATED GROUP—HISTORICAL FINANCIAL INFORMATION” and the consolidated audited financial statements in APPENDIX B hereto.

The foregoing notwithstanding, the Master Indenture provides that the financial information upon which the various calculations under the Master Indenture will be based may include financial results of Immaterial Affiliates, in addition to Members of the Obligated Group. See APPENDIX C—“SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE—Covenants of the Members—Filing of Financial Statements, Reports and Other Information.”

Limitations on Enforceability

Bankruptcy. In the event of bankruptcy of the Corporation or the Foundation, the rights and remedies of the Holders are subject to various provisions of the federal Bankruptcy Code. If the Corporation or the Foundation were to file a petition in bankruptcy, payments made by the Corporation or the Foundation during the 90-day (or perhaps one-year) period immediately preceding the filing of such petition may be avoidable as preferential transfers to the extent such payments allow the recipients thereof to receive more than they would have received in the event of such entity’s liquidation. Security interests and other liens granted to the Master Trustee and perfected during such preference period also may be avoided as preferential transfers to the extent such security interest or other lien secures obligations that arose prior to the date of such perfection. Such a bankruptcy filing would operate as an automatic stay of the commencement or continuation of any judicial or other proceeding against the Corporation or the Foundation and its property and as an automatic stay of any act or proceeding to enforce a lien upon or to otherwise exercise control over such property, as well as various other actions to enforce, maintain or enhance the rights of the Master Trustee. If the bankruptcy court so ordered, the property of the Corporation or the Foundation, including accounts receivable and proceeds thereof, could be used for the financial rehabilitation of the Corporation or the Foundation despite any security interest of the Master Trustee therein. The rights of the Master Trustee to enforce its security interests and other liens could be delayed during the pendency of the rehabilitation proceeding.

The Corporation or the Foundation could file a plan for the adjustment of its debts in any such proceeding, which could include provisions modifying or altering the rights of creditors generally or any class of them, secured or unsecured. The plan, when confirmed by a court, binds all creditors who had notice or knowledge of the plan and, with certain exceptions, discharges all claims against the debtor to the extent provided for in the plan. No plan may be confirmed unless certain conditions are met, among which conditions are that the plan be feasible and that it shall have been accepted by each class of claims impaired thereunder. Each class of claims has accepted the plan if at least two-thirds in dollar amount and more than one-half in number of the class cast votes in its favor. Even if the plan is not so accepted, it may be confirmed if the court finds that the plan is fair and equitable with respect to each class of non-accepting creditors impaired thereunder and does not discriminate unfairly.

In addition, the obligations of the Corporation or the Foundation to pay debt service on the Bonds is not secured by a lien on or security interest in any assets or revenues of the Corporation or the Foundation, other than Collateral. Except with respect to such security interest on Collateral, in the event of a bankruptcy of the Corporation or the Foundation, Holders would be unsecured creditors and would be in an inferior position to any secured creditors and on a parity basis with all other unsecured creditors.

In the event of bankruptcy of the Corporation or the Foundation, there is no assurance that certain covenants, including tax covenants, contained in the Loan Agreement or other documents would survive. Accordingly, a bankruptcy trustee could take action that would adversely affect the exclusion of interest on the Bonds from gross income for federal income tax purposes.

Security Interest in Collateral. The enforceability, priority and perfection of the security interest granted by the Members of the Obligated Group in its Collateral may be limited by a number of factors, or be subordinated to the interest and claims of others. Some examples of such factors and cases of subordination or prior claims are (i) statutory liens, (ii) rights arising in favor of the United States of America or any agency thereof, (iii) present or future prohibitions against assignment in any federal statutes or regulations, (iv) constructive trusts, equitable liens or other rights impressed or conferred by any state or federal court in the exercise of its equitable jurisdiction, (v) federal or State bankruptcy or insolvency laws that may affect the enforceability of the Master Indenture or of the security interest of Collateral and (vi) rights of third parties, and in some instances, the Members of the Obligated Group, in Collateral constituting cash or instruments and not in the possession of the Master Trustee or the its agent. In addition, it may not be possible to perfect a security interest in any manner whatsoever in certain types of Collateral (e.g., gifts, donations, certain insurance proceeds and Medicare or Medi-Cal payments) prior to actual receipt by a Member for deposit in the Gross Revenue Accounts. See APPENDIX C – “SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE—Covenants of the Members—Gross Revenue Account.”

Risks Related to Master Indenture Financings; Fraudulent Transfer or Conveyance Statutes. It is possible that the joint and several obligations of an Obligated Group Member to make payments under Obligations in respect of moneys used by another Obligated Group Member may be avoided in an action brought by creditors of the first Obligated Group Member pursuant to California’s fraudulent conveyance statutes or may be avoided for the benefit of other creditors by a debtor or trustee in bankruptcy in the event of the bankruptcy of such Obligated Group Member. Depending upon whether the federal Bankruptcy Code or California’s fraudulent conveyance statutes are applicable, an obligation may be avoided if (a) the obligation was incurred without receipt by the Member of “fair consideration” or “reasonably equivalent value,” and (b) the obligation renders the Member “insolvent,” as such terms are defined under the applicable statute. Interpretation by the courts of the tests of “Insolvency,” “reasonably equivalent value” and “fair consideration” has resulted in a conflicting body of case law. For example, joint and several obligation under the Master Indenture to pay all Obligations issued thereunder, including payments in respect of funds used for the benefit of other Obligated Group Members, may be held to be a “transfer” which makes such Obligated Group Members “insolvent,” in the sense that the total amount due under all Obligations could be considered as causing liabilities to exceed its assets. Also, an Obligated Group Member may be deemed to have received less than “fair consideration” for its joint and several obligation because only a portion of the proceeds of the Bonds are to be used to finance facilities occupied or used by an Obligated Group Member. While an Obligated Group Member may benefit generally from facilities financed with proceeds of the Bonds for the other Obligated Group Members, the actual cash value of this benefit may be less than the value of the Obligated Group Member’s joint and several obligation.

In addition, Obligated Group Members that are nonprofit corporations may be held by a court to be subject to a charitable trust which prohibits payments in respect of obligations incurred by or for the benefit of others. Such a determination may be made if the Obligated Group Member making the payments has insufficient assets remaining to carry out its own charitable functions or, under certain circumstances, if the obligation paid was incurred for purposes inconsistent with or beyond the scope of the charitable purposes of the Obligated Group Member which made the payment.

Enforceability of the Loan Agreement, Bond Indenture and Master Indenture. The legal right and practical ability of the Trustee to enforce rights and remedies under the Loan Agreement and the Bond Indenture, and of the Master Trustee to enforce remedies under the Master Indenture, may be limited by laws relating to bankruptcy, insolvency, reorganization, fraudulent conveyance or moratorium and by other similar laws affecting creditors’ rights and by application of equitable principles. In addition, enforcement of such rights and remedies will depend upon the exercise of various remedies specified by such documents, which, in many instances, may require judicial actions that are subject to discretion and delay, that otherwise may not be readily available or that may be limited by certain legal principles.

The various legal opinions delivered concurrently with the delivery of the Bonds will be qualified as to the enforceability of the various legal instruments by limitations imposed by State and federal laws, rulings, policy and decisions affecting remedies and by bankruptcy, reorganization or other laws of general application affecting the enforcement of creditors' rights or the enforceability of certain remedies or document provisions.

BONDHOLDERS' RISKS

The purchase of the Bonds involves investment risks that are discussed throughout this Official Statement. Prospective purchasers of the Bonds should evaluate all of the information presented in this Official Statement. The discussion under this caption focuses primarily on the general risks associated with the operations and activities of hospitals and healthcare systems, whereas APPENDIX A describes some of the risks related to the Obligated Group specifically. These should be read together. This discussion is not intended to be comprehensive or definitive, but rather to summarize certain matters which could affect payment of the Bonds.

General

Payment of the Debt Service on the Bonds will be made solely from payments made by the Obligated Group and certain funds held by the Trustee under the Bond Indenture. No representation or assurance can be made that the Obligated Group will have revenues in amounts sufficient to pay the Debt Service on the Bonds. Any of the risk factors described in the Official Statement may adversely affect revenues of the Obligated Group and impair its ability to pay the Debt Service on the Bonds. There can be no assurance that the financial condition or operations of the Obligated Group will not be adversely affected by any of these or other factors.

The Obligated Group and its affiliates are subject to a wide variety of federal and State regulatory actions and legislative and policy changes by those governmental agencies and private entities that administer Medicare, Medi-Cal (Medicaid) and other payors, and is subject to actions by, among others, the Centers for Medicare and Medicaid Services (CMS), of the U.S. Department of Health and Human Services (DHHS), the National Labor Relations Board, The Joint Commission, and other federal, state and local government agencies. The future financial condition of the Obligated Group and its affiliates could be adversely affected by, among other things, changes in the method and amount of payments to the Obligated Group by governmental and nongovernmental payors, the financial viability of these payors, volatility in income from investments and contributions, increased competition from other health care entities, demand for health care, costs associated with responding to governmental inquiries and investigations, changes in the methods by which employers purchase health care for employees, capability of management, future changes in the economy, demographic changes, availability of physicians and nurses, and malpractice claims and other litigation. These factors and others may adversely affect payment by the Obligated Group under Obligation No. 1 and, consequently, payment of the Bonds.

Set forth below is a limited discussion of certain of the risks affecting the Obligated Group and its ability to pay the Bonds. Investors should recognize that the discussion below does not cover all such risks, that payment provisions and regulations and restrictions on hospitals change frequently, and that additional material payment limitations and regulations or restrictions may be created, implemented or expanded while the Bonds are Outstanding.

Significant Risk Areas Highlighted

Certain of the primary risks associated with the operations of, and investments by, the Obligated Group are briefly summarized in general terms below and are explained in greater detail in subsequent sections. The occurrence of one or more of these risks could have a material adverse effect on the financial conditions and results of operations of the Obligated Group, and in turn, the ability of the Obligated Group to pay the Bonds.

General Economic Conditions; Bad Debt and Indigent Care. The financial results of health care facilities are influenced by the economy of the regions in which they are located. To the extent that State, county or city governments are unable to provide a safety net to pay for hospital and medical services, pressure is applied to hospitals to increase free or under-reimbursed care. Economic downturns and lower funding of State Medi-Cal (Medicaid) and other federal, State and local healthcare programs may increase the number of patients treated by

hospitals who are uninsured or otherwise unable to pay for some or all of their care. These conditions may cause increased bad debt and increased care provided to indigent persons. At the same time, non-operating revenue from investments and other sources may be reduced or eliminated. These factors may have a material adverse impact on hospitals.

State Medi-Cal (Medicaid) Programs. Medi-Cal is a State program of medical assistance, funded jointly by the Federal Government and the State, for certain qualifying individuals and their dependents. State Medi-Cal and other State and local health care programs constitute an important payor source to many hospitals and, in particular, to children's hospitals. These programs often pay hospitals at levels that may be below the actual cost of the care provided. As Medi-Cal is partially funded by the State, the budget challenges facing the State may result in lower funding levels and/or payment delays. These reductions and/or delays could have a material adverse impact on hospitals.

Investments. The Members of the Obligated Group have holdings in a broad range of investments. Market fluctuations have significantly affected and will likely significantly affect the income from, and the value of, those investments, and such fluctuations may be and historically have been at times material. For a discussion of the Obligated Group's investment performance, see APPENDIX A – "INFORMATION CONCERNING THE OBLIGATED GROUP—MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL PERFORMANCE."

Rate Pressure from Insurers and Major Purchasers. Certain hospital markets, including many regions in the State, are strongly impacted by large health insurers and, in some cases, by major purchasers of health services. In those areas, health insurers may have significant influence over hospital rates, utilization and competition. Rate pressure imposed by health insurers or other major purchasers of health services may have a material adverse impact on hospitals, particularly if major purchasers put increasing pressure on payors to restrain rate increases. Business failures by health insurers also could have a material adverse impact on contracted hospitals in the form of payment shortfalls or delays and continuing obligations to care for managed care patients without receiving payment.

Nonprofit Health Care Environment. Recently, an increasing number of the operations or practices of health care providers have been challenged or questioned to determine if they are consistent with the regulatory requirements that apply to nonprofit tax-exempt organizations. Areas that have come under examination have included pricing practices, billing and collection practices, charitable care, executive compensation, "excess benefit transactions" with insiders and exemption of property from real property taxation. These challenges and questions have come from a variety of sources, including state attorneys general, the Internal Revenue Service (the "IRS"), state taxing authorities, labor unions, Congress, state legislatures and patients, and in a variety of forums, including hearings, audits and litigation. The challenges and examinations and any resulting legislation, regulations, judgments or penalties could have a material adverse effect on nonprofit hospitals and particularly on nonprofit health care providers.

Capital Needs vs. Capital Capacity. Hospital operations are capital-intensive. Regulation, technology and physician/patient expectations require constant and often significant capital investment. Seismic requirements mandated by the State of California may require that many California hospital facilities be substantially modified, replaced or closed. Nearly all hospitals in California are affected. Estimated construction costs are substantial and actual costs of compliance may exceed estimates. Total capital needs may outstrip capital capacity.

Government "Fraud" Enforcement. "Fraud" in government funded health care programs is a significant concern of DHHS and CMS and many states and is one of the federal government's prime law enforcement priorities. The federal government and, to a lesser degree, state governments impose a wide variety of extraordinarily complex and technical requirements intended to prevent over-utilization based on economic inducements, misallocation of expenses, overcharging and other forms of "fraud and abuse" in the Medicare and Medicaid programs, as well as other state and federally-funded health care programs. This body of regulation impacts a broad spectrum of hospital commercial activity, including billing, accounting, recordkeeping, medical staff oversight, physician office leases, physician contracting and recruiting, cost allocation, clinical trials, discounts and other functions and transactions.

Violations and alleged violations may be deliberate but also frequently occur in circumstances where management is unaware of the conduct in question, as a result of mistake, or where the individual participants do not know that their conduct is in violation of law. Violations may occur and be prosecuted in circumstances that do not have the traditional elements of fraud, and enforcement actions may extend to conduct that occurred in the past. The government periodically conducts widespread investigations covering categories of services or certain accounting or billing practices.

Violations carry significant sanctions. The government and/or private whistleblowers in qui tam actions often pursue aggressive investigative and enforcement actions. The government has a wide array of civil, criminal and monetary penalties, including withholding essential hospital payments from the Medicare or Medicaid programs or exclusion from those programs. Aggressive investigation tactics, negative publicity and threatened penalties can be and often are used to force settlements, payment of fines and prospective restrictions that may have a materially adverse impact on hospital operations, financial condition, results of operations and reputation. Multi-million dollar fines and settlements are common. These risks are generally uninsured. Government enforcement and private whistleblower suits may increase in the hospital sector. Many hospitals and health systems are likely to be adversely impacted.

Nursing and Other Shortages. Currently, a nursing shortage exists which may have its primary impact on hospitals. Various studies have predicted that this nursing shortage will become more acute over time and grow to significant proportions. In California, new state regulation of nursing staff ratios will likely intensify the nursing shortage. In addition, shortages of other professional and technical staff such as pharmacists, therapists, laboratory technicians and others may occur or worsen. Hospital operations, patient and physician satisfaction, financial condition, results of operations and future growth could be negatively affected by these shortages, resulting in a material adverse impact to hospitals.

Labor Costs and Disruption. Inpatient health care facilities are labor-intensive. Labor costs, including salary, benefits and other liabilities associated with the workforce, have significant impact on hospital operations and financial condition. Employees are increasingly organized in collective bargaining units and may be involved in work actions of various kinds, including work stoppages and strikes. Overall costs of the hospital workforce are high, and turnover is high. Pressure to recruit, train and retain qualified employees is expected to accelerate. These factors may materially increase hospital costs of operation. Workforce disruption may negatively impact hospital revenues and reputation.

Technical and Clinical Developments. New clinical techniques and technology, as well as new pharmaceutical and genetic developments and products, may alter the course of medical diagnosis and treatment in ways that are currently unanticipated and that may dramatically change medical and hospital care. These developments could result in higher hospital costs, reductions in patient populations and/or new sources of competition for hospitals.

Costs and Restrictions from Governmental Regulation. Nearly every aspect of hospital operations is regulated, in some cases by multiple agencies of government. The level and complexity of regulation appear to be increasing, resulting in operational limitations, enforcement and liability risks, and significant and sometimes unanticipated cost impacts.

Proliferation of Competition. Health care facilities increasingly face competition from specialty providers of care and free-standing outpatient facilities such as diagnostic imaging centers and ambulatory surgery centers. This may cause hospitals to lose essential inpatient or outpatient market share. Competition may be focused on services or payor classifications where hospitals realize their highest margins, thus negatively affecting programs that are economically important to hospitals. Specialty hospitals may attract specialists as investors and may seek to treat only profitable classifications of patients, leaving full-service hospitals with higher acuity and/or lower paying patient populations. These new sources of competition may have a material adverse impact on hospitals. The growing consumer movement for pricing transparency may also adversely impact hospitals' charging structure.

Pension and Benefit Funds. As large employers, hospitals may incur significant expenses to fund pension and benefit plans for employees and former employees and to fund required workers' compensation benefits.

Funding obligations in some cases may be erratic or unanticipated and may require significant commitments of available cash needed for other purposes, either or both of which could have a material adverse impact on hospitals.

New Accounting Standards. On September 29, 2006, the Financial Accounting Standards Board (“FASB”) issued Statement No. 158, *Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans* (an amendment of FASB Statements No. 87, 88 106 and 132R). The issuance of Statement No. 158 marks the completion of the first phase of FASB’s comprehensive project to improve the accounting and disclosure for defined benefit pension and other postretirement plans. The new standard requires an employer to (i) recognize in its balance sheet an asset or a liability for a plan’s overfunded or underfunded status, as applicable, (ii) measure a plan’s funded status as of the end of the employer’s fiscal year, and (iii) recognize changes in the funded status of a defined benefit postretirement plan in the year in which the changes occur. The requirements to recognize the funded status of a benefit plan and to provide the required disclosures are effective for fiscal years ending after December 15, 2006 (for entities with publicly traded equity securities and after June 15, 2007 for all other entities), and the measurement date requirement is effective for fiscal years ending after December 15, 2008.

Medical Liability Litigation and Insurance. Medical liability litigation is subject to public policy determinations and legal and procedural rules that may be altered from time to time, with the result that the frequency and cost of such litigation and resultant liabilities may increase in the future. Health care facilities may be affected by negative financial and liability impacts on physicians. Costs of insurance, including self-insurance, may increase dramatically.

Facility Damage. Health care facilities are highly dependent on the condition and functionality of their physical facilities. Damage from earthquake, other natural causes, fire, deliberate acts of destruction, or various facilities system failures may have a material adverse impact on hospital operations, financial condition and results of operations. The Hospital is located near an active earthquake fault in California.

Patient Service Revenues

State Medi-Cal (Medicaid) Program. Medi-Cal is the “Medicaid” program in California. The Medi-Cal program often pays hospitals at levels that are below the actual cost of the care provided. The federal government provides substantial funding to the Medi-Cal program, so long as it meets federal standards. Attempts to balance or reduce the federal budget and/or California’s budget deficits will likely negatively impact Medi-Cal spending.

For the fiscal years ended December 31, 2004, 2005 and 2006, the Corporation received approximately 46.6%, 47.3% and 47.1%, respectively, of net patient service revenue from the Medi-Cal program. For the five-month periods ended May 31, 2006 and 2007, the Corporation received approximately 49.6% and 44.0%, respectively, of net patient service revenue from the Medi-Cal program. See APPENDIX A - “INFORMATION CONCERNING THE OBLIGATED GROUP—HISTORICAL FINANCIAL INFORMATION—Sources of Healthcare Revenue.”

Under a five-year federal Medicaid waiver approved in 2005, the State selectively contracts with hospitals to provide acute inpatient services to Medi-Cal patients. The financial impact of selective contracting with a particular hospital depends upon a variety of factors, such as the base contract rates, whether a hospital qualifies as a disproportionate share hospital, the availability of supplemental payments for disproportionate share hospitals and an individual hospital’s ability to control costs.

Generally, such selective inpatient contracting is made on a negotiated per diem payment basis, and such payment rates historically have not increased in direct relation to inflation or provider costs. Medi-Cal payments for inpatient hospital services are also subject to an aggregate statewide upper payment limit, under which aggregate payments to non-public hospitals may not exceed the aggregate amount which would have been paid if Medicare payment principles were utilized. Additionally, the total Medi-Cal payments to an individual hospital for inpatient hospital services for any fiscal period may not exceed that hospital’s customary charges for the services. These limitations apply to the per diem rates and supplemental payments received under S.B. 1100 (described below), but do not apply to disproportionate share hospital replacement payments under S.B. 1100. Medi-Cal payments for outpatient hospital services are based on fee schedules set by the State.

Generally, the State or the contracting hospitals may terminate Medi-Cal contracts upon 120 days' prior written notice. The State also may terminate these contracts without notice under certain circumstances and is obligated to make contractual payments only to the extent the State legislature appropriates adequate funding therefor.

Disproportionate Share Hospital Replacement Payments Under S.B. 1100. In 2005, the State legislature enacted the "Medi-Cal Hospital/Uninsured Care Demonstration Project Act," also known as S.B. 1100, to revise hospital inpatient reimbursement methodologies under the 2005 federal Medicaid waiver. Private hospitals such as the Hospital operated by the Corporation are eligible to receive payments funded from the State's General Fund and matching federal funds. Funding hence is subject to State and federal appropriation. These payments, called disproportionate share replacement payments under S.B. 1100, are made to hospitals that have disproportionately higher costs, volume or services related to the provision of services to Medi-Cal or other low-income patients than the statewide average. The non-federal portion of disproportionate share hospital replacement payments (approximately 50%) is funded through annual appropriations from the State General Fund. Disproportionate share payments are often the target of Medi-Cal payment reductions. Qualification for disproportionate share hospital replacement funds under S.B. 1100 is determined annually. Disproportionate share payments are extremely volatile and uncertain.

Supplemental Payments for Private Hospitals Under S.B. 1100. S.B. 1100 provides additional funding to disproportionate share hospitals providing emergency and outpatient services to Medi-Cal beneficiaries. Such payments are supplemental contract payments under the Medi-Cal selective contracting program payable from the Private Corporation Supplemental Fund, which is funded through discretionary annual appropriations from the State's General Funds, federal financial participation, and other governmental sources including voluntary inter-governmental transfers. Supplemental payments are often the target of Medi-Cal payment reductions. Qualification for supplemental payments is determined annually. Such payments are extremely volatile and uncertain.

The majority of the Corporation's patients are low-income and Medi-Cal eligible individuals. Historically, the Corporation has qualified as a disproportionate share hospital and, as such, has been eligible from year to year to receive funding under the State's predecessor disproportionate share hospital programs. There can be no assurance that such qualification will continue. See APPENDIX A – "HISTORICAL FINANCIAL INFORMATION— Sources of Healthcare Revenue."

State Children's Health Insurance Program. The State Children's Health Insurance Program ("SCHIP") is jointly financed by the federal and state governments and administered by the states. SCHIP is an insurance program for children whose families exceed the income threshold for Medicaid eligibility, but yet cannot afford commercial health insurance. CMS administers SCHIP, but each state creates its own program based upon minimum federal guidelines. Within broad federal guidelines, each state determines the design of its program, eligibility groups, benefit packages, payment levels for coverage and administrative and operating procedures. A SCHIP program can either be part of a state's Medicaid program, or a completely separate state program. California has implemented an SCHIP program. SCHIP provides a cap amount of funds to states on a matching basis for federal fiscal years through September 30, 2007.

While generally considered to be beneficial for both patients and providers by reducing the number of uninsured children, it is difficult to assess the fiscal impact of SCHIP on the payments to the Obligated Group because each state must periodically submit its SCHIP plan to the CMS for review to determine if it meets the federal requirements. If it does not meet the federal requirements, a state can lose its federal funding for its program. Finally, the SCHIP program currently is only funded by the federal government through 2007. Therefore, a state's decision to elevate the eligibility requirements, thereby decreasing the number of children eligible for SCHIP, the loss of federal approval for a state's program, or the failure of the federal government to appropriate additional funds for SCHIP after 2007 all could have an adverse impact on the financial condition of the Obligated Group.

Healthy Families Program. The State's Healthy Families Program, which is administered by the Managed Risk Medical Insurance Board, provides health care services to children of working parents who earn too much to qualify for Medi-Cal but who cannot afford private health insurance. The federal government funds approximately 65% of Healthy Families Program expenditures. There can be no assurance that this program will continue.

Medical Education Payments. In recent years, the direct and indirect medical education reimbursement programs have repeatedly emerged as targets in the legislative efforts to reduce the federal budget deficit. Legislation has capped the number of residents recognized by Medicare for reimbursement purposes and has limited reimbursement for both direct and indirect medical education costs.

State Budgets. Many states, including California, face severe financial challenges, including continuing budget deficits. These factors have resulted in a shortfall between revenue and spending demands. California continues to face a significant gap between the expected level of tax revenues and projected expenditures for fiscal years 2007-08 and beyond. No cuts in hospital reimbursement rates under Medi-Cal have been proposed in the Governor's proposed budget for fiscal year 2007-08. It is not possible to determine whether the Governor's proposed budget will be adopted as proposed or whether any cuts in provider reimbursement rates under Medi-Cal will take effect in the future.

The financial challenges facing the State may negatively affect hospitals in a number of ways, including, but not limited to, a greater number of indigent patients who are unable to pay for their care and a greater number of individuals who qualify for Medi-Cal and/or reductions in Medi-Cal reimbursement rates.

Medicare Program. Medicare is the federal health insurance system under which hospitals and other healthcare providers are paid for services provided to eligible elderly and disabled persons. Medicare is administered by CMS, which delegates to the states the process for certifying hospitals to which CMS will make payment. In order to achieve and maintain Medicare certification, hospitals must meet CMS's "Conditions of Participation" on an ongoing basis, as determined by the state and/or The Joint Commission. The requirements for Medicare certification are subject to change, and, therefore, it may be necessary for hospitals to effect changes from time to time in their facilities, equipment, personnel, billing, policies and services to address such changing requirements.

For the fiscal years ended December 31, 2004, 2005 and 2006 and for the five-month periods ended May 31, 2006 and 2007, Medicare payments represented less than one percent of the Corporation's net patient service revenue. See APPENDIX A — "INFORMATION CONCERNING THE OBLIGATED GROUP—HISTORICAL FINANCIAL INFORMATION—Sources of Healthcare Revenue."

California Health Care Proposal. California Governor Schwarzenegger has proposed a plan to enact universal health insurance coverage in California. The Governor stated that he believes that uncompensated care is a "hidden tax" that results in increased costs and that universal coverage, financed in part by fees on California employers and providers will help reduce these costs. As currently proposed, coverage would be funded by cost containment measures such as reducing regulatory requirements, requiring facilities and providers to implement measures to help prevent medical errors and health care acquired infections, and promoting healthy lifestyles, as well as the following fundraising measures: (a) assessing employment fees on California employers who have at least ten employees and who do not provide insurance coverage for those employees, (b) increasing payments to physicians and hospitals through improved Medi-Cal reimbursement rates, (c) requiring physicians and hospitals to contribute 2% and 4%, respectively, of their gross revenues to a fund used to finance the proposal, and (d) redirecting funds currently used to reimburse providers for indigent care. An additional component of the proposal would require insurers and hospitals to apply at least 85% of their premium revenues and spending on patient care rather than profit and administration. In addition, the proposal would establish potentially significant new regulatory requirements on California hospitals related to use of health information technology. The proposal continues to be revised, and it is not clear whether or in what form the proposal will be enacted, nor what impact the proposal would have on the health care industry in California.

If legislation were enacted in accordance with the above proposal, California hospitals would potentially receive higher reimbursement from Medi-Cal, and for indigent care, and perhaps higher private insurance payment, offset, however, by a potentially significant "tax" on gross revenues and the cost of complying with additional regulatory requirements. It is not possible to determine at this time whether the offset would be positive or negative to California hospitals as a whole or to any California hospital in particular.

Health Plans and Managed Care. Health care, including hospital services, increasingly is being provided through "managed care" plans that use discounts and other economic incentives to reduce or limit the cost and

utilization of health care services. Such plans include, without limitation, health maintenance organizations (“HMOs”) and preferred provider organizations (“PPOs”). Payments from managed care plans typically are lower than those received from traditional indemnity/commercial insurers. Failure to maintain contracts with managed care organizations could have the effect of reducing the market share and gross patient services revenues of the Corporation. Conversely, participation in managed care plans may maintain or increase the patient base, but could result in lower net income if the Corporation is unable to adequately contain its costs.

For the fiscal years ended December 31, 2004, 2005 and 2006, managed care, excluding Medi-Cal Managed Care, constituted approximately 44.7%, 45.9% and 47.3, respectively, of net patient service revenues of the Corporation. For the five-month periods ended May 31, 2006 and 2007, managed care, excluding Medi-Cal Managed Care, constituted approximately 44.5% and 53.5%, respectively, of net patient service revenues of the Corporation. See APPENDIX A – “INFORMATION CONCERNING THE OBLIGATED GROUP—HISTORICAL FINANCIAL INFORMATION - Sources of Healthcare Revenue.”

In California, managed care plans have replaced indemnity insurance as the primary source of non-governmental payment for hospital services, and hospitals must be capable of attracting and maintaining managed care business, often on a regional basis. Regional coverage and aggressive pricing may be required. However, it is also essential that contracting hospitals be able to provide the contracted services without significant operating losses, which may require multiple forms of cost containment.

Many HMOs and PPOs currently pay providers on a negotiated fee-for-service basis or, for institutional care, on a fixed rate per day of care, which, in each case, usually is discounted from the typical charges for the care provided. As a result, the discounts offered to HMOs and PPOs may result in payment to a provider that is less than its actual cost. Additionally, the volume of patients directed to a provider may vary significantly from projections, and/or changes in the utilization may be dramatic and unexpected, thus jeopardizing the provider’s ability to manage this component of revenue and cost.

Some HMOs employ a “capitation” payment method under which hospitals are paid a predetermined periodic rate for each enrollee in the HMO who is “assigned” or otherwise directed to receive care at a particular hospital. The hospital may assume financial risk for the cost and scope of institutional care given. If payment is insufficient to meet the hospital’s actual costs of care, or if utilization by such enrollees materially exceeds projections, the financial condition of the hospital could erode rapidly and significantly.

Often, HMO contracts are enforceable for a stated term, regardless of hospital losses, and may require hospitals to care for enrollees for a certain time period, regardless of whether the HMO is able to pay the hospital. Hospitals from time to time have disputes with managed care payors concerning payment and contract interpretation issues.

Failure to maintain contracts could have the effect of reducing the Corporation’s market share and gross patient services revenue. Conversely, participation may result in lower net income if participating hospitals are unable to adequately contain their costs. Thus, managed care poses one of the most significant business risks (and opportunities) the hospitals face.

Investments and Contributions

The Members of the Obligated Group have holdings in a broad range of investments. Investment income has historically constituted a significant portion of the net income of the Obligated Group. No assurance can be given that the investments of the Obligated Group will produce returns consistent with historical performance or that losses on investments will not occur in the future. Market fluctuations have significantly affected and will likely significantly affect the value of those investments, and such fluctuations may be and historically have been at times material. For a discussion of the Obligated Group’s investment performance, see APPENDIX A – “INFORMATION CONCERNING THE OBLIGATED GROUP—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL PERFORMANCE.”

A significant portion of the Foundation's income has historically consisted of donations. If the future level of donations decreases, this could have a material adverse impact on financial performance of the Obligated Group.

Limitations on Revenues for Research Programs

Funding of Research. The future funding of the Corporation's research programs is dependent on the continued availability of funds from the United States government, the State government, industry and other public, private and commercial sources and the ability of the Corporation to compete successfully for those funds. Although the Corporation's grant dollars have increased by 250% in the past seven years, there can be no assurance that such increases in funding will continue. For the fiscal year ended December 31, 2006, approximately 60.7% of the Corporation's contract and grant revenues was derived from United States government agencies. In recent years, funding of the Corporation's research programs has increased, but there can be no assurance as to the adequacy of future funding for research programs. Grants from federal and State agencies have been funded in past years, but they are subject to annual congressional and legislative, as appropriate, appropriations and payment. No assurance can be given that such appropriations or payments will be made in the future or that the various forms of federal and State grant, contract or aid programs will continue at current levels. A loss or significant reduction of such programs could have a material adverse effect on the Corporation's research activities, which could have a material adverse impact on the Corporation's financial position.

Payment and Recapture Methodology. Certain costs of the Corporation relating to its research programs are generally eligible for recovery through direct and indirect charges to all federal and State government contracts and grants. Direct costs are specifically related to a research project and include wages of scientists and technicians, supplies and grant-specific equipment. Indirect costs also are incurred in the accomplishment of research programs, but such costs have been incurred for purposes common to some or all of the research programs of the Corporation. Examples of indirect costs include utilities, occupancy and facility costs, and general management and administrative services such as accounting, purchasing, human resources and library.

The federal Office of Management and Budget ("OMB") has established regulations to govern indirect cost reimbursement recovery principles and procedures to ensure that the federal government bears a fair share of the total costs associated with research programs. The Corporation negotiates, prospectively, a predetermined rate for a specific number of years with the Division of Cost Allocation for the West Coast region of DHHS, the Corporation's "cognizant" agency. The indirect costs that are recovered with respect to any individual grant are determined by applying the negotiated indirect cost rate to the total of that grant's direct costs. The negotiated rate reflects, through carry-forward adjustments, the variances that occur between a prospectively negotiated rate based on budgets and actual experience. While the cost principles are intended to provide for a sharing and allocation of indirect costs, certain costs, such as fund-raising, are not allowable. There can be no assurance that the fixed rate cost reimbursement negotiated by the Corporation will cover the indirect costs associated with the Corporation's research functions. Any shortfall may have a material adverse impact on the Corporation's financial condition.

In addition, the Corporation recaptures from certain of its clients certain expenses associated with facility and equipment capital investments for the benefit of such clients. The recovery of such expenses is governed by the Federal Acquisition Regulations and/or the federal Cost Accounting Standards, as applicable, and the federal Cost Accounting Standards, and the rate of such recapture is based on the rates set semiannually by the United States Treasury.

Regulatory Environment. A substantial portion of the Corporation's research revenues is derived from government contracts. From time to time regulatory changes at the state or federal level are proposed that may impact the Corporation's performance with respect to government contracts. Such regulations may increase compliance burdens of the Corporation, and the Corporation may elect to alter its operations to mitigate the effect of such changes. Management does not expect such regulatory changes would result in a material adverse change in its operations; however, no assurance can be given that a material adverse change in the results of operations would not occur.

Increased Enforcement Affecting Clinical Research. In addition to increasing enforcement of laws governing payment and reimbursement, the federal government has also stepped up enforcement of laws and regulations governing the conduct of clinical trials at hospitals. DHHS elevated and strengthened its Office of

Human Research Protection, one of the agencies with responsibilities for monitoring federally-funded research. In addition, the National Institutes of Health significantly increased the number of facility inspections that these agencies perform. The Food and Drug Administration (“FDA”) also has authority over the conduct of clinical trials performed in hospitals when these trials are conducted on behalf of sponsors seeking FDA approval to market the drug or device that is the subject of the research. The FDA’s inspection of facilities increased significantly in recent years. These agencies’ enforcement powers range from substantial fines and penalties to exclusions of researchers and suspension or termination of entire research programs. Management of the Corporation believes that clinical research being conducted by any of the Members of the Obligated is in substantial compliance with material applicable requirements, but no assurance can be made that the FDA will not take a contrary position and that such position will not have a material adverse effect on the future operations or financial condition of the Obligated Group.

Nonprofit Health Care Environment

The Corporation and the Foundation are nonprofit tax-exempt organizations, subject to federal, State and local laws, regulations, rulings and court decisions relating to their organization and operation, including their operation for charitable purposes. At the same time, hospitals conduct complex business transactions and typically are one of the major employers in their geographic area. There can often be a tension between the rules designed to regulate a wide range of charitable organizations and the day-to-day operations of a health care organization.

Recently, an increasing number of the operations or practices of health care providers have been challenged or questioned to determine if they are consistent with the regulatory requirements for nonprofit tax-exempt organizations. These challenges, in some cases, are broader than concerns about compliance with federal and state statutes and regulations, such as Medicare and Medi-Cal compliance, and instead in many cases are examinations of core business practices of the health care organizations. Areas which have come under examination have included pricing practices, billing and collection practices, charitable care, executive compensation, excess benefit transactions with insiders, exemption of property from real property taxation, and others. These challenges and questions have come from a variety of sources, including state attorneys general, the IRS, state taxing authorities, labor unions, Congress, state legislatures, and patients, and in a variety of forums, including hearings, audits and litigation. These challenges or examinations include the following, among others:

Congressional Hearings. The House Committee on Energy and Commerce (the “House Committee”) has launched a nationwide investigation of hospital billing practices and prices charged to uninsured patients. A number of large hospital and health care systems were requested by the House Committee to provide detailed historical charge and billing practice information for acute care services. The Subcommittee on Oversight and Investigations of the House Committee conducted hearings in the summer of 2004 at which a number of representatives of the health care industry and others testified.

In April 2005, the House Committee requested additional information from the hospital industry regarding how hospital charges are communicated to patients and how hospital charge masters may affect the prices paid by patients and other payers. It is uncertain if the House Committee will recommend legislative changes as a result of its inquiry.

In addition, the Senate Finance Committee (the “Senate Committee”) conducted hearings on required reforms to the nonprofit sector in the summer of 2004. At the hearings, the Senate Committee released a staff discussion draft on proposals for reform in the area of tax-exempt organizations, including a proposal for a five-year review of tax-exempt status by the IRS. The Senate Committee has also requested information from a number of nonprofit hospitals and health care systems regarding their charitable activities, patient billing and ventures with for-profit corporations and hospitals. During March and September 2006, the Senate Committee conducted additional hearings. In April 2007, Senator Charles Grassley, the ranking member of the Senate Committee, asked the Government Accountability Office (the “GAO”) to formally undertake a study on how nonprofit hospitals meet the community benefit standard in exchange for their tax-exempt status. It is uncertain what actions, if any, the Senate Committee will take as a result of their inquiries, hearings or the GAO study.

In 2005, the House Committee on Ways and Means held hearings to examine the tax-exempt sector and hospital tax-exemption. On December 11, 2006, the Chairman of the House Committee on Ways and Means

introduced charity care legislation requiring that non-profit hospitals provide statutorily mandated amounts of charity care. The bill, H.R. 6420 (Tax Exempt Hospitals Responsibility Act of 2006) provided for the payment of penalties and excise taxes if a non-profit hospital failed to meet the requirements. Although this bill never became law, legislation similar to this could be introduced and passed into law which could have a material adverse impact on a hospital's operations, financial condition and results of operations. The effect of any such legislation, if enacted, cannot be determined at this time.

IRS Examination of Compensation Practices. In August 2004, the IRS announced a new effort to identify and halt abuses by tax-exempt organizations that pay excessive compensation and benefits to their officers and other insiders. The IRS announced that it would contact nearly 2,000 charities and foundations to seek more information about their compensation practices and procedures. This examination project is ongoing. On November 7, 2006, the IRS released its 2007 Exempt Organizations Implementing Guidelines. These guidelines include the 2007 Priority Guidance Plan which sets forth the IRS' goals and strategies for 2007. Among the identified "critical initiatives" for 2007 are executive compensation and tax-exempt hospitals.

California Attorney General. California nonprofit corporations, including the Corporation and the Foundation, are subject at all times to examination by the California Attorney General (the "AG") to ensure that the purposes of the nonprofit corporations are being carried out. The AG has, in recent years, made inquiries regarding the billing practices of nonprofit hospitals. It is unclear whether these inquiries represent an increased interest or scrutiny by the AG of hospital billing practices generally, or whether the AG will extend its inquiry to other nonprofit hospital issues. The California Attorney General has also increased its scrutiny of California nonprofit corporations with the passage of the California Nonprofit Integrity Act, effective January 1, 2005.

California Legislative Hearings. On December 7, 2005, the Chair of the California Assembly Committee on Revenue and Taxation held an oversight hearing to look at tax benefits received by nonprofit hospitals operating in California in parallel and in conjunction with the efforts of legislative committees at the federal, and local levels. The Chair of the Committee stated that the Committee desires to conduct a detailed examination of a variety of topics, including charity care, executive compensation, billing and pricing practices, treatment of the uninsured, tax-exempt status, for-profit affiliations, financial performance and related matters. It is uncertain whether the Committee will recommend legislative changes as a result of its inquiries.

Litigation Relating to Billing and Collection Practices. Lawsuits have been filed in both federal and state courts alleging, among other things, that hospitals have failed to fulfill their obligations to provide charity care to uninsured patients, have overcharged uninsured patients and have engaged in predatory collection practices. The cases are proceeding in various courts around the country with inconsistent results. While it is not possible to make general predictions, some hospitals have entered into substantial settlements.

Challenges to Real Property Tax Exemptions. Recently, the real property tax exemptions afforded to certain nonprofit health care providers by state and local taxing authorities have been challenged on the grounds that the health care providers were not engaged in sufficient charitable activities. These challenges have been based on a variety of grounds, including allegations of aggressive billing and collection practices and excessive financial margins.

Actions by Purchasers of Hospital Services and Consumers. Major purchasers of hospital services could take action to restrain hospital charges or charge increases. The California Public Employees' Retirement System, the nation's third largest purchaser of employee health benefits, has pledged to take action to restrain the rate of growth of hospital charges and has excluded certain California hospitals from serving its covered members. As a result of increased public scrutiny, it is also possible that the pricing strategies of hospitals may be perceived negatively by consumers, and hospitals may be forced to reduce fees for their services. Decreased utilization could result, and hospitals' revenues may be negatively impacted.

The foregoing are some examples of the challenges and examinations facing nonprofit health care organizations. The challenges and examinations and any resulting legislation, regulations, judgments, or penalties could have a material adverse effect on the ability of the Obligated Group to pay the Bonds.

Negative Rankings Based on Clinical Outcomes, Cost, Quality, Patient Satisfaction and Other Performance Measures. Health plans, Medicare, Medi-Cal, employers, trade groups and other purchasers of health services, private standard-setting organizations and accrediting agencies, increasingly are using statistical and other measures in efforts to characterize, publicize, compare, rank and change the quality, safety and cost of health care services provided by hospitals and physicians. Published rankings such as “score cards,” tiered hospital networks with higher co-payments and deductibles for non-emergent use of lower-ranked providers, “pay for performance” and other financial and non-financial incentive programs are being introduced to affect the reputation and revenue of hospitals and the members of their medical staffs and to influence the behavior of consumers and providers such as the Corporation. Prevalent currently are measures of quality based on clinical outcomes of patient care, reduction in costs, patient satisfaction, and investment in health information technology. Measures of performance set by others that characterize a hospital negatively may adversely affect its reputation and financial condition.

Regulatory Environment

“Fraud” and “False Claims.” Health care “fraud and abuse” laws have been enacted at the federal and state levels to broadly regulate the provision of services to government program beneficiaries and the methods and requirements for submitting claims for services rendered to the beneficiaries. Under these laws, hospitals and others can be penalized for a wide variety of conduct, including submitting claims for services that are not provided, billing in a manner that does not comply with government requirements or including inaccurate billing information, billing for services deemed to be medically unnecessary, “up-coding,” or billings accompanied by an illegal inducement to utilize or refrain from utilizing a service or product.

Federal and state governments have a broad range of criminal, civil and administrative sanctions available to penalize and remediate health care fraud, including, without limitation, the exclusion of a hospital from participation in the Medicare/Medicaid programs, imprisonment, civil monetary penalties, and suspension of Medicare/Medicaid payments. Fraud cases may be prosecuted by one or more government entities and/or private individuals, and more than one of the available sanctions may be, and often are, imposed for violations.

Laws governing fraud and abuse may apply to hospitals and other health care providers, and to nearly all individuals and entities with which a hospital or other health care provider does business. Fraud investigations, settlements, prosecutions and related publicity can have a catastrophic effect on hospitals and other health care providers. See “Enforcement Activity” below. Major elements of these often highly technical laws and regulations are generally summarized below.

Criminal Fraud and Abuse Liability. Both individuals and organizations are subject to prosecution under the criminal fraud and abuse statutes. Criminal conviction for an offense may result in substantial fines and/or the provider’s exclusion and debarment from all government programs.

Criminal False Claims Act. The criminal False Claims Act or Criminal FCA prohibits anyone from knowingly submitting a false, fictitious or fraudulent claim to the federal government. There are numerous specific rules that a health care provider must follow with respect to the submission of claims. Violation of the Criminal FCA can result in imprisonment of five years and a fine of up to \$250,000 for an individual or \$500,000 for an organization.

Anti-Kickback Law. The federal “Anti-Kickback Law” is a criminal statute that prohibits anyone from soliciting, receiving, offering or paying any remuneration, directly or indirectly, overtly or covertly, in cash or in kind, in return for a referral (or to induce a referral) for any item or service that may be paid by any federal or state health care program. The Anti-Kickback Law applies to many common health care transactions between persons and entities with which a hospital or health care system does business, including hospital-physician joint ventures, hospital-physician integration vehicles (such as a medical foundation), medical director agreements, physician recruitment agreements, physician office leases, purchases from vendors, and other transactions.

Violation or alleged violation of the Anti-Kickback Law can result in settlements that require multi-million dollar payments and compliance agreements. The Anti-Kickback Law can be prosecuted either criminally or civilly. Each violation is a felony, subject to a fine of up to \$25,000 for each act (which may be each item or each bill sent to a federal program), imprisonment and/or exclusion from the Medicare and Medicaid programs. This fine may be

increased to \$250,000 for individuals and \$500,000 for organizations. In addition, civil monetary penalties of \$10,000 per item or service in noncompliance (which may be each item or each bill sent to a federal program) or an “assessment” of three times the amount claimed may be imposed.

Civil Fraud and Abuse Liability. Unlike criminal statutes, which require the government to prove that the health care provider intended to violate the law, civil statutes may be violated simply by the provider’s participation in a prohibited financial arrangement or the provider having knowledge that its claims procedures are not in full compliance with the law.

Civil False Claims Act. The civil False Claims Act, or Civil FCA makes it illegal to submit or present a false, fictitious or fraudulent claim to the federal government, and may include claims that are simply erroneous. Civil FCA investigations and cases have become common in the health care field and may cover a range of activity from intentionally inflated billings, to highly technical billing infractions, to allegations of inadequate care. Violation or alleged violation of the Civil FCA can result in settlements that require multi-million dollar payments and compliance agreements. The Civil FCA also permits individuals to initiate civil actions on behalf of the government in lawsuits called “qui tam” actions. Qui tam plaintiffs, or “whistleblowers,” can share in the damages recovered by the government or recover independently if the government does not participate. The Civil FCA has become one of the government’s primary weapons against health care fraud. Civil FCA violations or alleged violations could lead to settlements, fines, exclusion or reputation damage that could have a material adverse impact on a hospital or other health care provider.

Stark Referral Law. The federal “Stark” statute prohibits the referral by a physician of Medicare and Medi-Cal patients for certain designated health services (including inpatient and outpatient hospital services, clinical laboratory services, and various diagnostic imaging services) to entities with which the referring physician has a financial relationship. It also prohibits a hospital or other health care provider furnishing the designated services from billing Medicare, Medi-Cal or any other payor or individual, for services performed pursuant to a prohibited referral. The government does not need to prove that the entity knew that the referral was prohibited to establish a Stark violation. Many ordinary business practices and economically desirable arrangements between physicians and hospitals or other health care providers arguably constitute “financial relationships” within the meaning of the Stark statute. The prohibition on referrals and billing would be triggered by the financial relationship unless the relationship fully complied with one of several exceptions. Most providers of the designated health services with physician relationships have some exposure to liability under the Stark statute.

Medicare may deny payment for all services related to a prohibited referral and a hospital or other health care provider that has billed for prohibited services may be obligated to refund the amounts collected from the Medicare program. For example, if an office lease between a hospital and a large group of heart surgeons is found to violate Stark, a hospital could be obligated to repay CMS for the payments received from Medicare for all of the heart surgeries performed by all of the physicians in the group for the duration of the lease; a potentially significant amount. The government may also seek substantial civil monetary penalties, and in some cases, a hospital or other health care provider may be liable for fines up to three times the amount of any monetary penalty, and/or be excluded from the Medicare and Medi-Cal programs. Potential repayments to CMS, settlements, fines or exclusion for a Stark violation or alleged violation could have a material adverse impact on a hospital or other health care provider.

Civil Monetary Penalties Law. The federal Civil Monetary Penalties Law (“CMPL”) provides for administrative sanctions against health care providers for a broad range of billing and other abuses. A health care provider is liable under the CMPL if it knowingly presents, or causes to be presented, improper claims for reimbursement to a federal or state agency, such as those that administer the Medicare and Medicaid programs. A hospital that participates in arrangements known as “gainsharing,” through which the hospital pays physicians to limit or reduce services to Medicare fee-for-service beneficiaries, also may be subject to substantial civil monetary penalties.

A health care provider may be found liable under the CMPL even if it did not have actual knowledge of the impropriety of the claim. It is sufficient that the provider “should have known” that the claim was false. Ignorance of the Medicare or Medicaid regulations is no defense. The Secretary of DHHS, acting through the OIG, also has

both mandatory and permissive authority to exclude individuals and entities from participation in federal health care programs pursuant to this statute.

HIPAA. The Health Insurance Portability and Accountability Act of 1996, or HIPAA, adds additional criminal sanctions through its “accountability” provisions for health care fraud and applies to all health care benefit programs, whether public or private. HIPAA also provides for punishment of a health care provider for knowingly and willfully embezzling, stealing, converting or intentionally misapplying any money, funds or other assets of a health care benefit program. A health care provider convicted of health care fraud also could be excluded from Medicare. In addition, HIPAA includes “administrative simplification” provisions that require standardization of electronic transactions, specific security protections for electronic medical information and processes, privacy protections for patient health information, and establishment of national employer and provider identifiers. DHHS and CMS have promulgated rules related to electronic transactions, national employer identifiers, national provider identifiers, security, and medical records privacy. Rules regarding national health plan identifiers, claims attachments standards and first report of injury standards have been published in proposed form or are under development.

These new rules required the implementation of new policies and procedures by health care providers for coding, maintaining, storing and transmitting medical information, as well as policies and procedures designed to protect the security of electronic medical information and the confidentiality of all medical information and to permit patients to exercise their specific rights under HIPAA. The Corporation was required to comply with HIPAA’s privacy standards by April 14, 2003. Compliance with the security standards was required by April 20, 2005, where health care providers had to implement administrative, physical and technical safeguards to protect the confidentiality, integrity and availability of electronic protected health information. The Corporation has made significant expenditures to date and anticipates the need for substantial additional expenditures to ensure compliance with all of these requirements. The Corporation was in compliance with the National Provider Identifier standards by May 23, 2007, the date on which such compliance was required.

The penalty for violating HIPAA’s administrative simplification requirements includes imposition of civil monetary penalties of not more than \$100 per person, per violation up to a maximum of \$25,000 for violation of the same standard within any calendar year. Criminal penalties may also be imposed on any person who knowingly obtains or discloses protected health information in violation of HIPAA. These penalties range from up to \$50,000 and one year in prison for knowingly obtaining or disclosing protected health information in violation of the administrative simplification requirements; up to \$100,000 and up to five years in prison for knowingly obtaining or disclosing protected health information under “false pretenses;” and up to \$250,000 and up to 10 years in prison for knowingly obtaining protected health information with the intent to sell, transfer or use it for commercial advantage, personal gain or malicious harm. The Secretary of DHHS and the Secretary’s designees have the authority to conduct compliance reviews to determine whether any covered entity is complying with HIPAA requirements, and to investigate complaints filed by any person who believes a covered entity is not complying with those requirements. However, HIPAA requires the Secretary of DHHS, to the extent practicable, to seek cooperation in obtaining compliance prior to formal action for civil monetary or criminal penalties. Except for the privacy rule, which is enforced by the Office for Civil Rights of DHHS, the standards promulgated pursuant to HIPAA’s administrative simplification provisions are enforced by CMS.

Exclusions from Medicare or Medi-Cal Participation. The government may exclude from Medicare/Medicaid program participation a hospital that is convicted of a criminal offense relating to the delivery of any item or service reimbursed under Medicare or a state health care program, any criminal offense relating to patient neglect or abuse in connection with the delivery of health care, fraud against any federal, state or locally financed health care program, or an offense relating to the illegal manufacture, distribution, prescription, or dispensing of a controlled substance. The government also may exclude individuals or entities under certain other circumstances, such as an unrelated conviction of fraud, or other financial misconduct relating either to the delivery of health care in general or to participation in a federal, state or local government program. Exclusion from the Medicare and Medi-Cal programs means that a hospital would be decertified and no program payments would be made. Any hospital exclusion could be a materially adverse event.

Administrative Enforcement. Administrative regulations may require less proof of a violation than do criminal laws, and, thus, health care providers may have a higher risk of imposition of monetary penalties as a result of administrative enforcement actions.

Compliance with Conditions of Participation. CMS, in its role of monitoring participating providers' compliance with conditions of participation in the Medicare program, may determine that a provider is not in compliance with its conditions of participation. If not corrected, a termination of participation in the Medicare or Medicaid program could be imposed.

Enforcement Activity. Enforcement activity against hospitals and health care providers has increased and enforcement authorities have adopted aggressive approaches. Hospitals and other health care providers are frequently subject to audits, investigations or other enforcement actions regarding the health care fraud laws mentioned above. In addition, enforcement agencies increasingly pursue sanctions for violations of health care fraud and abuse laws through civil administrative actions. Administrative regulations may require less proof of a violation than do criminal laws and, thus, health care providers may have a higher risk of imposition of monetary penalties as a result of administrative enforcement actions.

Enforcement authorities are often in a position to compel settlements by providers charged with or being investigated for false claims violations by withholding or threatening to withhold Medicare, Medi-Cal and/or similar payments and/or by instituting criminal action. In addition, the cost of defending such an action, the time and management attention consumed, and the facts of a case may dictate settlement. Therefore, regardless of the merits of a particular case, a hospital or other health care provider could experience materially adverse settlement costs, as well as materially adverse costs associated with implementation of any settlement agreement. Prolonged and publicized investigations could be damaging to the reputation and business of a hospital or other health care provider, regardless of outcome.

Certain acts or transactions may result in violation or alleged violation of a number of the federal health care fraud laws described above and, therefore, penalties or settlement amounts can be compounded. Generally, these risks are not covered by insurance. Enforcement actions may involve multiple hospitals or health care providers in a health system, as the government often extends enforcement actions regarding health care fraud to other hospitals or health care providers in the same organization. Therefore, Medicare fraud related risks identified as being materially adverse as to a hospital or other health care provider could have materially adverse consequences to a health system taken as a whole.

Liability Under State "Fraud" and "False Claims" Laws. Hospitals and other health care providers in California also are subject to state laws related to false claims, anti-kickback, and physician referrals, which pose the possibility of material adverse impact for the same reasons as the federal statutes. In addition, in contrast to federal laws which typically apply only to services rendered to beneficiaries covered under federal or state health care financing programs, these state laws typically apply to services rendered to any patients, regardless of the source of payment for such services.

EMTALA. The Emergency Medical Treatment and Active Labor Act, or EMTALA, is a federal civil statute that requires hospitals to conduct a medical screening for emergency conditions and to stabilize a patient's emergency medical condition before releasing, discharging or transferring the patient. Over the last few years, the federal government has increased its enforcement of EMTALA. A hospital that violates EMTALA is subject to civil penalties of up to \$50,000 per offense and exclusion from Medicare and Medi-Cal programs. In addition, a hospital may be liable for any claim by an individual who has suffered harm as a result of a violation of EMTALA.

Licensing, Surveys, Investigations and Audits. Health facilities are subject to numerous legal, regulatory, professional and private licensing, certification and accreditation requirements. These include, but are not limited to, requirements of state licensing agencies and The Joint Commission. Renewal and continuation of certain of these licenses, certifications and accreditations are based on inspections or other reviews generally conducted in the normal course of business of health facilities. Loss of, or limitations imposed on, hospital licenses could reduce hospital utilization or revenues, or a hospital's ability to operate all or a portion of its facilities.

Renewal and continuance of certain of these licenses, certifications and accreditations are based on inspections, surveys, audits, investigations or other reviews, some of which may require or include affirmative action or response by the Corporation. These activities generally are conducted in the normal course of business of health facilities. Nevertheless, an adverse result could result in a loss or reduction in the Corporation's scope of licensure, certification or accreditation, or could reduce the payment received or require repayment of amounts previously remitted.

Environmental Laws and Regulations. Hospitals are subject to a wide variety of federal, state and local environmental and occupational health and safety laws and regulations. These include, but are not limited to: air and water quality control requirements; waste management requirements; specific regulatory requirements applicable to asbestos and radioactive substances; requirements for providing notice to employees and members of the public about hazardous materials handled by or located at the hospital; and requirements for training employees in the proper handling and management of hazardous materials and wastes.

Health facilities may be subject to requirements related to investigating and remedying hazardous substances located on their property, including such substances that may have migrated off the property. Typical hospital operations include the handling, use, storage, transportation, disposal and/or discharge of hazardous, infectious, toxic, radioactive, flammable and other hazardous materials, wastes, pollutants and contaminants. As such, hospital operations are particularly susceptible to the practical, financial and legal risks associated with the environmental laws and regulations. Such risks may result in damage to individuals, property or the environment; may interrupt operations and/or increase their cost; may result in legal liability, damages, injunctions or fines; and may result in investigations, administrative proceedings, civil litigation, criminal prosecution, penalties or other governmental agency actions; and may not be covered by insurance.

Business Relationships and Other Business Matters

Integrated Physician Groups. Hospitals and health systems often own, control or have affiliations with relatively large physician groups. See Appendix A – “INFORMATION CONCERNING THE OBLIGATED GROUP—INTRODUCTION.” Generally, the sponsoring hospital or health system will be the primary capital and funding source for such alliances and may have an ongoing financial commitment to provide growth capital and support operating deficits.

These types of alliances are generally designed to respond to trends in the delivery of medicine to better integrate hospital and physician care, to increase physician availability to the community, and/or to enhance the managed care capability of the affiliated hospitals and physicians. However, these goals may not be achieved, and an unsuccessful alliance may be costly and counterproductive to all of the above-stated goals.

Integrated delivery systems carry with them the potential for legal or regulatory risks in varying degrees. The ability of hospitals or health systems to conduct integrated physician operations may be altered or eliminated in the future by legal or regulatory interpretation or changes, or by health care fraud enforcement. In addition, participating physicians may seek their independence for a variety of reasons, thus putting the hospital's or health system's investment at risk, and potentially reducing its managed care leverage and/or overall utilization.

Hospital Pricing. Inflation in hospital costs may evoke action by legislatures, payors or consumers. It is possible that legislative action at the state or national level may be taken with regard to the pricing of health care services.

Indigent Care. Tax-exempt hospitals often treat large numbers of indigent patients who are unable to pay in full for their medical care. Typically, pediatric hospitals may treat significant numbers of indigent patients. These hospitals may be susceptible to economic and political changes that could increase the number of indigent patients or their responsibility for caring for this population. General economic conditions that affect the number of employed individuals who have health coverage affect the ability of persons financial responsible for pediatric patients to pay for their care. Similarly, changes in governmental policy, which may result in coverage exclusions under local, state and federal health care programs (including Medicare and Medicaid) may increase the frequency and severity of indigent treatment by such hospitals and other providers. It also is possible that future legislation

could require that tax-exempt hospitals and other providers maintain minimum levels of indigent care as a condition to federal income tax exemption or exemption from certain state or local taxes.

Physician Medical Staff. The primary relationship between a hospital and physicians who practice in it is through the hospital's organized medical staff. Medical staff bylaws, rules and policies establish the criteria and procedures by which a physician may have his or her privileges or membership curtailed, denied or revoked. Physicians who are denied medical staff membership or certain clinical privileges or who have such membership or privileges curtailed or revoked often file legal actions against hospitals and medical staffs. Such actions may include a wide variety of claims, some of which could result in substantial uninsured damages to a hospital. In addition, failure of the hospital governing body to adequately oversee the conduct of its medical staff may result in hospital liability to third parties.

An emerging area of potential risk for all hospitals surrounds the appropriate management of physician conflicts of interest with hospitals that grant practice privileges. Described as "economic credentialing" by physicians who oppose efforts of hospitals to manage the presence of direct competitors within the leadership or boardroom, the issue requires all hospitals to thoughtfully manage these potential conflicts to maintain a healthy, collegial and professional relationship required with the independent medical staff, while ensuring the organization is not suffering irreversible harm from a competitor gaining specific or specialized information not available to the public regarding the Corporation's plans. In the worst circumstances, such efforts have led to litigation and potentially material effects on the practice patterns of physicians at a specific facility. It is not possible to predict the course of such decisions or make any assurances that the Corporation will be successful in managing such conflicts without causing some changes in physician practice patterns, which could have a material effect on the Corporation.

Physician Supply. Sufficient community-based physician supply is important to hospitals and health systems. The State annually reviews overall physician reimbursement formulas under Medi-Cal. Changes to physician compensation formulas could lead to physicians locating their practices in communities with lower Medi-Cal populations. Hospitals and health systems may be required to invest additional resources for recruiting and retaining physicians, or may be required to increase the percentage of employed physicians in order to continue serving the growing population base and maintain market share.

Competition. Increased competition from a wide variety of sources, including specialty hospitals, other hospitals and health care systems, inpatient and outpatient health care facilities, long-term care and skilled nursing facilities, clinics, physicians and others, may adversely affect the utilization and revenues of hospitals. Existing and potential competitors may not be subject to various restrictions applicable to hospitals, and competition, in the future, may arise from new sources not currently anticipated or prevalent.

Specialty hospital developments that attract away an important segment of an existing hospital's admitting specialists may be particularly damaging. For example, some large hospitals may have significant dependence on cardiovascular and/or orthopedic surgery programs, as revenue streams from those programs may cover significant fixed overhead costs. If a significant number of such a hospital's cardiovascular or orthopedic surgeons develop their own specialty hospital (alone or in conjunction with a growing number of specialty hospital operators and promoters), taking with them their patient base, a hospital could experience a rapid and dramatic decline in net revenues that is not proportionate to the number of patient admissions or patient days lost. It is also possible that the competing specialty hospital, as a for-profit venture, would not accept indigent patients or other payors and government programs, leaving low-pay patient populations in the full-service hospital. In certain cases, such an event could be materially adverse to a hospital.

Likewise, freestanding ambulatory surgery centers may attract away significant commercial outpatient services traditionally performed at hospitals. Commercial outpatient services, currently among the most remunerative for hospitals, may be lost to competitors who can provide these services in an alternative, less costly setting. Full-service hospitals rely upon the revenues generated from commercial outpatient services to fund other less remunerative services, and the decline of such business may result in a significant reduction in income. Competing ambulatory surgery centers, more likely a for-profit business, may not accept indigent patients or low paying programs and would leave these populations to receive services in the hospital setting. Consequently, hospitals are vulnerable to competition from ambulatory surgery centers.

Additionally, scientific and technological advances, new procedures, drugs and devices, preventive medicine and outpatient health care delivery may reduce utilization and revenues of a hospital in the future or otherwise lead the way to new avenues of competition. In some cases, hospital investment in facilities and equipment for capital-intensive services may be lost as a result of rapid changes in diagnosis, treatment or clinical practice brought about by new technology or new pharmacology.

Private Health Care Plans and Managed Care. The Corporation contracts with several third party payors. For the fiscal years ended December 31, 2004, 2005 and 2006, non-governmental payors accounted for approximately 53.3%, 52.3% and 52.7%, respectively, of the total net patient service revenue of the Corporation. For the five-month periods ended May 31, 2006 and 2006, non-governmental payors accounted for approximately 50.1% and 56.0%, respectively, of the total net patient services revenue of the Corporation.

E-Medicine. The growth of e-commerce also may result in a shift in the way that health care is delivered. Persons residing in the Corporation's service areas may be able to receive certain health services from remote providers. For example, physicians will be able to provide certain services over the internet (e.g., teleradiology and second opinions). Pharmaceuticals and other health services may also now be ordered on-line. Additionally, other service providers may now compete with the Corporation through this new medium by advertising their services and providing easy registration for competing services over the internet. Also, alternative forms of health care payment including managed care organizations and consumer-driven care, as well as expanded preventive medicine and outpatient treatment, could affect the Corporation's ability to maintain their market share at current levels.

Technology. Scientific and technological advances, new procedures, drugs and devices, preventive medicine, occupational health and safety, and outpatient health care delivery may reduce utilization and revenues of the Corporation in the future. Technological advances in recent years have accelerated the trend toward the use by hospitals of sophisticated and costly equipment and services, and the Corporation may have to incur significant costs to acquire the equipment needed to maintain or enhance their competitive position. Recently, President Bush called for the establishment of a nationwide electronic medical records system over the next 10 years and created a national health information technology office within DHHS to lead the effort. The costs to acquire and implement an electronic medical records system are significant but it is widely believed that such systems will lead to greater efficiencies in the provision of patient care and improved quality of care. The acquisition and operation of certain equipment and services may continue to be a significant factor in hospital utilization, but the ability of the Corporation to offer such equipment or services may be subject to the availability of equipment and specialists, governmental approval and the ability to finance such acquisitions and operations.

Antitrust. Antitrust liability may arise in a wide variety of circumstances, including medical staff privilege disputes, payor contracting, physician relations, joint ventures, merger, affiliation and acquisition activities, certain pricing or salary setting activities, and anticompetitive business conduct or practices. The application of the federal and state antitrust laws to health care is evolving, and therefore not always clear. Currently, the most common areas of potential liability for hospitals and other health care providers are joint action among providers with respect to payor contracting, medical staff credentialing disputes and anticompetitive business conduct or practices by hospitals and other health care providers with sufficiently large market share.

Violation of the antitrust laws could result in criminal and/or civil enforcement proceedings by federal and state agencies, as well as actions by private litigants. In certain actions, private litigants may be entitled to treble damages, and in others, governmental entities may be able to assess substantial monetary fines. Moreover, successful private or governmental litigants may obtain injunctive relief that can adversely affect the defendant's ability to conduct or continue certain business practices or activities.

Labor Relations and Collective Bargaining. Hospitals are large employers with a wide diversity of employees. Increasingly, employees of hospitals are becoming unionized, and many hospitals have collective bargaining agreements with one or more labor organizations. Employees subject to collective bargaining agreements may include essential nursing and technical personnel, as well as food service, maintenance and other trade personnel. Renegotiation of such agreements upon expiration may result in significant cost increases to hospitals. Employee strikes or other adverse labor actions may have an adverse impact on operations, revenue and hospital reputation. Certain employees of the Corporation currently are covered by collective bargaining

agreements. See APPENDIX A – “INFORMATION CONCERNING THE OBLIGATED GROUP - OTHER INFORMATION--Employees and Labor Relations.”

Wage and Hour Class Actions and Litigation. Federal law and many states impose standards related to worker classification, eligibility and payment for overtime, liability for providing rest periods and similar requirements. Large employers with complex workforces, such as hospitals, are susceptible to actual and alleged violations of these standards. In recent years there has been a proliferation of lawsuits over these “wage and hour” issues, often in the form of large, sometimes multi-state, class actions. For large employers such as hospitals, such class actions can involve multi-million dollar claims, judgments and/or settlements. A major class action decided or settled adversely to the Obligated Group could have a material adverse impact on Members' financial conditions and results of operations.

Health Care Worker Classification. Health care providers, like all businesses, are required to withhold income taxes from amounts paid to employees. If the employer fails to withhold the tax, the employer becomes liable for payment of the tax imposed on the employee, plus interest and potentially penalties. On the other hand, businesses are not required to withhold federal taxes from amounts paid to a worker classified as an independent contractor. The IRS and State Authorities have established criteria for determining whether a worker is an employee or an independent contractor for tax purposes. If these agencies were to reclassify a significant number of hospital independent contractors as employees, back taxes and penalties could be material.

Staffing. In recent years, the health care industry has suffered from a scarcity of nursing personnel, respiratory therapists, pharmacists and other trained health care technicians. A significant factor underlying this trend includes a decrease in the number of persons entering such professions. This is expected to intensify in the future, aggravating the general shortage and increasing the likelihood of hospital-specific shortages. Competition for employees, coupled with increased recruiting and retention costs will increase hospital operating costs, possibly significantly, and growth may be constrained. This trend could have a material adverse impact on the financial conditions and results of operations of hospitals.

Effective January 1, 2004, California implemented mandatory nurse staffing ratios for all hospital patient care areas. In January 2005, these standards were made more stringent. The impact on California hospitals will vary by facility. The required staffing, in aggregate, is more costly than prior staffing patterns. See Appendix A – “INFORMATION CONCERNING THE OBLIGATED GROUP—OTHER INFORMATION—Nursing Staff.”

Professional Liability Claims, Property and General Liability Insurance. In recent years, the number of professional and general liability suits and the dollar amounts of damage recoveries have increased in health care nationwide, resulting in substantial increases in malpractice insurance premiums, higher deductibles and generally less coverage. Professional liability and other actions alleging wrongful conduct and seeking punitive damages are often filed against health care providers. Insurance does not provide coverage for judgments for punitive damages.

Litigation also arises from the corporate and business activities of hospitals, from a hospital's status as an employer or as a result of medical staff or provider network peer review or the denial of medical staff or provider network privileges. As with professional liability, many of these risks are covered by insurance, but some are not. For example, some antitrust claims or business disputes are not covered by insurance or other sources and may, in whole or in part, be a liability of an Obligated Group Member if determined or settled adversely.

Hospital property can be damaged by events and forces beyond a hospital's control. Hospitals generally maintain property and casualty insurance in some combination of purchased, self-insurance and re-insurance policies to cover property damage.

There is no assurance that hospitals will be able to maintain coverage amounts currently in place in the future, that the coverage will be sufficient to cover judgments or claims rendered against a hospital or that such coverage will be available at a reasonable cost in the future.

Tax-Exempt Status and Other Tax Matters

Maintenance of the Tax-Exempt Status of the Obligated Group Members. The tax-exempt status of the Bonds depends upon maintenance by each Obligated Group Member that receives or benefits from the proceeds of the Bonds (the “Benefiting Member”) of its status as an organization described in Section 501(c)(3) of the Code. The maintenance of such status is contingent on compliance with general rules promulgated in the Code and related regulations regarding the organization and operation of tax-exempt entities, including their operation for charitable purposes and their avoidance of transactions that may cause their earnings or assets to inure to the benefit of private individuals. As these general principles were developed primarily for charities that do not conduct large-scale technical operations and business activities, they often do not adequately address the myriad operations and transactions entered into by a modern health care organization. Although traditional activities of health care providers, such as medical office building leases, have been the subject of interpretations by the IRS in the form of Private Letter Rulings, many activities or categories of activities have not been fully addressed in any official opinion, interpretation or policy of the IRS.

The IRS has periodically conducted audit and other enforcement activities regarding tax-exempt health care organizations. The IRS conducts special audits of large tax-exempt health care organizations with at least \$500 million in assets or \$1 billion in gross receipts. Such audits are conducted by teams of revenue agents, often take years to complete and require the expenditure of significant staff time by both the IRS and taxpayers. These audits examine a wide range of possible issues, including tax-exempt bond financing of partnerships and joint ventures, retirement plans and employee benefits, employment taxes, political contributions and other matters.

If the IRS were to find that an Obligated Group Member has participated in activities in violation of certain regulations or rulings, the tax-exempt status of such entity could be in jeopardy. Although the IRS has not frequently revoked the 501(c)(3) tax-exempt status of nonprofit health care hospitals, it could do so in the future. Loss of tax-exempt status by the Members of the Obligated Group potentially could result in loss of tax exemption of amounts treated for federal income tax purposes as interest payments with respect to the Bonds and of other tax-exempt debt of the Obligated Group Members, and defaults in covenants regarding the Bonds and other related tax-exempt debt and obligations likely would be triggered. Loss of tax-exempt status also could result in substantial tax liabilities on income of the Obligated Group.

In some cases, the IRS has imposed substantial monetary penalties on tax-exempt hospitals in lieu of revoking their tax-exempt status. In those cases, the IRS and exempt hospitals entered into settlement agreements requiring the hospital to make substantial payments to the IRS.

In lieu of revocation of exempt status, the IRS may impose penalty excise taxes on certain “excess benefit transactions” involving 501(c)(3) organizations and “disqualified persons.” An excess benefit transaction is one in which a disqualified person or entity receives more than fair market value from the exempt organization or pays the exempt organization less than fair market value for property or services, or shares the net revenues of the tax-exempt entity. A disqualified person is a person (or an entity) who is in a position to exercise substantial influence over the affairs of the exempt organization during the five years preceding an excess benefit transaction. The statute imposes excise taxes on the disqualified person and any “organization manager” who knowingly participates in an excess benefit transaction. These rules do not penalize the exempt organization itself, so there would be no direct impact on an Obligated Group Member or amounts treated for federal income tax purposes as interest payments with respect to the Bonds if an excess benefit transaction were subject to IRS enforcement, pursuant to these “intermediate sanctions” rules. However, the payment of these taxes would become public record and could adversely affect the Corporation's reputation and therefore its ability to successfully conduct future fundraising activities.

State and Local Tax Exemption. Until recently, the State has not been as active as the IRS in scrutinizing the income tax exemption of health care organizations. In California, it is possible that legislation may be proposed to strengthen the role of the California Franchise Tax Board and the Attorney General in supervising nonprofit health systems. It is likely that the loss by any of the Obligated Group Members of federal tax exemption would also trigger a challenge to its state tax exemption. Depending on the circumstances, such event could be material and adverse to that entity and the Obligated Group as a whole.

State, county and local taxing authorities undertake audits and reviews of the operations of tax-exempt health care providers with respect to their real property tax exemptions. In some cases, particularly where authorities are dissatisfied with the amount of services provided to indigents, the real property tax-exempt status of the health care providers has been questioned. The majority of the real property of the Obligated Group is currently treated as exempt from real property taxation. Although the real property tax exemption of the Obligated Group has not, to the knowledge of management, been under challenge or investigation, an audit could lead to a challenge that could adversely affect the real property tax exemption of the Obligated Group.

It is not possible to predict the scope or effect of future legislative or regulatory actions with respect to taxation of nonprofit corporations. There can be no assurance that future changes in the laws and regulations of state or local governments will not materially adversely affect the financial condition of the Obligated Group by requiring payment of income, local property or other taxes.

Future Developments. On May 21, 2007, the United States Supreme Court agreed to review the decision of the Court of Appeals of Kentucky in the matter of *Kentucky v. Davis*, which held that it was a violation of the Commerce Clause of the United States Constitution for the Commonwealth of Kentucky to grant a state income tax exemption to the interest on bonds issued by or on behalf of the Commonwealth of Kentucky and its political subdivisions while subjecting interest on bonds issued by or on behalf of other states and their political subdivisions to Kentucky state income tax. It is not possible to know at this time how the Supreme Court will decide *Kentucky v. Davis*. If the Kentucky decision is affirmed by the United States Supreme Court, states such as the State of California may be required to eliminate the disparity between the income tax treatment of out-of-state bonds and the income tax treatment of in-state bonds, such as bonds issued by the District, including the Bonds. The impact of this decision may also affect the market price for, or the marketability of, the Bonds.

Maintenance of Tax-Exempt Status of Interest with Respect to the Bonds. The Code imposes a number of requirements that must be satisfied for interest with respect to state and local obligations, such as the Bonds, to be excludable from gross income for federal income tax purposes. These requirements include limitations on the use of proceeds, limitations on the investment earnings of proceeds prior to expenditure, a requirement that certain investment earnings on proceeds be paid periodically to the United States Treasury, and a requirement that the Authority file an information report with the IRS. The Corporation has covenanted in the Loan Agreement that it will comply with such requirements. Failure by the Corporation to comply with the requirements stated in the Code and related regulations, rulings and policies may result in the treatment of interest with respect to the Bonds as taxable, retroactively to the date of issuance. The Authority has covenanted in the Bond Indenture that it will not take any action or refrain from taking any action that would cause interest with respect to the Bonds to be included in gross income for federal income tax purposes.

IRS officials have recently indicated that more resources will be invested in audits of tax-exempt bonds in the charitable organization sector, with specific reviews of private use. The Bonds may be, from time to time, subject to audits by the IRS. Management of the Obligated Group believes that the Bonds properly comply with the tax laws. In addition, Bond Counsel will render an opinion with respect to the tax-exempt status of amounts treated for federal income tax purposes as interest payments with respect to the Bonds, as described under the caption "TAX MATTERS." Management of the Obligated Group has not sought to obtain a private letter ruling from the IRS with respect to the Bonds, and the opinion of Bond Counsel is not binding on the IRS. There is no assurance that an IRS examination of the Bonds will not adversely affect the market value of the Bonds. See "TAX MATTERS" herein.

Limitations on Contractual and Other Arrangements Imposed by the Internal Revenue Code. As tax-exempt organizations, the Obligated Group Members are limited with respect to their use of practice income guarantees, reduced rent on medical office space, low-interest loans, joint venture programs and other means of recruiting and retaining physicians. Uncertainty in this area has been reduced somewhat by the issuance by the IRS of guidelines on permissible physician recruitment practices. The IRS scrutinizes a broad variety of contractual relationships commonly entered into by hospitals and has issued a detailed audit guide suggesting that field agents scrutinize numerous activities of the hospitals in an effort to determine whether any action should be taken with respect to limitations on or revocation of their tax-exempt status or assessment of additional tax. Any suspension, limitation, or revocation of one or more Members' tax-exempt status or assessment of significant tax liability would have a materially adverse effect on the Obligated Group and might lead to loss of tax exemption of amounts treated for federal income tax purposes as interest payments with respect to the Bonds.

Interest Rate Swap and Other Hedge Risks

Any interest rate swap or other hedge agreement to which a Member of the Obligated Group is a party may, at any time, have a negative value to such Member. If either a swap or other hedge counterparty or the Member terminates such an agreement when the agreement has a negative value to the Member, the Member would generally be obligated to make a termination payment to the counterparty in the amount of such negative value, and such payment could be substantial and potentially materially adverse to the Member's financial condition. A counterparty may generally only terminate such an agreement upon the occurrence of defined termination events or events of default, such as nonpayment by the Member and any insurer thereof, or in the event rating agencies withdraw or downgrade below a specified level the ratings of the Member and an insurer of the Member's obligation under such an agreement, if any.

The Preexisting Swap Agreement requires the Obligated Group to secure its obligations thereunder in certain circumstances including without limitation a downgrade of the long-term debt issued on behalf of the Corporation. Under the terms of the Preexisting Swap Agreement, no collateral is currently required to be posted. See "THE OBLIGATED GROUP—Interest Rate Agreements" herein. If the Obligated Group is unable to secure its obligations under the Preexisting Swap Agreement with sufficient collateral, MLCS will have the right to terminate the Preexisting Swap Agreement, and the Obligated Group could be required to make a termination payment to MLCS, the amount of which could be substantial and potentially materially adverse to the Obligated Group's financial condition. In the event of an early termination of the Preexisting Swap Agreement, there can be no assurance that (i) the Obligated Group will receive any termination payment payable to it by the respective Swap Counterparty, (ii) the Obligated Group will have sufficient amounts to pay a termination payment payable by it to MLCS, and (iii) the Obligated Group will be able to obtain a replacement swap agreement with comparable terms.

Secondary Market

There can be no guarantee that there will be a secondary market for the Bonds, or, if a secondary market exists, that such Bonds can be sold for any particular price. Occasionally, because of general market conditions or because of adverse history or economic prospects connected with a particular issue, secondary marketing practices in connection with a particular issue are suspended or terminated. Additionally, prices of issues for which a market is being made will depend upon the then prevailing circumstances. Such prices could be substantially different from the original purchase price.

Other Risk Factors

Changes in Federal and State Legislation and Regulation. Hospitals and health care systems are subject to a wide variety of federal and state legislative, regulatory and policy changes which could have a significant adverse impact on their operations and activities. Federal and state legislative bodies and regulatory agencies have broad discretion in altering or eliminating programs that contribute significantly to the revenues of hospital and health care systems, including the Medicare and Medi-Cal programs. In addition, federal and state legislative bodies and regulatory agencies may in the future enact legislation which imposes significant new burdens on the operations or activities of hospitals and health care systems, or require the termination or restructuring of certain common business transactions and arrangements.

Earthquakes and Seismic Compliance. Many hospitals in California, including the Hospital, are in close proximity to active earthquake faults. A significant earthquake in California could destroy or disable facilities of the Obligated Group Members or otherwise severely disrupt their operations and the regional economy.

California requires each acute care hospital in the state to either comply with new hospital seismic safety standards or cease acute care operations by January 1, 2008. Delays in compliance with the January 1, 2008 deadline will be permitted if a hospital shows that capacity lost in the closure of a facility cannot be provided by another facility in the area or if a hospital agrees that, on or before January 1, 2013, designated services will be provided by moving into an existing conforming building, relocating to a newly built building, or continuing in the building as retrofitted to comply with the standards. The Corporation has applied for and received such an extension until 2013. The 2013 deadline may be extended up to two years to January 1, 2015 if the hospital demonstrates that it meets certain requirements, including that it is under construction at the time of the request for the extension, and

that it has made reasonable progress in meeting the deadline, but it cannot meet the deadline due to reasons beyond its control. Management of the Corporation believes that its facilities that are subject to the seismic requirements will be in compliance with such seismic requirements within the prescribed guidelines; however, no assurance can be given at this time that the deadline will be met. See APPENDIX A – “INFORMATION CONCERNING THE OBLIGATED GROUP—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL PERFORMANCE – Capital Planning.”

Other Future Risks. In the future, the following factors, among others, may adversely affect the operations of health care providers, including the Corporation or the market value of the Bonds, to an extent that cannot be determined at this time.

(a) Adoption of legislation that would establish a national or statewide single-payor health program or that would establish national, statewide or otherwise regulated rates applicable to hospitals and other health care providers.

(b) Bankruptcy of an indemnity/commercial insurer, managed care plan or other payor.

(c) Efforts by insurers and governmental agencies to limit the cost of hospital services, to reduce the number of beds and/or to reduce the utilization of hospital facilities by such means as preventive medicine, improved occupational health and safety and outpatient care, or comparable regulations or attempts by third-party payors to control or restrict the operations of certain health care facilities.

(d) The occurrence of an epidemic or pandemic or a natural or man-made disaster, including terrorist acts, that could damage the facilities of the Corporation, interrupt utility service to the facilities, result in an abnormally high demand for health care services, or otherwise impair the Corporation’s operations or the generation of revenues from the facilities.

(e) Reduced demand for the services of the Corporation that might result from decreases in population.

In the future, other events may adversely affect the operations or income of the Obligated Group, as well as other health care providers, in a manner and to an extent that cannot be determined at this time.

VERIFICATION OF MATHEMATICAL COMPUTATIONS

As a condition to the delivery of the Bonds, Barthe & Wahrman, a firm of independent accounts, will deliver its report indicating that it has verified, in accordance with standards established by the American Institute of Certified Public Accountants, certain information and assertions provided by the Underwriter. The scope of its verification will include the mathematical accuracy of: (a) the mathematical computations of the adequacy of the maturing principal of and interest on the Escrow Securities to pay, when due, the principal, premium and interest on the Refunded Securities; and (b) the mathematical computations supporting the conclusion of Bond Counsel that the Bonds are not “Arbitrage Bonds” under the code and the regulations promulgated thereunder.

ABSENCE OF MATERIAL LITIGATION

The Authority

There is no controversy or litigation of any nature now pending or, to the knowledge of its officers, threatened against the Authority restraining or enjoining the execution, sale or delivery of the Bonds, or in any way contesting or affecting the validity of the Bonds, any proceedings of the Authority taken concerning the execution, sale or delivery thereof, the pledge or application of any moneys or security provided for the payment of the Bonds, or existence or powers of the Authority relating to the execution or delivery of the Bonds.

The Obligated Group

There is no action, suit, proceeding, or investigation at law or in equity before or by any court, public board or body pending or, to the Obligated Group's knowledge, threatened against or affecting the Obligated Group restraining or enjoining the execution, sale or delivery of the Bonds; or in any way contesting or affecting the validity of the Bonds, any proceedings of the Obligated Group taken concerning the execution, sale or delivery thereof, the pledge or application of any moneys or security provided for the payment of the Bonds, existence or powers of the Obligated Group relating to the execution or delivery of the Bond Purchase Agreement relating to the sale and purchase of the Bonds, among the Underwriter, the Authority and the Corporation (the "Purchase Contract"), this Official Statement, the Loan Agreement, the Bond Indenture, the Master Indenture or Obligation No. 1 (collectively, the "Bond Documents"); or wherein an unfavorable decision, ruling or finding would have a materially adverse effect on the business, properties or financial condition of the Obligated Group, or the transactions contemplated by this Official Statement, the Bonds or the Bond Documents.

The members of the Obligated Group are subject to certain legal actions that, in whole or in part, are not or may not be covered by insurance because of the type of action or amount or types of damages requested (e.g., punitive damages), because of a reservation of rights by an insurance carrier, or because the action has not proceeded to a stage that permits full evaluation. Management of the Corporation does not anticipate that any such suits will ultimately result in damage awards or judgments in excess of self-insurance reserves or insured limits, other than matters that have been disclosed in this Official Statement, or if such awards or judgments were to be entered, that they would have a material adverse impact on the financial condition or operations of the Obligated Group. There can be no assurance, however, that future litigation will not have a material adverse effect on the Obligated Group.

CONTINUING DISCLOSURE

The Corporation has covenanted, on behalf of itself and the Foundation, for the benefit of Holders and Beneficial Owners of the Bonds, to provide certain financial information and operating data relating to the Obligated Group by not later than five months following the end of the Obligated Group's Fiscal Year (which currently is December 31) (the "Annual Report"), and to provide notices of the occurrence of certain enumerated events, if material. The Annual Report and notices of material events will be filed on behalf of the Obligated Group with each Nationally Recognized Municipal Securities Information Repository ("NRMSIRs") or the Central Post Office and with a repository designated by the State of California, if any, as the state depository (the "State Repository"). The specific nature of the information to be contained in the Annual Report, or the notices of material events is described in the Continuing Disclosure Agreement, the form of which is included as APPENDIX E hereto. These covenants have been made in order to assist the Underwriter in complying with SEC Rule 15c2-12. The Obligated Group has never failed to comply in any material respect with any previous undertaking with respect to said Rule to provide annual reports or notices of material events.

The Corporation has also covenanted that it will provide to the NRMSIRs or the Central Post Office and to the State Repository, if any, not later than two months after the end of each fiscal quarter (except the fourth fiscal quarter), commencing with the fiscal quarter ending September 30, 2007, certain unaudited financial information for the Obligated Group for such fiscal quarter. See APPENDIX E – "Form of Continuing Disclosure Agreement."

RELATIONSHIPS AMONG PARTIES

The Members of the Obligated Group from time to time and in the ordinary course of their business may contract for services with persons who are also members of the Boards of Directors of the Corporation and/or the Foundation described in APPENDIX A to this Official Statement. The Obligated Group believes that all such contracts are on terms which are no less favorable than could be obtained from unaffiliated persons.

The Underwriter, the underwriter of the Bonds, and MLCS, the counterparty under the Preexisting Swap Agreement, are both subsidiaries of Merrill Lynch & Co., Inc.

TAX MATTERS

General

In the opinion of Bond Counsel, under existing statutes, regulations, rulings and judicial decisions and assuming compliance by the Issuer and the Corporation with certain covenants in the Indenture, the Loan Agreement and other documents pertaining to the Bonds and certain requirements of the Code regarding the organization and operation of the Corporation, the use, expenditure and investment of proceeds of the Bonds and timely payment of certain investment earnings to the United States, interest on the Bonds is not includable in gross income of the owners of the Bonds for federal income tax purposes.

In the further opinion of Bond Counsel, interest on the Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability.

In addition, Bond Counsel has relied on the opinion of Hanson, Bridgett, Marcus, Vlahos & Rudy, LLP, regarding the qualification of the Corporation as an organization described in Section 501(c)(3) of the Code. Neither Bond Counsel nor Hanson, Bridgett, Marcus, Vlahos & Rudy, LLP, can give or has given any opinion or assurance about the future activities of the Corporation or about the effect of future changes in the Code, applicable regulations, the interpretation thereof, or the resulting changes in enforcement thereof by the IRS. Failure to comply with the above-mentioned covenants and requirements or failure of the Corporation to be organized and operated in accordance with the IRS's requirements for the maintenance of its status as an organization described in Section 501(c)(3) of the Code may cause interest on the Bonds to be included in gross income retroactively to the date of issuance of the Bonds. See "BONDHOLDERS' RISKS—Tax-Exempt Status and other tax matters."

Ownership of, or the receipt of interest on, tax-exempt obligations may result in collateral tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits, taxpayers that may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, and taxpayers who may be eligible for the earned income credit. Bond Counsel expresses no opinion with respect to any collateral tax consequences and, accordingly, prospective purchasers of the Bonds should consult their tax advisors as to the applicability of any collateral tax consequences.

Certain requirements and procedures contained or referred to in the Indenture, the Loan Agreements and other documents pertaining to the Bonds may be changed, and certain actions may be taken, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of tax-exempt obligations. Bond Counsel expresses no opinion as to the exclusion of interest on the Bonds from gross income for federal income tax purposes on and after the date on which any such change occurs or action is taken upon the advice or approval of counsel other than Sidley Austin LLP.

In the further opinion of Bond Counsel, interest on the Bonds is exempt from personal income taxes imposed by the State of California.

Legislation affecting municipal securities is continually being considered by the United States Congress. There can be no assurance that legislation enacted after the date of issuance and delivery of the Bonds will not have an adverse effect on the tax-exempt status of the Bonds. Legislative or regulatory actions and proposals may also affect the economic value of tax exemption or the market prices of the Bonds.

A copy of the proposed form of opinion of Bond Counsel is attached hereto as APPENDIX D.

Backup Withholding

The Tax Increase Prevention and Reconciliation Act of 2005, enacted on May 17, 2006, contains a provision under which interest paid on tax-exempt obligations will be subject to information reporting in a manner similar to interest paid on taxable obligations. Although the new reporting requirement does not, in and of itself, affect the excludability of such interest from gross income for federal income tax purposes, the reporting requirement causes the payment of interest on the Bonds to be subject to backup withholding if such interest is paid to beneficial owners who (a) are not “exempt recipients,” and (b) either fail to provide certain identifying information (such as the beneficial owner’s taxpayer identification number) in the required manner or have been identified by the IRS as having failed to report all interest and dividends required to be shown on their income tax returns. Generally, individuals are not exempt recipients, whereas corporations and certain other entities generally are exempt recipients. Amounts withheld under the backup withholding rules from a payment to a beneficial owner would be allowed as a refund or a credit against such beneficial owner’s federal income tax liability, provided the required information is furnished to the IRS.

Premium Bonds

Certain of the Bonds may be purchased in the initial offering for an amount in excess of their principal amount (“Premium Bonds”). The excess of the tax basis of a purchaser of a Premium Bond (other than a purchaser who holds a Premium Bond as inventory, stock in trade or for sale to customers in the ordinary course of business) over the principal amount of such Premium Bond is “bond premium.” Bond premium is amortized for federal income tax purposes over the term of a Premium Bond based on the purchaser’s yield to maturity in the Premium Bond, except that in the case of a Premium Bond callable prior to its stated maturity, the amortization period and the yield may be required to be determined on the basis of an earlier call date that results in the lowest yield on such Premium Bond. A purchaser of a Premium Bond is required to decrease his or her adjusted basis in such Premium Bond by the amount of bond premium attributable to each taxable year in which such purchaser holds such Premium Bond. The amount of bond premium attributable to a taxable year is not deductible for federal income tax purposes. Purchasers of Premium Bonds should consult their tax advisors with respect to the precise determination for federal income tax purposes of the amount of bond premium attributable to each taxable year and the effect of bond premium on the sale or other disposition of a Premium Bond, and with respect to the state and local tax consequences of owning and disposing of a Premium Bond.

Discount Bonds

The initial public offering price of certain of the Bonds (collectively, the “Discount Bonds”) is less than the principal amount of the Discount Bonds. The difference between the principal amount of a Discount Bond and its initial public offering price is original issue discount. Original issue discount on a Discount Bond accrues over the term of such Discount Bond at a constant interest rate. To the extent it has accrued, original issue discount on a Discount Bond is treated as interest excludable from gross income for federal income tax purposes under the conditions and limitations described above. The amount of original issue discount that accrues on a Discount Bond in each year is not an item of tax preference for purposes of calculating federal alternative minimum taxable income, but is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation’s alternative minimum tax liability. Additionally, such accrued original issue discount is taken into account in determining the distribution requirements of certain regulated investment companies. Consequently, owners of Discount Bonds should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability, additional distribution requirements or other collateral federal income tax consequences although the owner may not have received cash in such year.

The accrual of original issue discount on a Discount Bond will increase the owner’s adjusted basis in such Discount Bond. This will affect the amount of taxable gain or loss realized by the owner of the Discount Bond upon the redemption, sale or other disposition of such Discount Bond. The effect of the accrual of original issue discount on the federal income tax consequences of a redemption, sale or other disposition of a Discount Bond that is not purchased at the initial public offering price may be determined according to rules that differ from those described above. Owners of Discount Bonds should consult their tax advisors with respect to the precise determination for federal income tax purposes of the amount of original issue discount that properly accrues with respect to the

Discount Bonds, other federal income tax consequences of owning and disposing of the Discount Bonds and any state and local tax consequences of owning and disposing of the Discount Bonds.

APPROVAL OF LEGALITY

Certain legal matters incident to the issuance of the Bonds are subject to the approving opinion of Sidley Austin LLP, San Francisco, Bond Counsel. A complete copy of the proposed form of opinion of Bond Counsel is set forth as APPENDIX D. Bond Counsel undertakes no responsibility for the accuracy, completeness or fairness of this Official Statement. Certain legal matters will be passed upon for the Obligated Group by Hanson, Bridgett, Marcus, Vlahos & Rudy LLP, for the Authority by Jones Hall, A Professional Law Corporation, and for the Underwriter by Holland & Knight L.L.P. These law firms undertake no responsibility for the accuracy, completeness or fairness of this Official Statement, except as otherwise stated in their respective opinions delivered at the Closing of the Bonds, and none of such opinions is addressed to or may be relied upon by purchasers of the Bonds.

UNDERWRITING

The Bonds are being purchased by Merrill Lynch, Pierce, Fenner & Smith Incorporated (the "Underwriter") at an aggregate purchase price of \$59,862,488.95 (which represents the \$60,100,000.00 par amount of the Bonds plus net original issue premium of \$93,038.95, less the Underwriter's discount of \$330,550.00). The Purchase Contract provides that the Underwriter will be obligated to purchase all of the Bonds, if any are purchased, the obligation to make such purchase being subject to certain terms and conditions to be satisfied by the Obligated Group and the Authority. The Purchase Contract contains the agreement of the Obligated Group to indemnify the Underwriter and the Authority against certain liabilities to the extent permitted by law. The Underwriter may offer and sell the Bonds to certain dealers and others at prices lower than the offering prices stated on the inside cover page. The offering prices may be changed from time to time by the Underwriter.

INDEPENDENT ACCOUNTANTS

The consolidated financial statements of the Corporation, the Foundation, CFHN and Family House, as of and for the years ended December 31, 2006 and 2005 included as APPENDIX B to this Official Statement have been audited by Moss Adams, San Francisco, California, independent certified public accountants, as stated in their report appearing therein.

RATING

The Bonds are rated "A" by Standard & Poor's Rating Service, a division of The McGraw-Hill Companies, Inc. ("S&P").

The rating reflects only the views of S&P, and any explanation of the significance of such rating should be obtained from S&P at the following addresses: Standard & Poor's Ratings Service, a division of The McGraw-Hill Companies, Inc., Public Finance Department, 55 Water Street, New York, NY 10041. In order to obtain such rating, the Obligated Group furnished to the rating agency certain information and materials, some of which has not been included in this Official Statement. Generally, rating agencies base their ratings on such information and materials and their own investigation, studies and assumptions. There is no assurance that the rating will be maintained for any given period of time or that it will not be revised downward or withdrawn entirely by S&P, if, in its judgment, circumstances so warrant. The Obligated Group undertakes no responsibility to oppose any such revision or withdrawal. Any such downward revision or withdrawal of the rating obtained may have an adverse effect on the market price of the Bonds.

The Obligated Group expects to furnish to each rating agency such information and materials as it may request. The Obligated Group, however, assumes no obligation to furnish requested information and materials, and may issue debt for which a rating is not requested. The failure to furnish requested information and materials, or the issuance of debt for which a rating is not requested, may result in the suspension or withdrawal of a rating on the Bonds.

MISCELLANEOUS

The references to and the descriptions of the Bonds, the Purchase Contract, the Loan Agreement, the Bond Indenture, the Master Indenture, Obligation No. 1, the Swap Obligation and the Preexisting Swap Agreement contained herein and in APPENDIX C are brief outlines of certain provisions thereof. Such outlines, and the constitutional provisions, statutes and other documents referenced herein, do not purport to be complete. For full and complete statements of such provisions, reference is made to such documents, constitutional provisions and statutes. Copies of the documents mentioned under this heading are available as described under “INTRODUCTION – Availability of Documents.”

The attached Appendices are integral parts of this Official Statement and should be read together with the balance of this Official Statement. All estimates, projections and other statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Official Statement is not to be construed as a contract or agreement between the Authority or the Obligated Group and the purchasers or Holders of any Bonds.

The distribution and use of this Official Statement has been duly authorized by the Authority. This Official Statement and its distribution have been approved by the boards of directors of the Corporation and the Foundation.

ABAG FINANCE AUTHORITY FOR NONPROFIT CORPORATIONS

By: _____ /S/ _____
Joseph K. Chan
Chief Financial Officer

APPROVED:

**CHILDREN’S HOSPITAL & RESEARCH CENTER
AT OAKLAND**
For itself and on behalf of the Obligated Group

By: _____ /S/ _____
Douglas T. Myers
Senior Vice President and
Chief Financial Officer

APPENDIX A

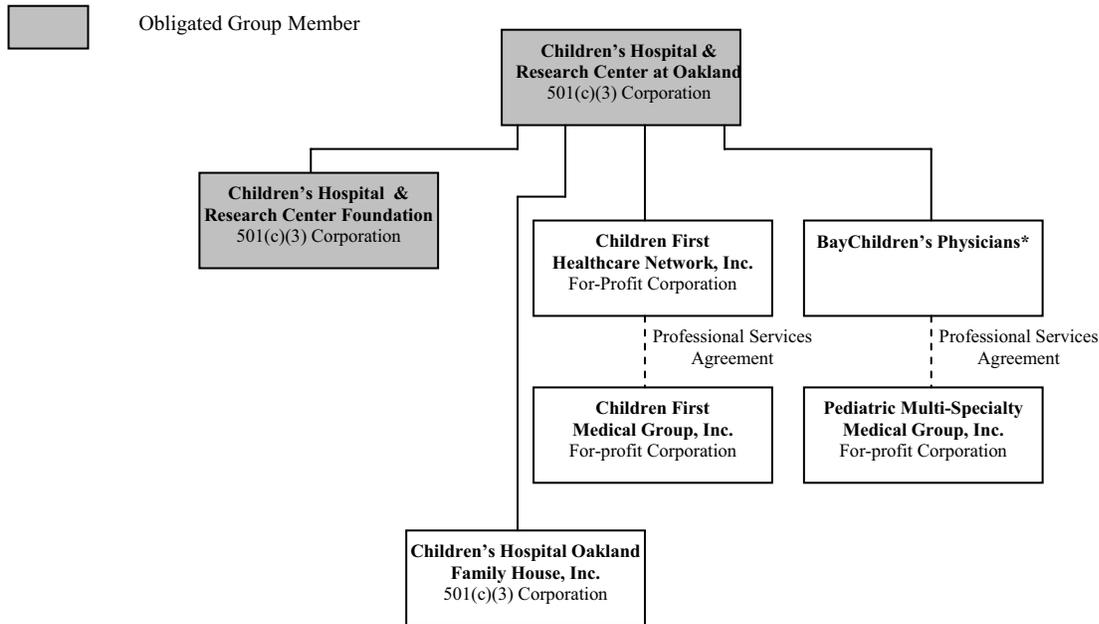
**INFORMATION CONCERNING
THE OBLIGATED GROUP**

THE INFORMATION CONTAINED HEREIN AS APPENDIX A
TO THIS OFFICIAL STATEMENT HAS BEEN OBTAINED FROM THE OBLIGATED
GROUP

TABLE OF CONTENTS

INTRODUCTION.....	1
The Corporation.....	1
The Obligated Group	1
Other Affiliated Corporations.....	2
Other Entities	3
GOVERNANCE AND EXECUTIVE MANAGEMENT	3
Corporation’s Board of Directors	3
Executive Management.....	4
FACILITIES AND SERVICES.....	5
Current Facilities.....	5
Licenses, Accreditations, and Memberships.....	8
Educational, Training And Research Programs.....	8
Historical Utilization of Health Facilities.....	10
SERVICE AREA, PATIENT ORIGIN, AND COMPETITION.....	10
Description of Service Area.....	10
Map of Service Area	12
Patient Origin	13
Utilization, Market Share Analysis and Competition.....	14
Sources of Healthcare Revenue	19
Other Sources of Revenue	20
MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL PERFORMANCE	21
General Overview	21
Critical Accounting Policies and Estimates.....	21
Comparative Financial Results	23
Liquidity and Capital Resources.....	26
Capitalization	27
Capital Planning and Seismic Compliance.....	27
Historical and Pro Forma Debt Service Coverage.....	28
OTHER INFORMATION	30
Medical Staff.....	30
Nursing Staff.....	34
Employee and Labor Relations.....	34
Pension and Deferred Compensation.....	35
Insurance and Risk Management	35

INTRODUCTION
ORGANIZATIONAL CHART



*BayChildren's Physicians will submit an application for determination as a 501(c)(3) Organization (defined below).

The Obligated Group

Children's Hospital & Research Center at Oakland (the "Corporation") is a California nonprofit public benefit corporation and is exempt from federal income taxation as an organization described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (a "501(c)(3) Organization"). The Corporation owns and operates a general acute care hospital located in Oakland, California known as Children's Hospital & Research Center at Oakland (the "Hospital").

The Hospital was founded in 1912 and commenced operations in 1914 as a 20-room hospital. In 1928, the Hospital's operations were moved to a new 78-bed facility. A number of renovations and expansions occurred after 1928. The Hospital is currently licensed for 190 beds, of which 170 are located on the Hospital's main campus and 20 are located, through a lease arrangement, at Alta Bates – Summit Medical Center in Oakland, California.

The Corporation also operates the Children's Hospital Oakland Research Institute ("CHORI") as a division of the Hospital. CHORI specializes in pediatric medical research and related areas. In 1999, the operations of CHORI were relocated from the Hospital campus to the Corporation's Martin Luther King, Jr. Plaza facility at 5700 Martin Luther King Jr. Way, located five blocks from the Hospital.

The “Obligated Group” consists of the Corporation (described above) and Children’s Hospital & Research Center Foundation.

Children’s Hospital & Research Center Foundation (the “Foundation”) is a nonprofit public benefit corporation and a 501(c)(3) Organization. The Foundation has been in operation since 1967. Its primary goal is to acquire charitable gifts and other resources exclusively for the Corporation’s programs, services and operations. The Corporation is the sole corporate member of the Foundation.

Other Affiliated Corporations

The following corporations are controlled by the Corporation but are not members of the Obligated Group:

BayChildren’s Physicians (“BCP”) is a medical practice foundation of which the Corporation is the sole member. BCP was formed in August 2006 and its business operations commenced on January 1, 2007. BCP will apply for recognition as a 501(c)(3) Organization. The boards of directors of the Corporation and BCP have adopted resolutions, pursuant to which BCP will become a member of the Obligated Group (i) if and when it receives recognition as a 501(c)(3) Organization and (ii) provided the terms of the Master Indenture relating to adding members to the Obligated Group are satisfied. See APPENDIX C – “SUMMARY OF PRINCIPAL DOCUMENTS – MASTER INDENTURE Membership in Obligated Group.” However, no assurance can be given the BCP will become a member of the Obligated Group.

BCP has entered into a Professional Services Agreement, effective January 1, 2007, with Pediatric Multispecialty Medical Group, Inc., dba BayChildren’s Medical Group, a multispecialty medical group (“BCMG”), which is described under “Other Entities” below. Under the Professional Services Agreement, BCMG, through its employed or subcontracted physicians, agrees to provide care to BCP’s patients, including on-call coverage, care to Medi-Cal beneficiaries, and uncompensated care in accordance with BCP’s policies. BCMG also agrees to perform research and education and otherwise cooperate with BCP in administering the group’s medical practice.

In turn, BCP provides the infrastructure to support BCMG’s medical practice, including, without limitation, all facilities, equipment, supplies, administrative and management services, non-physician personnel, medical records systems, accounting and bookkeeping services, insurance and consultants. BCP also negotiates and enters into all third-party payor contracts on BCMG’s behalf. All revenues and expenses of BCMG’s practice run through BCP, which compensates BCMG for the professional services it provides. After the first year, the compensation paid to BCMG includes certain incentives to increase productivity. The Agreement has a ten-year term and includes a reciprocal right to terminate without cause after two years.

Children First Healthcare Network, Inc. (“CFHN”) is a physician-hospital organization designed to provide, on a contracted basis, utilization management, claims management, and other services to the Corporation and to Children First Medical Group, Inc. described below. It is organized as a California stock corporation and its revenues come primarily from administrative

service fees. The Corporation is the sole shareholder of CFHN and expects that it will dissolve CFHN by the end of 2007.

Children’s Hospital Oakland Family House, Inc. (“Family House”) is a California nonprofit public benefit corporation and a Section 501(c)(3) Organization that provides housing for eligible families whose children are being treated at the Hospital. The Corporation is the sole corporate member of Family House.

Other Entities

BayChildren’s Medical Group (“BCMG”), the business name for Pediatric Multispecialty Medical Group, Inc., is a new California professional medical corporation formed as a multi-specialty medical group under California law. BCMG provides patient care services pursuant to a Professional Services Agreement with BCP, which is described under “Other Affiliated Corporations” above.

Children First Medical Group, Inc. (“CFMG”) is a California professional medical corporation formed as a multi-specialty independent medical practice association. CFMG represents independent medical practitioners who care for children and participate in CFHN, which is described under “Other Affiliated Corporations” above. CFMG is owned and controlled by its shareholders.

GOVERNANCE AND EXECUTIVE MANAGEMENT

Corporation’s Board of Directors

The Corporation’s bylaws prescribe a Board of Directors (“Board”) consisting of 13 to 17 members. Currently, the Board consists of 14 members, all of whom are elected for three-year terms. The Board includes two voting *ex officio* directors: the Corporation’s Chief Executive Officer (“CEO”) and the President of the Medical Staff. The Board elects all other directors. The Governance Committee interviews and recommends new members to the Board. Up to 25% of the Board (including *ex officio* directors) can be physicians. Directors may serve up to three consecutive terms and may be re-elected after a one-year hiatus. The current directors, their occupations, and the year in which their terms expire are as follows:

<u>Board Member</u>	<u>Occupation</u>	<u>Term Expires:</u>
Jeffrey Cheung	Banking Executive	March 2008
Arthur D’Harlingue, M.D.	Neonatologist	March 2008
Harold Davis	Retired Business Leader	March 2008
Arnold Grisham	Banker	March 2009
James Keefe	Real Estate Investor	March 2009
Watson Laetsch, Ph.D.	Consultant	March 2010
Michael LeNoir, M.D.	Community Physician	March 2009
Barbara May	Businesswoman	March 2008
Melba Muscarolas	AT&T Executive	March 2010
Howard Pien	Former President & CEO, Chiron Corporation	March 2010
Lloyd Takao, M.D.	President, Medical Staff	<i>Ex-Officio</i>
Frank Tiedemann	President & CEO, Children’s Hospital	<i>Ex-Officio</i>

Gene Upshaw, M.D.
Harold C. Warner, Ph.D.

Sports Association Executive
Investment Advisor

March 2009
March 2010

Executive Management

Certain members of the Corporation's management are described below:

FRANK TIEDEMANN, President and Chief Executive Officer. Mr. Tiedemann earned a master's degree in business administration from the Canadian School of Management in 1983. He was appointed as President and Chief Executive Officer of the Corporation in 2005. From 2001 to 2005, Mr. Tiedemann was the Chief Executive Officer and President of St. Mary's Health System, a \$330 million regional system of two acute care Catholic hospitals with 540 licensed acute beds. St. Mary's is part of Ascension Health in Evansville, Indiana. During his tenure at St. Mary's, Mr. Tiedemann launched the region's first trauma center. Prior to that, he was President of St. Paul Medical Center in Dallas, Texas (1996-2001) and Senior Vice President of System Development at Yale-New Haven Health System in New Haven, Connecticut (1994-1996). He also served as a Senior Vice President of Corporate Development at John Muir Medical Center in Walnut Creek, California from 1990 to 1994.

BRAD BARBER, ESQ, Senior Vice President and Chief Development Officer. Mr. Barber earned his undergraduate degree from the University of California Berkeley in 1968 and his law degree from Boalt Hall School of Law in 1971. He joined the Corporation in 2006 as Senior Vice President and Chief Development Officer of the Foundation. Previously, Mr. Barber spent more than 25 years fundraising for the University of California, where he was the Assistant Vice President for Institutional Advancement from 1998 to 2005.

MARY L. DEAN, Senior Vice President, External Affairs. Ms. Dean earned her master of arts degree from the University of Kentucky in 1968. She joined the Corporation in 2001 and oversees strategic planning, marketing, communication and government relations. She previously served as Senior Vice President, Public Policy at Valley Children's Hospital in Fresno, California from 1984-1991 and again from 1995-2000. Ms. Dean was the Associate Commissioner of the Kentucky State Department of Education from 1991-1995. She presently serves on the boards of Med-Alert and the Marcus Foster Educational Institute.

PAMELA FRIEDMAN, MHA, Senior Vice President and Chief Administrative Officer, BayChildren's Physicians. Ms. Friedman earned her bachelor of arts degree from the University of California, Berkeley in 1976, and her master's degree in health administration from the University of Colorado Health Sciences Center in 1980. She joined the Corporation as Vice President for Regional Development in 2005. Previously, Ms. Friedman was the Vice President of Business Development at ValleyCare Health System in Pleasanton, California (1996-2005). She has spent her entire healthcare career in the Bay Area, including 15 years at John Muir Medical Center.

BERTRAM H. LUBIN, MD, Senior Vice President, Research. Dr. Lubin earned his medical degree from the University of Pittsburgh Medical School in 1964, completed his internship and residency at Children's Hospital of Philadelphia in 1966, and completed a fellowship in hematology/oncology at Children's Hospital Medical Center, Boston in 1970. Since joining the Corporation in 1971, Dr. Lubin has been responsible for developing the Hospital's Sick Cell Screening, Counseling and Education Program, the Northern California Comprehensive Sick Cell

Center and the Sibling Donor Cord Blood Program. Dr. Lubin is also an adjunct professor of pediatrics at the University of California, San Francisco.

VIPUL N. MANKAD, MD, Senior Vice President and Chief Medical Officer. Dr. Mankad earned his medical degree in 1968 from Government Medical College, The Maharaja Sayajirao University in Baroda, India. He joined the Corporation in 2006. Previously, he was Senior Medical Advisor for Child Health at the United States Centers for Medicare and Medicaid Services (2004-2005). From 2003-2004, Dr. Mankad worked for the United States Senate Committee on Health, Education, Labor and Pensions. He has also held leadership positions at medical centers in Lexington, Kentucky, Mobile, Alabama and Chicago.

DOUGLAS T. MYERS, MBA, CPA, Senior Vice President, Chief Financial Officer (“CFO”) and Chief Operating Officer (“COO”). Mr. Myers earned a bachelor’s degree in business administration from Youngstown State University in 1983 and a master’s degree in business administration from Loyola College in 1990. He is also a Certified Public Accountant. Mr. Myers joined the Corporation in 2005. From 2002-2005, Mr. Myers was Executive Vice President of Finance and Chief Financial Officer (“CFO”) for Saint Vincent Health System in Erie, PA. From 1997-2002, Mr. Myers was CFO for Texas Health Resources in Dallas, Texas. Mr. Myers was Regional CFO for Hospital Corporation of America, also based in Dallas, Texas, from 1994-1997.

JACQUELYN GARMAN, ESQ, Vice President, General Counsel. Ms. Garman earned her law degree at Stanford Law School in 1980, after receiving her bachelors and master of arts degrees at Washington State University in 1975 and 1977, respectively. She was named Vice President and General Counsel of the Corporation in 2006. From 1980-2006, she was an attorney at Hanson Bridgett Marcus Vlahos & Rudy, LLP, the Corporation’s primary law firm, where she specialized in litigation on behalf of healthcare clients.

NANCY SHIBATA, RN, MSN, Vice President, Nursing. Ms. Shibata received her master of science degree in nursing administration from the University of San Francisco in 1991 and has been a member of the Corporation’s staff since 1979. She has served in a variety of roles including: PICU staff nurse, PICU Assistant Head Nurse, PICU Manager, Nursing Supervisor, Director of Ambulatory Care, Director of Critical Care Services, and Director of Nursing. In 2003, she was named Vice President of Nursing. In her current role, she directs operational, financial, quality and strategic activities for the nursing division including inpatient, surgical, and ambulatory areas.

FACILITIES AND SERVICES

Current Facilities

The Hospital’s main campus is located on approximately 5½ acres in Oakland, California and consists of approximately 200,000 square feet of clinical space, a five-story parking garage, and a freestanding ambulatory surgery center. In addition, a 100,000-square-foot facility, located five blocks from the Hospital’s main campus, houses CHORI, the Hospital’s medical research division. The Corporation also operates satellite subspecialty clinics in Walnut Creek and Brentwood (Contra Costa County, California), Larkspur (Marin County, California) and Pleasanton (Alameda County, California).

The Corporation’s licensed bed complement is set forth in the table below, entitled, “List of Hospital Services: Inpatient Services.” Twenty of the Corporation’s licensed pediatric acute care beds are located at Alta Bates-Summit Medical Center in Oakland and are leased by the Corporation.

The Corporation continues to explore other possibilities in its service area to offer additional services and provide additional sites. It has held discussions with several hospitals to develop pediatric inpatient and/or neonatal units. No assurances can be made at this time that such discussions will proceed to execution of definitive agreements or that the development of such units will occur.

The Corporation is exploring the development of a new tertiary care facility, discussed under “MANAGEMENT’S DISCUSSION AND ANALYSIS – Capital Planning and Seismic Compliance” below.

The following table presents a detailed inventory of services currently available at the Hospital.

Inpatient Services (including number of beds)

- Neonatal Intensive Care Unit (NICU) (44)
- Pediatric Acute Care (111)
- Pediatric Intensive Care Unit (PICU) (23)
- Pediatric Rehabilitation (12)

Pediatric Subspecialty Services

- Adolescent Medicine
- Allergy/Immunology
- Anemia/Hemophilia
- Anesthesiology
- Bone Marrow Transplant
- Cardiology/Open and Closed Heart Surgery /Cardiac Catheterization
- Child Development
- Child Psychiatry
- Critical Care Medicine
- Dentistry (Pedodontics)
- Dermatology
- Endocrinology/Metabolism
- Gastroenterology
- General Surgery
- Hematology/Oncology/Sickle Cell
- Infectious Diseases
- Gynecology
- Medical Genetics
- Neonatology
- Nephrology
- Neurology
- Neurosurgery
- Ophthalmology
- Orthopedics
- Otolaryngology
- Pathology
- Pediatric Rehabilitation
- Plastic Surgery
- Pulmonary Medicine
- Thoracic Surgery
- Urology

Outpatient Services

- Day Hospital
- Emergency Services
- Primary Care
- Ambulatory Surgery
- Trauma
- Satellite Clinics
 - Brentwood
 - Larkspur
 - Pleasanton
 - Walnut Creek

Outpatient Clinics

- Adolescent and Gynecology Clinics
- Allergy Clinic
- Arthritis Clinic
- Behavioral Pediatric Clinic
- Child Development Clinic
- Child Psychiatric Clinic
- Chronic Respiratory Diseases Clinic
- Cystic Fibrosis Clinic
- Craniofacial Clinic
- Dental Clinic *
- Dermatology Clinic
- Down Syndrome Clinic
- Ear, Nose and Throat Clinic
- Eye Clinic
- Foot Clinic
- Gastroenterology Clinic
- Genetics Clinic
- Hand Clinic
- Hematology/Oncology/Hemophilia Clinic
- Sickle Cell Anemia Clinic
- Infectious Disease Clinic
- Neonatal Clinic
- Neurology Clinic
- Obesity Clinic
- Orthopedic Clinic
- Pediatric Rehabilitation Clinic
- Pre-Op Surgery Clinic
- Renal Clinic
- Scoliosis Clinic
- Sexual Abuse Management Clinic
- Transfusion Clinic
- Urology Clinic

*Dental Services provided at site of Hospital, operated by a third party (La Clinica de la Raza).

Social and Rehabilitative Services

- Center for Pediatric Rehabilitation (includes Audiology, Occupational Therapy and Physical Therapy)
- Center for the Vulnerable Child
- Child Life Services
- Early Intervention Program
- Family House
- Hall of Health
- Infant Mental Health
- Interpreter Services
- Neonatal Follow-Up Program
- Parent-Infant Program
- Pastoral Services
- School Program
- Social Services
- Speech and Language Services
- Volunteer Services

Support Services

- Nursing
- Clinical Laboratory/Pathology
- Clinical Nutrition/Dietary Services
- Diagnostic Imaging (Radiology, CT, MRI)
- Pharmacy

Licenses, Accreditations, and Memberships

In September 2005, The Joint Commission completed an on-site survey of the Hospital in conjunction with its accreditation process. The Hospital was awarded accreditation from The Joint Commission for three years, expiring in 2008.

The Hospital is licensed as a general acute care hospital each year by the California Department of Public Health. The current license expires on December 31, 2007. The California Medical Association and the American Medical Association have accredited the pediatric residency program. The Corporation is a member of the California Hospital Association, the Hospital Council of Northern and Central California, the California Children's Hospital Association, Child Health Corporation of America, and the National Association of Children's Hospitals and Related Institutions. The Hospital also is an eligible provider under the Medicare, Medi-Cal (California's Medicaid program) and California Children's Service programs.

Educational, Training And Research Programs

The Corporation offers a three-year pediatric residency program which, as of May 31, 2007, enrolled 79 residents. The Corporation also offers fellowships in pediatric hematology/oncology, emergency medicine, and infectious disease. The Accreditation Council for Graduate Medical Education has accredited both resident and fellowship programs. The Corporation also has a Critical Care fellowship under an affiliation with the University of California, San Francisco. Many of the current medical staff physicians were trained at the Hospital, and the residency program continues to attract highly qualified specialists. For the 2006-07 resident year beginning July 1, the residency program received 547 applications for 26 first-year positions. In addition to the pediatric residents in the Hospital-accredited training program, approximately 16 resident full-time-equivalents and fellows from 13 affiliated programs also rotate through the Hospital. These include residents from surgical, orthopedic, dental, anesthesia and other subspecialty residency programs. In addition, the Corporation sponsors teaching programs for nurses, allied health professionals, and technologists, as well as an active in-service education program.

The Corporation participates with a number of educational institutions in various clinical experience programs, including:

<u>Educational Institution</u>	<u>Program</u>
Boston University (Boston, Massachusetts)	Occupational Therapy
California State University at Hayward	Social Worker
California State University at Hayward	Nursing Students
California State University at Sacramento	Social Worker
California State University at San Francisco	Nursing Students
California State University at San Francisco	Social Worker
California State University at San Jose	Social Worker; Occupational Therapy
California State University at Sonoma	Nursing Students
Chabot College (Hayward, California) and extended campus	Nursing Students

Educational Institution

Program

at Valley Care Hospital (Pleasanton, California)	
College of Marin (Kentfield, California)	Nursing Students
Contra Costa College (San Pablo, California)	Nursing Students
Dominican College (San Rafael, California)	Nursing Students
Drexel University (Philadelphia, Pennsylvania)	Physical Therapy
Duke University (Durham, North Carolina)	Physical Therapy
Holy Names College (Oakland, California)	Nursing Students
Los Medanos College (Pittsburg, California)	Nursing Students
Mendocino College (Willits, California)	Nursing Students
Merritt College (Oakland, California)	Nursing Students
Merritt College (Oakland, California)	Physical Therapy
Napa Valley College (Napa, California)	Nursing Students
Napa Valley College (Napa, California)	Respiratory Therapy Students
NCP Vocational School (Hayward, California)	Nursing Students
Northwestern University Medical School (Chicago, Illinois)	Physical Therapy
Ohlone College (Fremont, California)	Respiratory Therapy Students
Old Dominion University (Norfolk, Virginia)	Occupational Therapy
Samuel Merritt College (Oakland, California)	Occupational Therapy
Samuel Merritt School of Nursing (Oakland, California)	Nursing Students
Smith College (Northampton, Massachusetts)	Social Worker
University of California, Berkeley	Clinical Nutrition
University of California, Berkeley	Social Worker / Psychology
University of California, San Francisco	Nursing Students
University of California, San Francisco	Dentistry
University of California, San Francisco	Physical Therapy
University of San Francisco	Nursing Students
University of Southern California (Los Angeles, California)	Occupational Therapy
University of the Pacific (Stockton, California)	Physical Therapy
University of Washington (Seattle, Washington)	Occupational Therapy

The Corporation provides teaching and training opportunities at various community hospitals for physicians, nurses, and respiratory therapy staff in the fields of perinatal outreach, neonatal clinical skills, respiratory therapy and pediatric intensive care. In addition, physicians receive training and experience to become board-certified subspecialists through the fellowship programs in hematology/oncology, pediatric critical care, emergency medicine, and infectious disease. The Corporation maintains a specialized Education Resource Department for training and continuing education of its nursing and other allied healthcare providers.

Through CHORI, its research division, the Corporation conducts basic and clinical research into the molecular, cellular and biochemical bases of disorders such as cystic fibrosis, cancer, hemophilia, sickle cell disease, and infectious disease. This research is primarily supported by grants from the federal government. In some cases, specific inventions have led to licensing arrangements with third parties to commercially develop and market the invention.

Historical Utilization of Health Facilities

The following table sets forth historical utilization of the Corporation's facilities.

Statistics	Years Ended December 31,			Five Months Ended May 31,	
	2004	2005	2006	2006	2007
Admissions	8,898	9,571	9,351	4,087	4,612
Patient Days	47,546	52,216	53,163	23,730	24,685
Average Daily Census	129.9	143.1	145.7	157.2	163.5
Average Length of Stay	5.4	5.5	5.7	5.8	5.4
Clinic Visits	105,968	121,869	128,920	53,583	59,339
Urgent Care Visits	21,546	24,529	23,540	11,779	10,903
ER Visits	25,862	27,079	26,935	11,910	13,380
Other Outpatient Visits	32,937	29,877	32,560	13,553	14,289
Outpatient Visits – Total	186,313	203,354	211,955	90,825	97,911

Source: Hospital Finance Department

The following table sets forth certain data relating to the Corporation's payor mix. See "HISTORICAL FINANCIAL INFORMATION — Sources of Healthcare Revenue" and "—Other Sources of Revenue" herein for more information concerning payors.

Admissions by Payor	Years Ended December 31,						Five Months Ended May 31,			
	2004	%	2005	%	2006	%	2006	%	2007	%
Medi-Cal/CCS	3,448	38.6	3,797	39.7	3,981	42.6	1,678	41.1	1,935	42.0
Medi-Cal Managed Care	1,876	21.1	2,160	22.6	1,842	19.7			990	21.5
Medicare	9	0.1	17	0.2	16	0.2	883	21.6		
Managed Care	3,206	36.1	3,290	34.4	3,256	34.8	3	0.1	10	0.2
Insurance	42	0.5	33	0.3	3	0.0	1,375	33.6	1,544	33.5
Other	317	3.6	261	2.7	257	2.7	2	0.0	0	0.0
Total	8,898	100.0	9,558	100.0 ⁽¹⁾	9,355	100.0	146	3.6	133	2.9

Source: Hospital Finance Department.

⁽¹⁾ Percentage does not total exactly due to rounding.

SERVICE AREA, PATIENT ORIGIN, AND COMPETITION

Description of Service Area

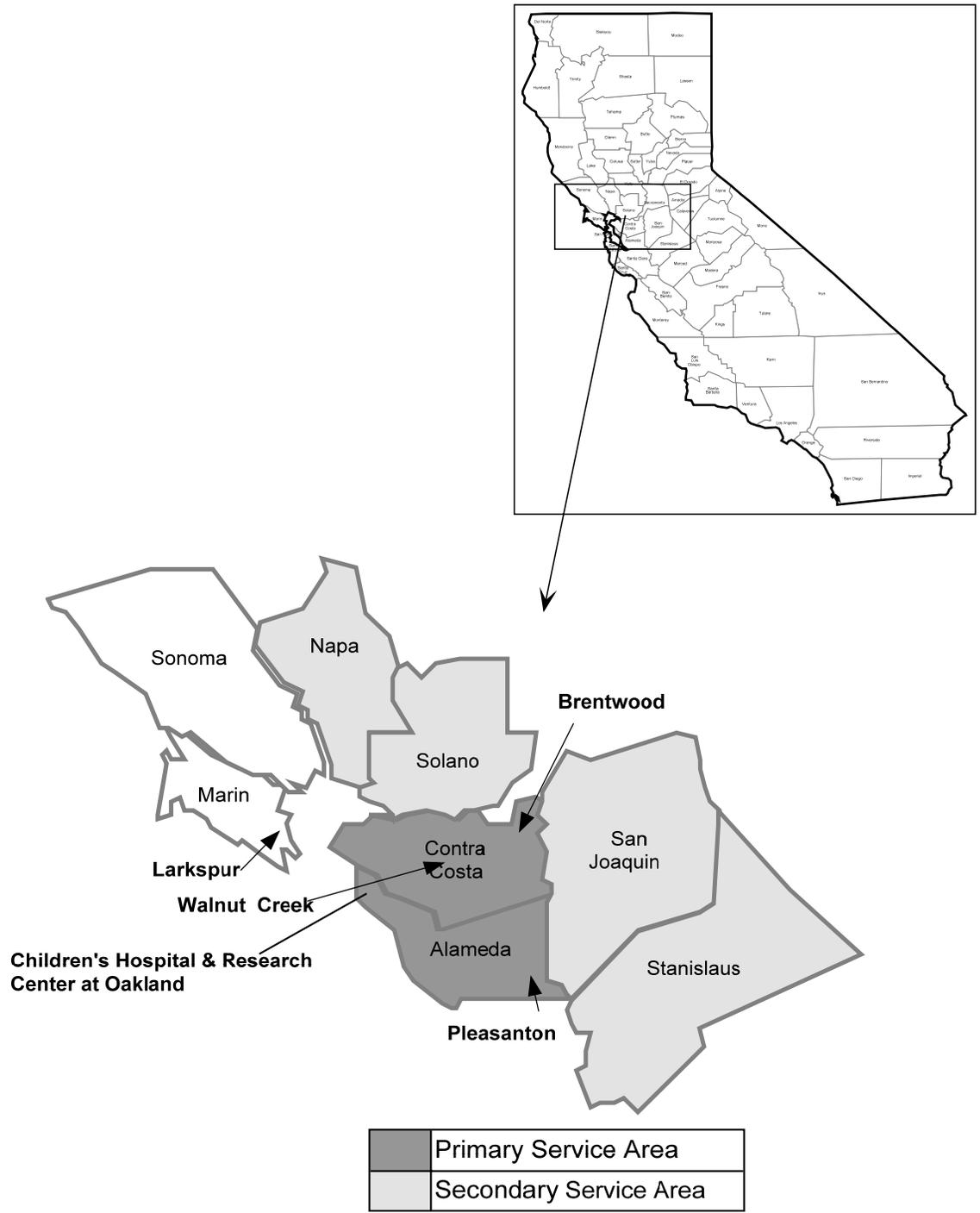
The Corporation defines the Hospital's primary service area as Alameda and Contra Costa Counties, which include the major cities of Oakland, Berkeley, Richmond and Walnut Creek, California (the "Primary Service Area"). The Primary Service Area represents the major population centers of the East Bay region of the San Francisco Bay Area. In 2006, 79.3% of the Hospital's

patient discharges came from the Primary Service Area and 12.3% came from its “Secondary Service Area.” The Corporation defines the Hospital’s Secondary Service Area as four counties in close proximity to the Primary Service Area, namely Napa, Solano, San Joaquin, and Stanislaus Counties.

Due to the referral nature of tertiary services provided at the Hospital, patients from a broad geographic base receive care at the Hospital. The patient service areas outside the Primary and Secondary Service Areas are referred to as outlying areas and consist of all other markets. In 2006, outlying areas accounted for 8.4% of the Hospital’s total patient discharges.

The map on the following page shows the Primary and Secondary Service Areas for the Hospital in 2006.

Map of Service Area



Patient Origin

The table below presents the Hospital's discharge market data for the Primary and Secondary Service Areas and for the outlying areas for the three fiscal years ended December 31, 2004, 2005 and 2006 and for the five months ended May 31, 2006 and 2007.

	Years Ended December 31,						Five Months Ended May 31,			
	2004		2005		2006		2006		2007	
	Discharges	%	Discharges	%	Discharges	%	Discharges	%	Discharges	%
Primary Service Area										
Alameda County	5,017	56.5	5,275	55.4	5,211	55.6	2,329	56.8	2,450	53.9
Contra Costa County	2,191	24.7	2,336	24.5	2,225	23.7	984	24.0	1,097	24.1
Total Primary	7,208	81.2	7,611	79.9	7,436	79.3	3,313	80.8	3,547	78.0
Secondary Service Area										
Napa County	35	0.4	59	0.6	57	0.6	26	0.6	41	0.9
Solano County	425	4.8	498	5.2	547	5.8	222	5.4	283	6.2
San Joaquin County	303	3.4	348	3.7	396	4.2	148	3.6	238	5.2
Stanislaus County	98	1.1	118	1.2	157	1.7	69	1.7	65	1.4
Total Secondary	861	9.7	1,023	10.7	1,157	12.3	465	11.3	627	13.8
Outlying Areas	805	9.1	895	9.4	785	8.4	321	7.8	372	8.2
Total Discharges	8,874	100.0⁽¹⁾	9,529	100.0	9,378	100.0	4,099	100.0	4,546	100.0

Source: Hospital Finance Department based on publicly available information. Data include discharges for all ages and all cases. Information as to all ages and patient origin obtained at time of admission.

⁽¹⁾ Percentage does not total exactly due to rounding.

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Utilization, Market Share Analysis and Competition

The following tables provide utilization levels for the pediatric acute and intensive care patients in the Hospital's Primary and Secondary Service Areas for the years ended December 31, 2003, 2004 and 2005 (the latest full-year data available). Included in the tables are the number of discharged pediatric patients residing in the Primary and Secondary Service Areas, the hospitals from which such patients are discharged, and the counties in which those hospitals are located.

Primary Service Area Hospital Utilization * Pediatric Discharges For Calendar Years 2003, 2004 and 2005⁽¹⁾ Children Ages 0-17

County	Hospital	Years Ended December 31,					
		2003		2004		2005	
		Discharges	Market Share	Discharges	Market Share	Discharges	Market Share
ALAMEDA	CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND	7,189	30.8%	6,795	29.1%	7,235	29.9%
VARIOUS	KAISER HOSPITALS	4,240	18.2%	4,938	21.2%	6,186	25.6%
ALAMEDA	ALTA BATES-SUMMIT MEDICAL CENTER- ALL CAMPUSES ⁽²⁾	3,171	13.6%	2,434	10.4%	1,934	8.0%
CONTRA COSTA	JOHN MUIR MEDICAL CENTER	1,734	7.4%	1,854	7.9%	1,775	7.3%
SANTA CLARA	LUCILE PACKARD CHILDREN'S HOSPITAL AT STANFORD	1,021	4.4%	1,215	5.2%	1,073	4.4%
SAN FRANCISCO	MEDICAL CENTER AT UCSF/MT. ZION	453	1.9%	541	2.3%	544	2.2%
VARIOUS	ALL OTHER HOSPITALS	<u>5,542</u>	<u>23.7%</u>	<u>5,559</u>	<u>23.8%</u>	<u>5,461</u>	<u>22.6%</u>
	TOTAL DISCHARGES	<u>23,350</u>	<u>100.0%</u>	<u>23,336</u>	<u>100.0%</u> ⁽³⁾	<u>24,208</u>	<u>100.0%</u>
Newborns with Minor Complications		8,906		7,686		8,015	

*Excludes normal newborns, neonatology, obstetrics, burns, trauma, rehabilitation, chemical dependency, and mental health service lines.

Source: Office of Statewide Health Planning and Development Discharge Data Set.

⁽¹⁾ Most recent data available.

⁽²⁾ Excludes beds operated by the Corporation through its lease arrangement with Alta Bates-Summit Medical Center.

⁽³⁾ Percentage does not total exactly due to rounding.

**Secondary Service Area Hospital Utilization
Pediatric Discharges For Calendar Years 2003, 2004 and 2005⁽¹⁾
Children Ages 0-17**

		Years Ended December 31,					
		2003		2004		2005	
County	Hospital	Discharges	Market Share	Discharges	Market Share	Discharges	Market Share
VARIOUS	KAISER HOSPITALS	1,575	9.2%	2,174	12.7%	2,189	12.3%
STANISLAUS	DOCTORS MEDICAL CENTER	2,219	13.0%	2,013	11.8%	2,121	11.9%
SAN JOAQUIN	ST. JOSEPH'S MEDICAL CENTER OF STOCKTON	1,633	9.6%	1,578	9.2%	1,683	9.4%
SAN JOAQUIN	SAN JOAQUIN GENERAL HOSPITAL.	1,711	10.0%	1,456	8.5%	1,640	9.2%
SAN JOAQUIN	DAMERON HOSPITAL	1,517	8.9%	1,375	8.0%	1,413	7.9%
STANISLAUS	MEMORIAL HOSPITAL MODESTO	1,335	7.8%	1,131	6.6%	1,115	6.2%
ALAMEDA	CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND	747	4.4%	816	4.8%	989	5.5%
SAN FRANCISCO	MEDICAL CENTER AT UCSF/MT. ZION	595	3.5%	761	4.4%	714	4.0%
SANTA CLARA	LUCILE PACKARD CHILDREN'S HOSPITAL AT STANFORD	263	1.5%	376	2.2%	370	2.1%
VARIOUS	ALL OTHER HOSPITALS	5,437	31.9%	5,448	31.8%	5,620	31.5%
	TOTAL DISCHARGES	17,032	100.0%⁽²⁾	17,128	100.0%	17,854	100.0%
Newborns with Minor Complications		5,567		4,801		5,040	

*Excludes normal newborns, neonatology, obstetrics, burns, trauma, rehabilitation, chemical dependency, and mental health service lines.

Source: Office of Statewide Health Planning and Development Discharge Data Set.

⁽¹⁾ Most recent data available.

⁽²⁾ Percentage does not total exactly due to rounding.

In 2005, there were 8,015 and 5,040 cases of newborns with minor complications in the Primary and Secondary Service Areas, respectively. The Hospital's market shares of 29.9% and 5.5%, for Primary and Secondary Service Areas, respectively, shown in the tables above, are based on total pediatric discharges, including newborns with minor complications. Newborns with minor complications are typically newborn patients who are admitted to the neonatal intensive care units located in the community hospitals in which they were born. Such patients are seldom transferred to referral neonatal centers (such as the Hospital), and the Hospital did not serve any such patients in 2005. Management believes that calculating the Hospital's market share based only on discharges with complications provides a more accurate representation of the Corporation's potential market. Excluding discharges for newborns with minor complications, the Hospital's market shares become 44.7% and 7.9% for the Primary and Secondary Service Areas, respectively.

HISTORICAL FINANCIAL INFORMATION

The following tables of summarized financial information have been derived by management from the consolidated audited statements of changes in unrestricted net assets of the Corporation, the Foundation, CHFN and Family House for fiscal years ended December 31, 2004, 2005 and 2006, which are prepared in conformity with accounting principles generally accepted in the United States of America. This financial information should be read in conjunction with the financial statements, related notes and other financial information included in APPENDIX B. The summary of financial information for the five months ended May 31, 2006 and 2007, shown in the tables below, has been prepared by management, is derived from unaudited consolidated financial statements, and is presented for additional information and analysis. In the opinion of management, this summary reflects all adjustments necessary to present such information in conformity with accounting principles generally accepted in the United States of America and is not necessarily indicative of the results that may be expected for any other interim period or for the full year.

The consolidated audited financial statements of the Obligated Group, CHFN and Family House (collectively, the “System”) for the years ended December 31, 2006 and 2005 are included as APPENDIX B. Management of the Corporation indicates that the net patient service revenue, the excess of revenues, gains and other support over expenses, and the total net assets of CHFN and Family House are not material to the financial performance of the Obligated Group.

The consolidated audited financial statements of the System included as APPENDIX B, the consolidated audited financial data presented in this APPENDIX A for the fiscal years ended 2004, 2005 and 2006 and the unaudited consolidated financial data for the five-month periods ended May 31, 2006 and 2007 presented in this APPENDIX A also reflect the impact of the operations of BCP. The Obligated Group anticipates that BCP will become a member of the Obligated Group if and when it becomes recognized as a 501(c)(3) Organization and provided its meets certain conditions set forth in the Master Indenture. See “INTRODUCTION—Other Affiliated Corporations—BayChildren’s Physicians” herein and APPENDIX C—“SUMMARY OF PRINCIPAL DOCUMENTS—MASTER INDENTURE—Membership in Obligated Group.” As of January 1, 2007, BCP commenced operations as a legal entity separate from the Corporation. For the fiscal years ended December 31, 2004, 2005 and 2006, the operations attributable to BCP account for approximately 4.6%, 5.4% and 5.1%, respectively, of the net patient service revenue of the System, on a consolidated basis.

The Members of the Obligated Group are the sole obligors with respect to the Bonds. None of BCP, CFHN or Family House (collectively, the “Affiliated Entities”) is obligated to make payments with respect to the Bonds. None of the assets or revenues of any of the Affiliated Entities is pledged to secure payments with respect to the Bonds.

**Summarized Consolidated Statements of Operation and Changes in Unrestricted Net Assets
For the Years Ended December 31, 2004, 2005 and 2006 and Five Months
Ended May 31, 2006 and 2007
(Dollars in thousands)**

	Years Ended December 31 (Audited)			Five Months Ended May 31 (Unaudited)	
	2004	2005	2006	2006	2007
UNRESTRICTED REVENUE, GAINS, AND OTHER SUPPORT					
Net patient service revenue	\$217,770	\$253,700	\$269,019	\$117,617	\$130,412
Net assets released for operations	42,157	44,384	47,954	19,761	17,278
Other Income	13,475	15,379	19,658	6,732	8,012
Total unrestricted revenue, gains, and other support	<u>\$273,402</u>	<u>\$313,463</u>	<u>\$336,631</u>	<u>\$144,110</u>	<u>\$155,702</u>
EXPENSES					
Operating expenses	223,884	256,299	292,672	121,331	127,617
Research and specific purpose grant expenses	43,113	47,050	48,886	20,143	19,731
Depreciation and amortization	12,041	12,594	13,325	4,626	4,620
Interest, net	3,368	3,156	3,794	1,573	1,577
Total expenses	<u>\$282,406</u>	<u>\$319,099</u>	<u>\$358,677</u>	<u>\$147,673</u>	<u>\$153,545</u>
Operating income (loss)	<u>\$ (9,004)</u>	<u>\$ (5,636)</u>	<u>\$ (22,046)</u>	<u>\$ (3,563)</u>	<u>\$ 2,157</u>
NONOPERATING GAINS AND (LOSSES)					
Donations	\$(5)	\$200	\$0	\$0	\$0
Investment income (loss)	8,299	11,124	20,707	2,318	4,065
Change in fair value of basis swap	(117)	(8)	793	0	0
Other income	590	564	554	147	461
Total nonoperating gains	<u>\$8,767</u>	<u>\$11,880</u>	<u>\$22,054</u>	<u>\$2,465</u>	<u>\$4,526</u>
EXCESS (DEFICIENCY) OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES	\$(237)	\$6,244	\$8	\$(1,098)	\$6,683
Net assets released for capital purchases	2,582	6,750	1,877	*	*
Changes in unrealized gains/(losses)	3,082	(2,648)	(2,960)	*	*
State and county grants for capital additions	0	0	1,696	*	*
INCREASE IN UNRESTRICTED NET ASSETS	<u>\$5,427</u>	<u>\$10,346</u>	<u>\$621</u>	<u>*</u>	<u>*</u>

* These values are not calculated on a monthly basis for internal financial statements.

Summarized Consolidated Balance Sheets
For the Years Ended December 31, 2004, 2005 and 2006 and Five Months Ended
May 31, 2006 and 2007
(Dollars in thousands)

	Years Ended December 31 (Audited)			Five Months Ended May 31 (unaudited)	
	2004	2005	2006	2006	2007
ASSETS					
Current Assets					
Cash and Investments	\$25,953	\$19,599	\$27,462	\$13,572	\$25,239
Patient accounts receivable, net	33,869	50,002	42,065	35,298	45,549
Grants and contracts receivable	7,490	7,950	9,439	9,579	11,141
Other current assets	45,990	81,568	75,110	97,593	90,756
Total current assets	<u>113,302</u>	<u>159,119</u>	<u>154,076</u>	<u>156,042</u>	<u>172,685</u>
Property, plant and equipment, net	150,103	149,513	152,918	151,461	153,549
Investments, net of current portion	170,224	174,890	181,903	177,562	175,469
Other assets	15,961	16,465	16,598	16,681	17,485
TOTAL ASSETS	<u>\$449,590</u>	<u>\$499,987</u>	<u>\$505,495</u>	<u>\$501,746</u>	<u>\$519,188</u>
LIABILITIES AND NET ASSETS					
Current Liabilities					
Accounts payable and accrued expenses	\$11,937	\$12,336	\$14,277	\$10,333	\$13,445
Accrued payroll and related liabilities	19,490	23,523	23,494	23,153	24,670
Current portion of long-term debt	3,280	2,680	2,750	2,020	4,085
Other current liabilities	4,098	5,446	7,260	4,902	4,625
Total current liabilities	<u>38,805</u>	<u>43,985</u>	<u>\$47,781</u>	<u>\$40,408</u>	<u>\$46,825</u>
Long-term debt, less current maturities	74,920	101,924	99,001	101,325	97,095
Other long-term liabilities	31,597	34,203	33,565	36,537	39,077
Total liabilities	<u>145,322</u>	<u>180,112</u>	<u>180,347</u>	<u>178,270</u>	<u>182,997</u>
Net Assets					
Unrestricted	251,475	261,821	262,442	263,672	272,525
Temporarily & permanently restricted	52,793	58,054	62,706	59,804	63,666
Total Net Assets	<u>304,268</u>	<u>319,875</u>	<u>325,148</u>	<u>323,476</u>	<u>336,191</u>
TOTAL LIABILITIES & NET ASSETS	<u>\$449,590</u>	<u>\$499,987</u>	<u>\$505,495</u>	<u>\$501,746</u>	<u>\$519,188</u>

Sources of Healthcare Revenue

The following is a summary of net patient service revenue by payor source for each of the years ended December 31, 2004, 2005 and 2006 and for the five months ended May 31, 2006 and 2007.

	Net Patient Service Revenue by Payor Source (Dollars in Thousands)*									
	Years Ended December 31						Five Months Ended May 31 (Unaudited)			
	2004	%	2005	%	2006	%	2006	%	2007	%
Medi-Cal/CCS	\$57,818	30.8	\$65,260	31.3	\$76,208	33.3	\$33,433	33.1	\$34,067	33.1
Medi-Cal Managed Care ⁽¹⁾	29,645	15.8	33,744	16.1	31,559	13.8	16,691	16.5	11,214	10.9
Medicare	215	0.1	601	0.3	634	0.3	269	0.3	44	0.0
Managed Care	84,050	44.7	96,033	45.9	108,281	47.3	44,947	44.5	55,108	53.5
Insurance / Self pay	16,167	8.6	13,441	6.4	12,307	5.4	5,610	5.6	2,618	2.5
Total	\$187,895	100.0	\$209,079	100.0⁽²⁾	228,989	100.0⁽²⁾	\$100,950	100.0	\$103,051	100.0

Source: Hospital Finance Department

⁽¹⁾ Medi-Cal Managed Care includes payments received for services rendered to enrollees of Medi-Cal Managed Care plans regardless of whether the Corporation is a contracting provider to such plans.

⁽²⁾ Percentage does not total exactly due to rounding.

*The amounts reported in this table exclude "Supplemental Funding," defined below under "Other Sources of Revenue," and therefore will not match total net patient service revenue shown on the table entitled, "Summarized Consolidated Statements of Operation and Changes in Unrestricted Net Assets," on p. A-17.

The Corporation renders services to eligible patients pursuant to a contractual arrangement with the Medi-Cal program. Under the terms of the contract with the California Medical Assistance Commission, which extends to May 12, 2009, inpatient services are reimbursed on a per-diem basis, while outpatient services are reimbursed based on a schedule of maximum allowances. Under California Welfare and Institutions Code Section 14094, the State of California provides funding for the care of children under the California Children's Services ("CCS") program if their health needs meet certain eligible conditions. These services are reimbursed on a per diem basis if the family meets Medi-Cal guidelines. As of May 31, 2007, the Hospital is a CCS-Approved Center for seventeen clinical areas.

Under federal Medicaid waivers, California has implemented a variety of program models to expand Medi-Cal managed care in specified counties. The program models include Geographic Managed Care, County Organized Health Systems, and "Two-Plan" models in which the State of California contracts with two managed care plans in each designated county to provide for the care of Medi-Cal beneficiaries on a capitated basis. Both Alameda and Contra Costa Counties are currently operating under the Two-Plan model. In Alameda County, one plan is referred to as the "Local Initiative," also called the Alameda Alliance for Health, and the other plan is a commercial HMO plan called "Medi-Cal Blue Cross."

The Corporation is a contracting provider for both the Local Initiative and Medi-Cal Blue Cross in Alameda County. The Corporation derived approximately 16.1% of its net patient service revenue from the Medi-Cal managed care programs in 2005 and 13.8% in 2006. Net patient service

revenue from Medi-Cal managed care includes amounts received from the contracted plans and non-contract payments received for services rendered to enrollees from other counties.

The Corporation’s contracts with payors, including the contracts with the Local Initiative and Medi-Cal Blue Cross, are subject to review, renewal and renegotiations at various times. As part of this process, the Corporation assesses the economics of each payor contract subject to renegotiations. There are no assurances that such renegotiations will be successfully concluded on terms favorable to the Corporation or that such contracts will continue.

Other Sources of Revenue

In addition to fee-for-service Medi-Cal reimbursement and Medi-Cal managed care reimbursement discussed above, the Corporation also receives additional patient-related reimbursement from the State of California. Because the Hospital serves a high proportion of low-income and Medi-Cal-eligible individuals, it qualifies as a “disproportionate share hospital” (“DSH”) under the Medi-Cal program. A hospital’s status as a DSH is determined annually, usually in September or October following the end of the State of California fiscal year (June 30), by the California Department of Health Services. As a DSH, the Corporation receives supplemental payments for inpatient hospital services rendered to Medi-Cal beneficiaries. This funding is received pursuant to two California State Senate Bills: SB 855 and SB 1100 (formerly known as SB 1255).

The Hospital is also a designated pediatric trauma facility and receives supplemental trauma funding from Alameda County and additional matching funds through a California Trauma State Plan Amendment (“Trauma”). Through Alameda County, the Corporation receives a portion of supplemental sales tax funding (“Measure A”) and related State matching dollars. Measure A is an Alameda County ballot measure that passed in 2004 to raise the sales tax for health care for the poor. The increase in the sales tax rate, based on the passage of Measure A, became effective in mid-2004. In addition, because of the Hospital’s pediatric residency program, the Corporation receives graduate medical education (“GME”) funding from the federal government.

The DSH, Trauma, Measure A, GME and any related matching dollars are referred to as “Supplemental Funding.” The table below lists the total Supplemental Funding received by the Hospital for years ended December 31, 2004, 2005 and 2006, and for the five months ended May 31, 2006 and 2007 under these various programs. No assurance can be given that Supplemental Funding will continue at levels shown in the following table.

Supplemental Funding (Dollars in Thousands)⁽¹⁾

	Years Ended December 31			Five Months Ended May 31, (Unaudited)	
	2004	2005	2006	2006	2007
	Disproportionate Share Hospital Funding	\$22,140	\$24,417	\$36,763	\$9,031
Trauma and Measure A Funding	1,953	75	6,054	2,990	67
Graduate Medical Education Funding	7,487	7,255	7,664	2,693	2,030
Total	\$31,580	\$31,747	\$50,481	\$14,714	\$16,051

Source: Hospital Finance Department

⁽¹⁾ All of these funding sources are subject to significant volatility and uncertainty based on the availability of federal, state and county monies for these programs. The above table is based on the fiscal year the funding was received on a cash basis by the Corporation.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL PERFORMANCE

General Overview

The Corporation is one of the leading providers of pediatric healthcare in Northern California. It currently has a market share of approximately 29.9% in its Primary Service Area, defined above. In an effort to increase market share, particularly within the growing Secondary Service Area, management of the Corporation launched several strategic initiatives. Among other initiatives, management of the Corporation has focused on increasing patient volume since experiencing a decline in admissions and average daily census in 2004. Additionally, management has changed its strategic focus from total cost containment to steady growth and recognition of income opportunities.

In 2005, upon the retirement of the previous CEO, Mr. Tiedemann joined the Corporation as President and CEO. Under Mr. Tiedemann's leadership, a senior management team with a broad scope of experience that blends mission and business acumen was organized. (See "Executive Management" above.) Some of the accomplishments of the new Executive Team include:

- CFO oversight of both finances and operations.
- Use of the quality and reputation of the Hospital with managed care programs to secure favorable pricing and terms.
- Implementation of a new medical foundation to help retain physicians and align their financial incentives with the Corporation.
- Implementation and close monitoring of operational indicators. The Corporation has implemented a "daily dashboard" of key success indicators, a bi-weekly productivity report to help with flexible staffing, over-time and contract labor reporting, monthly operational reviews with all departments, and more timely completion of monthly financial statements.
- Development of a portfolio analysis to evaluate program financial performance, allowing the Corporation to focus its marketing and recruitment efforts on strong performers.

Critical Accounting Policies and Estimates

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 amounts reported in the financial statements and accompanying notes. Significant items subject to such estimates and assumptions primarily relate to the collectibility of accounts receivable, valuation of fixed assets, including depreciable lives assigned, valuation of derivative instruments, determination of the other-than-temporary impairments of marketable securities, and the assumptions utilized in valuation of self-insured reserves and retirement plan obligations. Actual results could differ from those estimates and such differences could be material.

Net patient service revenue – The Corporation has agreements with third-party payors that provide for payments to the Corporation 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 an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Premium revenue – The Corporation has agreements with various health maintenance organizations (“HMOs”) to provide medical services to subscribing participants. Under these arrangements, the Corporation receives monthly capitation payments based on the number of each HMO’s participants, and recognizes revenue during the period regardless of services actually performed by the Corporation. In addition, the HMOs make fee-for-service payments to the Corporation for certain covered services based upon discounted fee schedules.

Charity care and other community benefits – The Corporation provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates for that service. The Corporation accepts all patients in its Primary and Secondary Service Areas, regardless of their ability to pay. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. For the fiscal year ended December 31, 2006, the cost to the Corporation of charity care and other community benefits was as follows:

Charity Care	\$4,366,700
Bad Debt	\$13,937,700
Under-Reimbursed Care (estimated)	\$38,715,253
Physician Back-up Services	\$1,252,866
Total	\$58,272,519

Grants and contributions – The Corporation receives grants from federal agencies and other third parties, as well as contributions from private organizations. Government grants are reimbursed based on actual expenses incurred or units of services provided. Revenue from these grants is recognized either when expenses are incurred or when services are provided. Revenue recognition depends on the grant award agreements.

Contribution revenue is reported when cash is received, unconditional promises are made, or ownership of other assets is transferred to the Corporation. Contributions received may be designated by the donor for restricted purposes or may be without restriction as to their use. Net assets, revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions.

When there are no legally imposed restrictions on contributions or on income earned from restricted contributions, they are recorded as other unrestricted revenue when received. Contributions restricted by donors as to use or time period are recorded as temporarily restricted net assets until used in the manner designated or upon expiration of the time period.

Temporarily restricted contributions are generally subject to donor-imposed stipulations that may or will be met, either by actions of the Corporation and/or the passage of time. When a restriction is met, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statement of changes in net assets as net assets released from restrictions.

Permanently restricted contributions are subject to donor-imposed stipulations that they be maintained by the Corporation in perpetuity.

Investments – All investments in debt securities and short-term and long-term equity investments are measured at fair value in the balance sheet. Investment income or loss is included in unrestricted net assets unless their use is temporarily or permanently restricted by a donor or by law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses.

Comparative Financial Results

Fiscal Year-Ended December 31, 2004

During fiscal 2004, the Corporation continued to face financial challenges and, accordingly, the System posted a loss for the year. This loss was due to the continued deterioration of the payor mix (high Medi-Cal and low commercial volume), continued declining volumes, and expense challenges in part due to the Bay Area cost of living and a high percentage of unionized labor at the Hospital.

For the year ended December 31, 2004, the System reported a deficiency of revenue over expenses of (\$237,000) and an increase in unrestricted net assets of \$5,427,000. Total unrestricted revenues were \$273,402,000, reflecting an increase of 0.5% over fiscal 2003. Total net assets as of December 31, 2004 were \$304,268,000.

The increase in unrestricted net assets was due to the unrealized gains in the marketable securities portfolio of \$3,082,000 plus net assets released for capital purchases of \$2,582,000 and offset partially by the net operating loss of (\$9,004,000) and non-operating gains of \$8,767,000 (mostly realized investment gains).

Operating expenses increased 3.3% from \$216,659,000 in 2003 to \$223,884,000 in 2004.

In 2004, the Corporation generated the following volume statistics: patient days of 47,546, inpatient surgical operations of 3,353, outpatient surgical operations of 4,543, and outpatient visits of 186,313.

Unrestricted cash and investments totaled approximately \$165,139,000 or 224 days cash on hand as of December 31, 2004.

Fiscal Year-Ended December 31, 2005

The Corporation's new CEO started in January 2005, and under his leadership, management of the Corporation began to focus on growth. The Corporation also aggressively pursued increases in supplemental funding and was able to obtain a 41.6% increase in such revenues on an accrual

basis from \$31,508,000 in fiscal year 2004 to \$44,621,000 in fiscal year 2005. The increase resulted primarily from DSH payments and the increased sales tax levied by Alameda County (Measure A). The Corporation also launched a new branding campaign, hired a new CFO, recruited a new COO, and hired a Regional Development Vice President to commence formation of BCP, the medical foundation. An increase in volume, payor mix and realized investment income over the prior year helped the hospital achieve an excess of revenue over expenses.

For the year ended December 31, 2005, the System reported an excess of revenue over expenses of \$6,244,000 and an increase in unrestricted net assets of \$10,346,000. Total unrestricted revenues were \$313,463,000, reflecting an increase of 14.7% over fiscal year 2004. Total net assets as of December 31, 2005 were \$319,875,000.

The increase in unrestricted net assets was due primarily to the realized gains in the System's marketable securities portfolio of \$11,124,000 (offset by an unrealized loss of \$2,648,000) plus net assets released for capital purchases of \$6,750,000. This was all reduced by the operating loss of (\$5,636,000).

Operating expenses increased 14.5% from \$223,884,000 in 2004 to \$256,299,000 in 2005.

In 2005, the Corporation generated the following volume statistics: patient days of 52,216, inpatient surgical operations of 3,418, outpatient surgical operations of 4,657, and outpatient visits of 203,354.

Unrestricted cash and investments totaled approximately \$164,927,000 or 196 days cash on hand as of December 31, 2005.

Fiscal Year-Ended December 31, 2006

During the fiscal year 2006, the corporation posted an operating loss of \$22,046,000. This was due in part as of result of several key initiatives that were funded, but which associated budgeted earnings were not realized. These initiatives included the following:

- **Capacity.** A lease was signed at the end of 2005 with Alta Bates-Summit Medical Center in Oakland to add 20 beds to the Hospital's 170-bed licensed capacity to its Oakland facility. Due to licensing constraints and building approval delays, the unit was not placed into full service until late in the year. As a result, expenses from the unit exceeded revenues in 2006.
- **Call Center.** A new Call Center, designed to triage high-value calls from the Hospital's key referral sources, was not on line until early 2007, affecting volume and, to an extent, payor mix.
- **Expenses.** Staffing and other expenses, including consulting fees, were not reduced to reflect decreases in patient volume as compared to budget, and, thus, such expenses increased at a faster rate than revenues. Operating expenses increased 14.2% from \$256,299,000 in 2005 to \$292,672,000 in 2006.

In an effort to improve operations, an action plan to increase cost savings was developed and launched in the fall of 2006. This has resulted in a reduction in staff (primarily through attrition), a renewed focus on labor productivity, elimination of most consulting arrangements, renegotiation of service contracts, and consolidation of the COO and CFO positions.

Despite the setbacks described above, the Corporation managed to increase out patient volume, and improve overall net revenue through re-negotiations with managed care plans and the implementation of contract management software. The System posted significant interest and dividends, resulting in an excess of revenues over expenses of \$8,000 for the fiscal year of 2006 and an increase in unrestricted net assets of \$621,000 during the same period. Total unrestricted revenues were \$336,631,000, reflecting a 7.4% increase over fiscal year 2005. Total net assets as of December 31, 2006 were \$325,148,000.

The increase in unrestricted net assets was due primarily to nets assets released for capital purchases and state and county grants for capital additions, offset by an unrealized loss in the System's marketable securities portfolio of (\$2,960,000).

In 2006, the Corporation generated the following volume statistics: 53,163 patient days, inpatient surgical operations of 3,499, outpatient surgical operations of 4,958, and outpatient visits of 211,955.

Unrestricted cash and investments totaled approximately \$176,951,000 or 187 days cash on hand as of December 31, 2006.

The Five-Month Period Ended May 31, 2007 and 2006 (Unaudited)

During the five months ended May 31, 2007, the 2006 key initiatives were fully implemented: increased capacity with the opening of the additional licensed beds leased from Alta Bates – Summit Medical Center; expense control through very close financial tracking to budget for every department within the Corporation; revenue capture through the use of patient account audits; and increased patient volume and improved payor reimbursement through payor renegotiations. All of these factors contributed to improved financial results that met management's expectations. In 2007, compensation for all managers was changed to include a management incentive program that is tied to patient satisfaction, hospital financial operating results, employee safety, quality measures, and individual departmental operating results as compared to the 2007 budget.

The System posted excess of revenues over expenses of \$6,683,000 for the five months ended May 31, 2007, compared to a loss of (\$1,098,000) for the five months ended May 31, 2006. Total unrestricted revenues were \$155,702,000, reflecting an 8.0% increase over the comparable period in 2006. Total net assets as of May 31, 2007 were \$336,191,000.

The increase in unrestricted net assets was due to strong income from operations of \$2,157,000, realized gains in the System's marketable securities portfolio of \$4,065,000 and net assets released for capital purchases.

Operating expenses for the five months ended May 31, 2007 increased 5.2% from \$121,331,000 in 2006 to 127,617,000 in 2007.

For the five months ended May 31, 2007, the Corporation generated the following volume statistics: 24,685 patient days (versus 23,730 for the same period in 2006), inpatient surgical operations of 1,482 (versus 1,330 for the same period in 2006), outpatient surgical operations of 2,189 (versus 2,166 for the same period in 2006), and outpatient visits of 97,911 (versus 90,825 for the period in 2006).

Unrestricted cash and investments totaled approximately \$165,402,000 or 168 days cash on hand as of May 31, 2007.

The Obligated Group's ability to continue to generate investment income is dependent on market conditions and the composition of its investment portfolio. The value of the investment portfolio may fluctuate significantly from time to time, depending on the value of the underlying securities. Changes in the level of investment earnings may have a significant effect on the overall financial condition of the Obligated Group.

Liquidity and Capital Resources

The following table shows days cash on hand as of December 31, 2004, 2005 and 2006 and as of May 31, 2006 and 2007 for the System on a consolidated basis (unaudited):

	As of December 31			As of May 31 (Unaudited)	
	2004	2005	2006	2006	2007
Unrestricted Cash and Investments ⁽¹⁾	\$165,138,900	\$164,927,200	\$176,951,300	\$158,402,800	\$165,401,800
Total Expenses	\$282,406,100	\$319,099,300	\$358,676,800	\$147,673,000	\$153,545,000
Less Depreciation	(\$12,041,200)	(\$12,594,100)	(\$13,325,000)	(\$4,626,000)	(\$4,620,000)
Subtotal	\$270,364,900	\$306,505,200	\$345,351,800	\$143,047,000	\$148,925,000
# of days in year	366	365	365	151	151
Daily Operating Expenses	\$738,702	\$839,740	\$946,169	\$947,331	\$986,258
Days Cash on Hand	223.55	196.40	187.02	167.21	167.71

⁽¹⁾ Cash and investments are shown net of donor restrictions and assets limited as to use.

Capitalization

The following table sets forth the actual capitalization of the System, on a consolidated basis, as of December 31, 2005 and 2006 as derived from the audited financial statements. The table also sets forth the pro forma capitalization of the System, on a consolidated basis, as of December 31, 2006, adjusted to reflect the issuance of the Bonds in the aggregate principal amount of \$60,100,000, the advance refunding of the Refunded Securities, and the equity defeasance of the 1988 Bonds and 1994 Bonds, as if such transactions had occurred on December 31, 2006, without reflecting any expenses or savings to be incurred by the Obligated Group in connection with such transactions. See “PLAN OF FINANCE” and “THE OBLIGATED GROUP – Outstanding Indebtedness” in the body of this Official Statement.

Capitalization (Unaudited) (dollars in thousands)

	December 31, 2005	December 31, 2006	
	Actual	Actual	Pro Forma
Existing long-term debt, less current maturities	\$101,924	\$99,001	\$30,000
The Bonds	-	-	60,100
Total long-term debt	101,924	99,001	90,100
Unrestricted net assets	261,821	262,443	262,443
Total capitalization	\$363,745	\$361,444	\$352,543
Total long-term debt as a percentage of total capitalization	28.0%	27.4%	25.6%

Capital Planning and Seismic Compliance

California State Senate Bill 1953 (“SB 1953”) requires that after January 1, 2008, any acute care hospital building must meet minimum seismic safety standards established by the California Office of Statewide Planning and Development. The Corporation has requested and received an extension to January 1, 2013 to comply with these SB 1953 requirements. See “BONDHOLDERS’ RISKS—Other Risk Factors—Earthquakes and Seismic Compliance” in the front part of this Official Statement for further discussion of SB 1953 requirements and deadlines. Management of the Corporation expects that its facilities will be in compliance with requirements of SB 1953 by the deadlines established under SB 1953.

To better serve patients in its growing service areas and to address SB 1953 requirements, the Corporation is exploring development of a new tertiary care pediatric facility in its Primary Service Area, which it currently estimates would have approximately 240 beds. Oversight of this development is being directed by a steering committee, which is reviewing programming and space requirements for such a new facility. Preliminary cost estimates for such a new facility are at least \$650 million. The Corporation expects to fund such costs through a combination of public funds, charitable contributions, cash and debt. During 2008, the Corporation anticipates that voters in

Alameda County will be asked to approve a ballot measure to impose a parcel tax that would secure bonds to be issued by Alameda County to a pay portion of the costs of the new pediatric care facility for the Corporation. If such ballot measure does not receive the legally required two-thirds voter approval, the Corporation would pursue other less costly options for complying with SB 1953, including retrofitting the Hospital's current campus and converting part of the Hospital to non-hospital uses. Because retrofitting would disrupt operations, the Corporation would undertake the required retrofitting in phases. Whether at a new facility or at its existing Hospital facilities, the Corporation remains committed to providing primary pediatric care in its Primary Service Area.

Historical and Pro Forma Debt Service Coverage

The following table sets forth the Debt Service Coverage Ratio of the System, on a consolidated basis, for the fiscal year ended December 31, 2006 based on Annual Debt Service for that period. The table also sets forth, for the fiscal year ended December 31, 2006 and the five months ended May 31, 2007, the pro forma Maximum Debt Service Coverage Ratio of the Obligated Group, based on Maximum Annual Debt Service assuming the issuance of the Bonds in the aggregate principal amount of \$60,100,000, the advance refunding of the Refunded Securities, and the equity defeasance of the 1988 Bonds and 1994 Bonds, as if such transactions had occurred on January 1, 2006, and January 1, 2007, respectively, without reflecting any expenses or savings to be incurred by the Obligated Group in connection with such transactions. See "PLAN OF FINANCE" and "THE OBLIGATED GROUP – Outstanding Indebtedness" in the body of this Official Statement.

Debt Service Coverage
(Dollars in Thousands)

	December 31, 2006	May 31, 2007
Income Available for Debt Service:		
Excess (Deficiency) of Revenue, Gains and Other Support Over Expenses	\$(785)	\$6,683
Add: Interest ⁽¹⁾	5,803	2,395
Add: Depreciation and Amortization	<u>13,325</u>	<u>4,620</u>
Income Available for Debt Service	\$18,343	\$13,698
Annual Debt Service	\$8,689	-
Debt Service Coverage Ratio	2.1x	-
Pro Forma Maximum Annual Debt Service ⁽²⁾	\$5,964	\$2,485 ⁽³⁾
Pro Forma Maximum Debt Service Coverage Ratio	3.1x	5.5x ⁽³⁾

- (1) Interest expense as shown in the audited and unaudited financial statements is net of related interest income and, therefore, does not correspond to the amounts reported in the table above, which include gross interest expense, in accordance with the Master Indenture.
- (2) Represents scheduled maximum principal and interest payments for any fiscal year on long-term debt that will be outstanding following the issuance of the Bonds, which will include the Bonds and the 2005 Bonds, calculated in accordance with the Master Indenture. Assumes the refunding of the Refunded Securities, and the defeasance of the 1988 Bonds and the 1994 Bonds. In accordance with the Master Indenture, debt service on the 2005 Bonds incorporates payments under the Preexisting Swap Agreement and certain guaranty payments made to the Foundation, and is calculated assuming an interest rate of 5.03% and level annual debt service over 30 years beginning in 2009.
- (3) With respect to May 31, 2007, pro forma Maximum Annual Debt Service and pro forma Maximum Debt Service Coverage Ratio reflect five twelfths of pro forma Maximum Annual Debt Service.

OTHER INFORMATION

Medical Staff

The Hospital medical staff (“Medical Staff”) consisted of 547 physicians and dentists as of June 29, 2007, including 198 hospital-based physicians. The average age of the Medical Staff is 48. Hospital policy requires all physicians to be board-certified; however, new physicians have up to two years to receive their certification. As of June 29, 2007, 84.0% of the Medical Staff was board-certified. In 2006, the Hospital credentialed about 65 new physicians. On average, there are 40 resignations per year from the Medical Staff.

As shown by the following table, the Medical Staff includes 198 Active and 349 Courtesy staff members and represents the following specialties:

Specialties of Admitting Staff

Specialty	Active	Courtesy*	Total
Adolescent Medicine	1	0	1
Allergy/Immunology	0	2	2
Ambulatory Services	4	0	4
Anesthesiology	12	6	18
Cardiology	7	2	9
Child Development	4	1	5
Child Psychiatry	3	1	4
Clinical Psychology	4	26	30
Critical Care	7	3	10
Dentistry	0	17	17
Emergency Medicine	9	8	17
Employee Health	0	2	2
Endocrinology	4	2	6
Family Practice	0	5	5
Gastroenterology	2	6	8
General Surgery	0	2	2
Hematology/Oncology	13	4	17
Infectious Disease	3	1	4
Internal Medicine	1	1	2
Medical Genetics	2	0	2
Neonatology	12	10	22
Nephrology	2	3	5
Neurology	4	4	8
Neurosurgery	3	8	11
No Specialty	0	1	1
Ophthalmology	5	9	14
Oral Surgery	0	3	3
Orthodontics	0	2	2
Orthopedics	2	10	12
Otolaryngology	2	14	16
Pathology	1	2	3
Pediatric Surgery	6	1	7
Pediatrics	62	164	226
Pedodontics	3	4	7
Plastic Surgery	4	6	10
Pulmonary Medicine	2	6	8
Radiology	5	4	9
Rehabilitation	3	1	4
Rheumatology	1	0	1
Thoracic Surgery	2	4	6
Urology	3	4	7
TOTAL	198	349	547
PERCENT	36.2%	63.8%	100.0%

* Courtesy staff are defined as practitioners, each of whom meets the requirements for Medical Staff membership but not the criteria for Active Staff status. Once appointed, they must continue to meet the responsibilities of Courtesy Staff membership.

Source: Hospital Medical Staff Records.

The following table sets forth the top ten admitting physicians in 2006.

Physician	Specialty	Admissions	Patient Days
Saulys, Augusta	Emergency	660	2,268
Mccarten-Gibbs, Kevan	Emergency	571	2,000
Whitelaw, Kevin	Emergency	563	2,147
Henderson, Ellen L.	Emergency	554	1,891
Baker, Chris	Emergency	551	2,147
Johnson, Alan M	Emergency	494	1,975
Hart, Lisa S.	Emergency	435	1,436
Bell, Michael D.	Emergency	371	1,338
Mansour, Karim	Emergency	326	1,186
Morris, Claudia R.	Emergency	307	1,112
Total		4,832	17,500

Source: Hospital Finance Department

The following table sets forth the top ten non-emergency direct admitting physicians in 2006.

Physician	Specialty	Admissions	Patient Days
Chaconas, Ted J.	Pediatrics	194	778
Sun, Peter	Neurosurgery	146	724
Hoffinger, Scott A.	Orthopedics	125	368
Policy, James F.	Orthopedics	112	731
Torkildson, Joseph	Hematology	90	676
Golden, Carla B.	Hematology	73	574
Reed, Thomas D.	Critical Care	69	657
Flori, Heidi R.	Critical Care	67	515
Feusner, James H.	Hematology	64	647
Reinhartz, Olaf	Thoracic Surgery	64	600
Total		1,004	6,270

Once a patient is admitted, the responsibility for patient care passes to an attending physician. The following table sets forth the top four attending physician groups, responsible for 46.4% of all 2006 admissions.

Physician Group	Specialty	# of Physicians⁽¹⁾	Admissions	Patient Days
Hospitalists Medical Associates ⁽²⁾	Pediatrics	10	1,494	6,433
Pediatric Hematology/Oncology Group ⁽³⁾	Hematology/ Oncology	17	1,253	7,615
Pediatric Surgical Associates of the East Bay ⁽³⁾	Pediatric Surgery	7	1,030	3,448
Community Physicians	Pediatrics	24	561	2,119
Total, Top Four Physician Groups		58	4,338	19,615
Total, Hospital		547	9,351	53,163
Percent of total		10.6%	46.4%	36.9%

Source: Hospital Finance Department

⁽¹⁾ May not conform to Specialties of Admitting Staff Table on page A-31 due to physician turnover during the year.

⁽²⁾ Physicians employed by BCMG.

⁽³⁾ Independent physician group under contract with the Corporation.

Nursing Staff

The nursing staff of the Hospital consisted of 700 registered nurses as of the end of June 2007. Of this number, 620 nurses (88.6%) provide services in the inpatient nursing units, including the Emergency Department and Surgical Services. Fifty-nine percent of the nurses work full-time, and the remaining staff work part-time or per diem. Thirty certified pediatric nurse practitioners provide their services in most of the Hospital's subspecialty areas.

Approximately 350 nurses have advanced certifications to support their clinical roles. These certifications include:

<u>Clinical Role</u>	<u>% of Total</u>	<u>Certification</u>
Emergency Department	100%	Pediatric Advanced Life Support Trauma Nurse Core Curriculum
NICU/Transport Team	100%	Neonatal Resuscitation Program
Post Anesthesia Care Unit	100%	Pediatric Advanced Life Support
PICU/Transport Team	100%	Pediatric Advanced Life Support

The nursing division provides training and education for twelve nursing schools in the San Francisco Bay Area. This pool of new nursing graduates serves as the primary recruitment source for the Hospital's available nursing positions.

Nursing staff turnover in 2006 was 5.5%, whereas the industry norm for turnover in California is approximately 10.0% to 20.0%. Similarly, the vacancy rate on the nursing staff as of March 2007 was 3.5%, while hospital nursing shortages in California ranged from 11.0% to 14.0% in 2005. Nursing shortages at the Hospital are covered by temporary or registry staff.

Employee and Labor Relations

As of May 31, 2007, the Corporation employed 2,545 employees or 2,026 full-time equivalents. Currently, 1,291 or 50.7% of the employees of the Corporation are represented by six different labor unions. The Cooks who were formally represented by SEIU-Local 2850 have joined SEIU-Local 250 with the same expiration date of April 30, 2009.

The Hospital is currently in the process of bargaining for a new contract with the California Nurses Association, the union representing 88.6% of the registered staff nurses at the Hospital. The current contract has been extended through September 29, 2007. The Hospital expects a mutually satisfactory conclusion to these negotiations.

From time to time, the Corporation and various unions have filed grievances with the National Labor Relations Board ("NLRB") and other actions in court concerning union issues. At this time, no dispute is considered by management to be material to the Obligated Group.

Pension and Deferred Compensation

The Corporation has a noncontributory Defined Benefit Pension Plan, which covers substantially all employees, except those who are members of Local 39 Operating Engineers Union, for which the Corporation makes a contribution to the Local 39 Pension Trust based on an hourly rate per hour worked per worker.

For the Defined Benefit Plan, benefits are based on years of service and the employee's compensation during the last ten years of employment for years of service for employees retiring prior to December 31, 2004 and the last five years of service for employees retiring after December 31, 2005. The Corporation's funding policy has been to contribute annually the minimum actuarially determined amount with additional contributions based on management's judgment. Contributions are intended to provide not only for benefits attributed to service to date, but also for those expected to be earned in the future.

The pension plan's assets are invested in common stocks, corporate and government bonds, convertible securities and money market funds. The plan is qualified under the Employee Retirement Income Security Act of 1974 ("ERISA"). Audited financial statements of the plan are available. The most recent actuarial valuation of the pension plan, prepared by Watson Wyatt Worldwide of San Francisco and dated January 2007, indicated that the market value of the plan assets was 120.6% of the present value of accumulated benefits as of December 31, 2005.

Insurance and Risk Management

The Corporation currently carries healthcare entity comprehensive liability insurance coverage that includes protection for general liability, employee benefit liability, and professional liability protecting the Obligated Group and all employees acting within the scope of their duties against professional liability. This coverage is provided by BETA Health Care Group, a California joint powers authority. The Corporation's current professional liability insurance contract is renewed annually in July. The Corporation contracts with commercial insurance carriers for workers' compensation, unemployment, health, all-risk property (excluding earthquake), directors' and officers' liability, automobile liability, fiduciary responsibility, crime insurance, and miscellaneous other coverages. Management considers the coverage, deductibles, and terms of all such insurance to be consistent with industry norms and prudent management.

Because the Obligated Group's worker's compensation liability is insured under a large dollar deductible program, the System's audited financial statements describe this as "self-insurance;" however, in the event that the deductible is exceeded, coverage for claims above this sum exists. The Obligated Group is self-insured for the PPO component of its employer health insurance coverage.

The Corporation, on behalf of the Obligated Group, maintains excess liability policies, as appropriate, with coverage, deductibles, and terms that management deems consistent with industry norms and prudent management.

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**CHILDREN'S HOSPITAL & RESEARCH CENTER
AT OAKLAND**

**INDEPENDENT AUDITOR'S REPORT
AND
CONSOLIDATED FINANCIAL STATEMENTS
WITH
SUPPLEMENTAL INFORMATION**

DECEMBER 31, 2006 AND 2005

CONTENTS

	PAGE
INDEPENDENT AUDITOR'S REPORT	1
CONSOLIDATED FINANCIAL STATEMENTS	
Balance sheets	2 - 3
Statements of operations and changes in unrestricted net assets	4
Statements of changes in net assets	5
Statements of cash flows	6 - 7
Notes to financial statements	8 - 27
SUPPLEMENTAL INFORMATION	
Consolidating balance sheets	28 - 31
Consolidating statements of operations and changes in unrestricted net assets	32 - 33
Consolidating statements of changes in net assets	34 - 35

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Children's Hospital & Research Center at Oakland

We have audited the accompanying consolidated balance sheets of Children's Hospital & Research Center at Oakland (a California non-profit corporation) as of December 31, 2006 and 2005, and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Children's Hospital & Research Center at Oakland's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 consolidated financial position of Children's Hospital & Research Center at Oakland at December 31, 2006 and 2005, and the consolidated results of its operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements of Children's Hospital & Research Center at Oakland, taken as a whole. The accompanying supplemental schedules of the consolidating balance sheets, consolidating statements of operations and changes in unrestricted net assets and consolidating statements of changes in net assets for the years ended December 31, 2006 and 2005, are presented for purpose of additional analysis and are not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied to the audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

Moss Adams LLP

San Francisco, California
May 24, 2007

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2006 AND 2005**

	<u>2006</u>	<u>2005</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 17,312,100	\$ 7,232,100
Investments	10,150,400	12,367,300
Assets limited as to use, held by trustee	39,053,400	45,506,800
Patient accounts receivable, net of allowance for doubtful accounts of \$8,168,900 for 2006 and \$6,925,600 for 2005	42,065,200	50,002,300
Estimated third-party payor settlements	-	253,700
Grants and contract receivables	9,438,900	7,950,200
Other receivables	30,244,100	30,209,800
Supplies	2,882,000	2,816,500
Prepaid expenses	<u>2,930,200</u>	<u>2,780,200</u>
Total current assets	154,076,300	159,118,900
ASSETS LIMITED AS TO USE, HELD BY TRUSTEE, net of current portion	14,088,700	13,270,400
PROPERTY, PLANT, AND EQUIPMENT, net	152,918,000	149,512,500
INVESTMENTS, net of current portion	181,903,300	174,890,300
OTHER ASSETS	<u>2,508,900</u>	<u>3,194,900</u>
Total assets	<u>\$ 505,495,200</u>	<u>\$ 499,987,000</u>

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2006 AND 2005**

	2006	2005
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	\$ 14,276,400	\$ 12,336,100
Accrued payroll and payroll related liabilities	23,494,100	23,523,200
Deferred revenue	5,184,300	5,445,700
Estimated third-party payor settlements	2,076,400	-
Current portion of long-term obligations	2,750,000	2,680,000
Total current liabilities	47,781,200	43,985,000
ACCRUED PROFESSIONAL LIABILITY	2,791,800	2,616,700
ACCRUED WORKERS' COMPENSATION LIABILITY	15,327,600	14,471,000
LONG-TERM OBLIGATIONS, net of current portion	99,001,000	101,923,500
OTHER LONG-TERM LIABILITIES	15,445,700	17,116,200
Total liabilities	180,347,300	180,112,400
COMMITMENTS AND CONTINGENCIES (Note 9)		
NET ASSETS		
Unrestricted	262,442,500	261,821,400
Temporarily restricted	45,433,200	42,387,600
Permanently restricted	17,272,200	15,665,600
Total net assets	325,147,900	319,874,600
Total liabilities and net assets	\$ 505,495,200	\$ 499,987,000

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN
UNRESTRICTED NET ASSETS
YEARS ENDED DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
UNRESTRICTED REVENUE, GAINS, AND OTHER SUPPORT		
Net patient service revenue	\$ 269,019,100	\$ 253,700,000
Other operating revenues	19,657,900	15,379,200
Net assets released from restrictions used for operations	<u>47,954,100</u>	<u>44,383,700</u>
Total unrestricted revenues, gains, and other support	<u>336,631,100</u>	<u>313,462,900</u>
EXPENSES		
Salaries and wages	151,638,000	134,286,600
Employee benefits	44,816,900	42,842,600
Supplies	32,245,300	27,159,200
Research and specific purpose grant expenses	48,886,400	47,050,200
Professional fees	19,903,000	15,817,900
Insurance and other direct expense	16,935,900	14,720,900
Depreciation and amortization	13,325,000	12,594,100
Purchased services	13,194,500	12,322,000
Provision for bad debts	13,937,700	9,149,700
Interest, net	<u>3,794,100</u>	<u>3,156,100</u>
Total expenses	<u>358,676,800</u>	<u>319,099,300</u>
Operating loss	<u>(22,045,700)</u>	<u>(5,636,400)</u>
NONOPERATING GAINS AND (LOSSES)		
Contributions	-	200,000
Investment income	20,706,600	11,123,700
Change in fair value of basis swap	793,600	(7,900)
Other	<u>553,800</u>	<u>565,000</u>
Total nonoperating gains	<u>22,054,000</u>	<u>11,880,800</u>
EXCESS OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES		
	8,300	6,244,400
Change in net unrealized gains and (losses) on investments	(2,959,600)	(2,647,500)
State and county grants for capital additions	1,695,300	-
Net assets released from restrictions for capital additions	<u>1,877,200</u>	<u>6,749,500</u>
Increase in unrestricted net assets	<u>\$ 621,200</u>	<u>\$ 10,346,400</u>

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2006 AND 2005**

	2006	2005
EXCESS OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES	\$ 8,300	\$ 6,244,400
Change in net unrealized gains and (losses) on investments	(2,959,600)	(2,647,500)
State and county grants for capital additions	1,695,300	-
Net assets released from restrictions for capital additions	1,877,200	6,749,500
Increase in unrestricted net assets	621,200	10,346,400
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS		
Contributions	12,562,500	14,859,100
Grants	39,613,400	37,449,300
Change in unrealized gains and losses on investments	205,900	46,600
Investment income	439,300	185,200
Net assets released from restrictions for operations	(47,954,100)	(44,383,700)
Net assets released from restrictions for capital additions	(1,877,200)	(6,749,500)
Other	55,700	159,300
Increase in temporarily restricted net assets	3,045,500	1,566,300
CHANGES IN PERMANENTLY RESTRICTED NET ASSETS		
Contributions	1,185,800	3,598,200
Change in unrealized gains and losses on investments	420,800	95,400
Increase in permanently restricted net assets	1,606,600	3,693,600
Increase in net assets	5,273,300	15,606,300
NET ASSETS, beginning of year	319,874,600	304,268,300
NET ASSETS, end of year	\$ 325,147,900	\$ 319,874,600

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase in net assets	\$ 5,273,300	\$ 15,606,300
Adjustments to reconcile the increase in net assets to net cash provided by operating activities		
Depreciation and amortization	13,325,000	12,594,100
Provision for bad debts	13,937,700	9,149,700
Non-cash contributions	(385,000)	-
Net realized and unrealized gains and losses on investments	(8,409,100)	2,434,600
Donor restricted contributions	(13,748,300)	(18,457,300)
Gain on sale of assets	(2,708,000)	22,700
Change in fair value of basis swap	(793,600)	7,900
Changes in operating assets and liabilities:		
Patient accounts receivable, net	(6,000,600)	(25,283,200)
Grants and contract receivables	(1,488,700)	(460,300)
Other receivables	(34,300)	(6,510,700)
Supplies	(65,500)	(612,100)
Prepaid expenses	(150,000)	(373,400)
Other assets	686,000	(489,400)
Accounts payable and accrued expenses	1,940,300	399,600
Accrued payroll and payroll related liabilities	(29,100)	4,033,200
Deferred revenue	(261,400)	1,347,700
Estimated third-party payor settlements	2,330,300	3,234,900
Accrued professional liability	175,100	331,900
Accrued workers' compensation liability	856,600	303,800
Other long-term liabilities	(1,670,500)	1,970,300
	<u>2,780,200</u>	<u>(749,700)</u>
Net cash from operating activities		
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant, and equipment	(16,345,600)	(12,662,100)
Change in assets limited as to use	11,627,200	(31,343,400)
Net change in investments	328,800	(7,897,600)
Proceeds on sale of assets	-	646,000
Gain on basis swap	793,600	(7,900)
	<u>(3,596,000)</u>	<u>(51,265,000)</u>
Net cash from investing activities		

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2006 AND 2005**

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Donor restricted contributions	13,748,300	18,457,300
Borrowing on long-term obligations	-	30,000,000
Payments on long-term obligations	<u>(2,852,500)</u>	<u>(3,596,400)</u>
Net cash from financing activities	<u>10,895,800</u>	<u>44,860,900</u>
NET INCREASE (DECREASE) IN CASH and CASH EQUIVALENTS	10,080,000	(7,153,800)
CASH and CASH EQUIVALENTS, beginning of year	<u>7,232,100</u>	<u>14,385,900</u>
CASH and CASH EQUIVALENTS, end of year	<u>\$ 17,312,100</u>	<u>\$ 7,232,100</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	<u>\$ 4,946,200</u>	<u>\$ 4,560,700</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Note 1 – Organization and Summary of Significant Accounting Policies

Description of organization – Children's Hospital & Research Center at Oakland, (the Hospital) provides a full range of pediatric acute and critical care medical services to both inpatients and outpatients. It is a nonprofit corporation organized and operated in accordance with Internal Revenue Code Section 501(c)(3) and the California Franchise Tax Board and is generally not subject to federal or state taxes on income.

The consolidated financial statements also include the accounts of Children's Hospital Oakland Research Institute (CHORI) and the Children's Hospital Oakland Family House, a tax-exempt subordinate corporation, operating as departments of the Hospital. In addition, the following controlled corporations are also included in these consolidated financial statements (collectively, CHRCO):

- Children's Hospital and Research Center Foundation (CHRCF) is a California nonprofit public benefit corporation organized to solicit support exclusively for the Hospital.
- Children First Health Care Network (CFHN), a California corporation, is a physician hospital organization designed to provide negotiation, administration, and utilization management for the contracted services of the Hospital and those of Children First Medical Group (CFMG), an independent group of pediatric primary care and subspecialty physicians. The Hospital is the sole shareholder of CFHN.

In January 2004, CHRCF ("Foundation") merged with Children's Hospital Foundation to become one foundation. Upon merger, the bylaws of CHRCF were changed; and, as a result, the Hospital became the sole member of the foundation. With control of the foundation residing with the Hospital, CHRCF is required to be consolidated with the Hospital.

Children's Hospital Branches, Inc. (Note 7) is a separate nonprofit corporation currently operating for the benefit of the Hospital. Their financial statements are not included with the Hospital's consolidated financial statements, as the Hospital neither controls the organization nor manages its operations. Thus, under existing accounting guidance, consolidation of this organization is not permitted.

Principles of consolidation – All significant inter-company transactions and balances have been eliminated in consolidation.

Basis of presentation – The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Net assets, revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Hospital and changes therein are classified and reported as follow:

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Unrestricted net assets – Net assets that are not subject to donor-imposed stipulations. Investment earnings are recorded as unrestricted net assets for certain temporarily restricted funds in accordance with donor stipulations.

Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that may, or will be met, either by actions of the Hospital and/or the passage of time. When a restriction is met, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of changes in net assets as net assets released from restrictions.

Permanently restricted net assets – Net assets subject to donor imposed stipulations that they be maintained by the Hospital in perpetuity.

Cash and cash equivalents – Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less.

Investments – All investments in debt securities and short-term and long-term equity investments are measured at fair value in the balance sheet. Investment income or loss is included in unrestricted net assets unless their use is temporarily or permanently restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses.

Life income trusts – As of December 31, 2006 and 2005, CHRCF was remainderman for 222 and 216 life income trusts, respectively. The Foundation was trustee for 21 of the 222 life income trusts in 2006, and 21 of the 216 life income trusts in 2005. The assets of the life income trusts, for which CHRCF is the trustee, are included in marketable securities and temporarily restricted net assets in the consolidated balance sheets.

CHRCF, as trustee, is obligated to make annual payments to certain beneficiaries pursuant to irrevocable charitable remainder trust agreements. These trust agreements have various payment requirements, which include either fixed yearly payments or payments calculated at a required fixed percentage on the annual fair-market value of the trust's assets. A liability has been established for future payments under the outstanding unitrust and annuity contracts for which the foundation is named as trustee. The liability is calculated using the most recent Internal Revenue Service mortality tables, with an interest rate assumption of 6% per annum. Upon the death of a beneficiary, CHRCF's interest in the trust becomes the unrestricted property of the foundation.

The remaining trusts for which CHRCF is not the trustee are recorded at the net present value of the foundation's interest in the underlying trust assets, of which the foundation will be the beneficiary, and are included in other receivables and temporarily restricted net assets in the consolidated balance sheets.

Assets limited as to use, held by trustee – Assets limited as to use primarily include assets held by trustees under bond indenture agreements and deposits required as security for the Hospital's workers' compensation self-insurance arrangement. Amounts required to meet current liabilities of the Hospital have been reclassified as current assets.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Supplies – Supplies are stated at cost, which is determined on the first-in, first-out method of accounting.

Property, plant, and equipment – Property, plant, and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method. Leasehold improvements are amortized over the shorter of the life of the lease or the useful life of the improvements.

Gifts of long-lived assets, such as land, buildings, or equipment, are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service. Costs for maintenance and repairs are charged to expense as incurred. Estimated useful lives are as follow:

Land improvements	5 - 20 years
Buildings	10 - 35 years
Equipment	2 - 10 years

Deferred debt issuance costs – Costs associated with the issuance of debt are being amortized over the term of the related borrowing.

Deferred revenue – Amounts classified as deferred revenue represent amounts received in advance of the Hospital's incurrence of certain qualifying expenditures under contracted cost reimbursement arrangements with various third parties.

Professional liability insurance – The Hospital insures for professional liability claims under a claims-made policy. Under the policy, insurance premiums cover only those claims actually reported during the policy term. Should the claims-made policy not be renewed, or replaced with equivalent insurance, claims related to occurrences during their terms but reported subsequent to their termination may be uninsured.

Accounting principles generally accepted in the United States of America require that a health care facility disclose estimated costs of malpractice claims in the period of the incident of malpractice, if it is reasonably possible that liabilities may be incurred and losses reasonably estimated. The Hospital has used an actuarial estimate of uninsured loss to recognize an estimated liability to cover the Hospital's potential exposure to incurred but unreported claims. The claim reserve is based on the best data available to the Hospital; however, the estimate is subject to a significant degree of inherent variability. Such an estimate is continually monitored and reviewed; and, as the reserve is adjusted, the difference is reflected in current operations. While the ultimate amount of professional liability is dependent on future developments, management is of the opinion that the associated liabilities recognized in the accompanying consolidated financial statements is adequate to cover such claims. Management is aware of no potential professional liability claims whose settlement, if any, would have a material adverse effect on the Hospital's consolidated financial position.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Workers' compensation – The Hospital has a large dollar deductible for its workers' compensation policy. Although, claims in excess of the deductible are insured, the hospital is effectively self-insured because the deductible amount is so high. The accrual for these costs includes the unpaid portion of claims that have been reported and estimates of amounts incurred for claims that have been incurred but not reported. The Hospital has used an actuarial estimate of uninsured losses to recognize the estimated liability up to the deductible amount. The claim reserve is based on the best data available to the Hospital; however, the estimate is subject to a significant degree of inherent variability. Such an estimate is continually monitored and reviewed; and, as the reserve is adjusted, the difference is reflected in current operations. While the ultimate amount of workers' compensation liability is dependent on future developments, management are of the opinion that the associated liabilities recognized in the accompanying consolidated financial statements is adequate to cover such claims. Management is aware of no potential workers' compensation liability whose settlement, if any, would have a material adverse effect on the Hospital's consolidated financial position.

Health benefits – The Hospital offers its benefited employees a choice of health insurance plans, including a preferred provider organization ("PPO") plan. The Hospital is self-insured for health claims under the PPO plan. The accrual for these costs includes the unpaid portion of claims that have been reported and estimates of amounts incurred for claims that have been incurred but not reported. Management recognized an estimated liability based upon the Hospital's historical claims experience and purchased stop loss coverage limits. The claim reserve is based on the best data available to the Hospital; however, the estimate is subject to a significant degree of inherent variability. The estimate is continually monitored and reviewed; and, as the reserve is adjusted, the difference is reflected in current operations.

While the ultimate amount of employee health liability claims is dependent upon future developments, management is of the opinion that the associated liabilities recognized in the accompanying consolidated financial statements are adequate to cover such claims. Management is aware of no potential employee health liability whose settlement, if any, would have a material adverse effect on the Hospital's consolidated financial position.

Excess of revenues, gains, and other support over expenses – The statement of operations includes excess of revenues, gains, and other support over expenses. Changes in unrestricted net assets which are excluded from excess of revenues, gains, and other support over expenses, consistent with industry practice, include unrealized gains and losses on investments other than trading securities, permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets).

Grants and contributions – The Hospital receives grants from federal agencies and other third parties, as well as contributions from private organizations. Government grants are reimbursed based on actual expenses incurred or units of services provided. Revenue from these grants is recognized either when expenses are incurred or when services are provided. Revenue recognition depends on the grant award agreements. Contribution revenue is reported when cash is received, unconditional promises are made, or ownership of other assets is transferred to the organization.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Contributions received may be designated by the donor for restricted purposes or may be without restriction as to their use. Contributions restricted by donors as to use or time period are recorded as temporarily restricted net assets until used in the manner designated or upon expiration of the time period. When there are no legally imposed restrictions on contributions or on income earned from restricted contributions, they are recorded as other unrestricted revenue when received.

Net patient service revenue – The Hospital has agreements with third-party payors that 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 an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Premium revenue – The Hospital has agreements with various Health Maintenance Organizations (HMOs) to provide medical services to subscribing participants. Under these arrangements, the Hospital receives monthly capitation payments based on the number of each HMO's participants, and recognizes as revenue during the period regardless of services actually performed by the Hospital. In addition, the HMOs make fee-for-service payments to the Hospital for certain covered services based upon discounted fee schedules. Premium revenues are included in net patient service revenues.

Charity care – The Hospital provides care to patients who meet certain criteria under its charity-care policy without charge or at amounts less than established rates for that service. The Hospital accepts all patients, regardless of their ability to pay. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care provided in 2006 and 2005, measured at established charge rates totaled approximately \$4,366,700 and \$2,124,500, respectively. These charges are not included in net patient service revenues. Costs and expenses incurred in providing these services in 2006 and 2005 were approximately \$2,163,200 and \$1,068,200, respectively, and are included in the Hospital's operating expenses.

Concentration of risk – Financial instruments potentially subjecting the Hospital to concentrations of credit risk consist primarily of bank demand deposits in excess of FDIC limits. Management believes, however, that the risk of loss is minimal due to the high financial quality of the banks.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

The Hospital grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. The Hospital manages its collection risk by regularly reviewing its accounts and contracts and by providing appropriate allowances. The mix of receivables from patients and third-party payors is as follows:

	Years Ended December 31,	
	2006	2005
Managed care payors	47%	46%
Medi-Cal	17%	18%
California Children's Services	14%	12%
Medi-Cal managed care	12%	18%
Self-pay and other	10%	6%
	100%	100%

Income taxes – CHRCO is organized as a not-for-profit entity under the general nonprofit corporation laws of the State of California. Exemptions from federal income taxation under Internal Revenue Code Section 501(c)(3) and California franchise taxation have been obtained. Certain activities and subsidiaries may be subject to income taxes; however, such activities are not significant to the consolidated financial statements. Accordingly, no provision for income taxes has been provided in the accompanying consolidated financial statements.

Reclassification – Certain reclassifications have been made to the prior year to conform to current year presentation.

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 amounts reported in the financial statements and accompanying notes.

For CHRCO, these estimates and assumptions primarily relate to the collectibility of accounts receivable, valuation of fixed assets, including depreciable lives assigned, valuation of derivative instruments, determination of the other-than-temporary impairments of marketable securities, and the assumptions utilized in valuation of self-insured reserves and retirement plan obligations. Actual results could differ from those estimates and such differences could be material.

Note 2 – Net Patient Revenue

The Hospital has arrangements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005 AND 2004

Medi-Cal – The Hospital renders services to patients under a contractual arrangement with the Medi-Cal program. Under the contractual arrangement, inpatient services are reimbursed on a per-diem basis, while outpatient services are reimbursed based on a schedule of maximum allowances. Gross Medi-Cal charges under this contractual arrangement were \$161,460,100 and \$144,327,200 for the years ended December 31, 2006 and 2005, respectively.

In 1997, Medi-Cal managed care was implemented in Alameda County with the introduction of two programs, the local initiative and the mainstream plan. The local initiative is administered by the Alameda Alliance for Health (Alliance), while the mainstream plan is administered by Blue Cross. Both plans operate as state-licensed health maintenance organizations that provide health care services on a prepaid basis to enrolled Medi-Cal members residing in the county. Eligible members select the plan in which they wish to participate.

The Hospital established contractual arrangements with both of the plans. The effect of these arrangements was a shift from the previous fee-for-service reimbursement, under the original contractual arrangement with Medi-Cal, to an arrangement with the Alliance that provides reimbursement based on capitated lives, with separate case rate provisions for specific diagnoses. The Blue Cross plan provides reimbursement on a per-diem basis. Gross revenues, included in net patient service revenue, under each of these arrangements were as follow:

	2006	2005
Alliance - Capitation	\$ 19,658,700	\$ 15,132,000
Alliance - Case Rate	17,248,000	16,853,400
Blue Cross Medi-Cal	23,385,900	20,103,400

In addition to the reimbursement program discussed above, the Hospital received additional reimbursement from the State of California under the following programs:

During 2006 and 2005, the Hospital recorded \$7,998,900 and \$8,733,300 in revenues related to funding from the State of California under Senate Bill 855 (SB855). This additional funding is based on the Hospital's qualification as a disproportionate share hospital. This legislative funding is subject to retroactive reductions and potential future elimination.

During 2006 and 2005, the Hospital recorded \$21,197,500 and \$24,442,500, respectively, in revenues related to funding from the State of California under Senate Bill (SB) 1255. This legislation provides supplemental payments to qualifying disproportionate share hospitals that provide emergency services to Medi-Cal beneficiaries. California Medical Assistance Commission negotiates the SB 1255 award amounts based on requests from eligible hospitals and the total pool of funding that is available for distribution at the time of the negotiations.

For the years ended December 31, 2006 and 2005, the Hospital recorded \$7,642,400 and \$7,639,300, respectively, in revenues related to funding for Graduate Medical Education.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Laws and regulations governing the Medi-Cal and Medicare programs are 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. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any significant pending or threatened investigations involving allegations of potential wrongdoing. While no such significant regulatory inquiries, other than discussed above, have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medi-Cal programs.

Other – The Hospital also has entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Note 3 – Investments

Assets Limited as to Use

The composition of assets limited as to use at December 31, 2006 and 2005, is set forth in the following table. Investments are stated at fair value:

	2006	2005
Assets held in trust:		
Held by trustee under indenture agreement:		
Cash	\$ 23,504,100	\$ 32,975,900
U.S. Treasury obligations	13,346,400	10,343,000
Guaranteed investment contract	1,949,000	1,949,000
Interest receivable	253,900	238,900
	39,053,400	45,506,800
Held by trustee under workers' compensation collateral agreement:		
Cash	603,300	3,240,500
U.S. Treasury obligations	6,246,500	6,187,500
U.S. government asset-backed securities	7,100,000	3,777,800
Interest receivable	138,900	64,600
	14,088,700	13,270,400
	\$ 53,142,100	\$ 58,777,200

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Other Investments

Other investments, stated at fair value, at December 31, 2006 and 2005, include:

	<u>2006</u>	<u>2005</u>
Marketable securities	\$ 50,328,700	\$ 87,056,500
Corporate bonds	13,576,600	15,464,500
U.S. Treasury obligations	-	1,703,200
U.S. government asset-backed securities	6,396,300	6,828,000
U.S. government obligations	5,220,500	8,461,200
Other investments	116,310,200	67,395,400
Interest receivable	<u>221,400</u>	<u>348,800</u>
	192,053,700	187,257,600
Less: current portion	<u>10,150,400</u>	<u>12,367,300</u>
	<u>\$ 181,903,300</u>	<u>\$ 174,890,300</u>

Investment income, realized and unrealized gains (losses) consists of the following for the year ended December 31, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Interest and dividends	\$ 18,454,600	\$ 10,710,800
Realized gains on sales of securities	<u>2,691,300</u>	<u>598,100</u>
	<u>\$ 21,145,900</u>	<u>\$ 11,308,900</u>
Net unrealized losses on investments	<u>\$ (2,332,900)</u>	<u>\$ (2,505,500)</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Note 4 – Property, Plant, and Equipment

Property, plant, and equipment consist of the following at December 31, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Land improvements	\$ 2,019,800	\$ 1,796,800
Buildings	201,143,000	198,632,900
Equipment	<u>64,319,400</u>	<u>79,751,400</u>
	267,482,200	280,181,100
Allowances for depreciation	<u>(134,299,000)</u>	<u>(146,531,500)</u>
	133,183,200	133,649,600
Construction-in-progress	9,174,600	6,291,400
Land	<u>10,560,200</u>	<u>9,571,500</u>
	<u>\$ 152,918,000</u>	<u>\$ 149,512,500</u>

The cost to complete the construction-in-progress at December 31, 2006 is estimated to be \$10,328,600. Depreciation expense totaled \$13,325,900 and \$12,594,100 for the period ended December 31, 2006 and 2005, respectively. Additionally, depreciation expense of \$1,603,700 and \$1,611,200 for the period ended December 31, 2006 and 2005, respectively, related to research specific property, plant and equipment.

Note 5 – Long Term Obligations

Long-term obligations consist of the following at December 31, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
ABAG Finance Authority for Nonprofit Corporations Hospital Revenue Certificates of Participation, \$30,000,000 weekly adjustable \$30,000,000 fixed rate bonds Series 1999 less unamortized bond discount of \$314,737 as of December 31, 2006; principal payable in annual installments ranging from \$1,635,000 in 2010 to \$4,930,000 in 2029; interest at stated coupon rates ranging from 5.875% to 6.00%, payable semiannually.	\$ 59,685,300	\$ 59,671,500

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
ABAG Finance Authority for Nonprofit Corporations Hospital Revenue Certificates of Participation, \$30,000,000 fixed rate bonds Series 2005; principal payable in annual installments ranging from \$500,000 in 2010 to \$2,300,000 in 2034; interest at stated coupon rate of 6.15%, payable semiannually.	30,000,000	30,000,000
City of Oakland, California, Weekly Adjustable/Fixed Rate Health Facility Revenue Bonds, 1988 Series A, plus unamortized bond premium of \$3,707 at December 31, 2006; principal payable in annual installments ranging from \$1,505,000 in 2005 to \$2,355,000 in 2008; interest at stated coupon rates ranging from 4.625% to 5.300%, payable semiannually.	4,593,700	6,101,700
City of Oakland, California, Insured Refunding Revenue Bonds, 1994 Series A, less unamortized bond discount of \$14,667 at December 31, 2006; principal payable in annual installments ranging from \$1,175,000 in 2006 to \$1,940,000 in 2009; interest at stated coupon rates ranging from 3.6% to 5.2%, payable semiannually.	<u>4,290,300</u>	<u>5,454,300</u>
	98,569,300	101,227,500
Unamortized proceeds from restructuring the 1999 swap	3,141,800	3,276,500
Fair value of 1988 interest rate swap	<u>39,900</u>	<u>99,500</u>
	101,751,000	104,603,500
Less current maturities	<u>2,750,000</u>	<u>2,680,000</u>
	<u>\$ 99,001,000</u>	<u>\$ 101,923,500</u>

The Series 1999 Certificates of Participation have been issued by the ABAG Finance Authority for Nonprofit Corporations pursuant to an Installment Sale Agreement, whereby the Hospital agrees to make installment payments that, in the aggregate, will be sufficient to pay all interest and principal on the Certificates of Participation as they become due.

Under the terms of the loan and reimbursement agreements, the Hospital is subject to certain limitations on its ability to incur additional debt, to pledge its assets as collateral, and to acquire or dispose of certain assets. CHRCO must also maintain certain financial ratios, including a ratio of unrestricted net assets to long-term debt of 1.50 to 1.00. As a result, \$148,501,500 and \$152,885,300 of unrestricted net assets is limited as to use under the terms of these covenants at December 31, 2006 and 2005.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

In October 1999, the Hospital entered into a swap agreement covering \$30,000,000 of its Series 1999 Certificates of Participation. Under the swap agreement, the Hospital paid the swap provider a floating swap payment, and receives a fixed swap payment, with semiannual settlements. In October 2001, the Hospital terminated the swap. In connection with the termination, the Hospital received an up-front payment of \$3,815,100. As the 1999 interest rate swap qualified as a fair value hedge under the provisions of FAS 133, the fair value of the swap (*i.e.*, the proceeds) at the time of the termination continues to be classified as an increase to the 1999 bonds and is amortized over the life of the debt.

In conjunction with the 1988 bonds, the Hospital has an outstanding interest rate swap agreement (Swap Agreement) with a commercial bank, having a total notional principal amount of \$4,590,000 and \$6,715,000 on December 31, 2006 and 2005 respectively. Under the Swap Agreement, the Hospital pays the swap provider a floating swap payment, and receives a fixed swap payment, with semiannual settlements. These settlements resulted in gains to the Hospital of \$57,800 for the year ended December 31, 2006 and \$154,600 for the year ended December 31, 2005. At December 31, 2006 and 2005, the fair value of the 1988 interest rate swap was \$39,900 and \$99,500, respectively, which has been recorded as an asset and a liability in debt in the accompanying consolidated balance sheet, in accordance with FAS 133. The Swap Agreement matures at the same time as the 1988 bonds. The Hospital is exposed to credit loss in the event of nonperformance by the other party to the Swap Agreement. However, the Hospital does not anticipate nonperformance by the counterparty.

The Hospital is party to a basis swap that serves to convert the underlying variable interest rate index of certain of the Hospital's debt. The swap does not qualify for hedge accounting under the provisions of FAS 133; therefore, changes in the fair value of the swap are recorded in earnings. The Hospital recognized a gain of \$795,900 for the year ended December 31, 2006 and a loss of \$7,900 for the year ended December 31, 2005 related to this swap. At December 31, 2006, the Hospital recognized the fair value of the basis swap of \$12,700 in other assets in the accompanying consolidated financial statements. At December 31, 2005, the Hospital recognized the fair value of the basis swap of \$783,200, in other long-term liabilities in the accompanying consolidated financial statements.

In 2004, the Hospital executed a tender offer for all of the outstanding series 1988A bonds and series 1994A bonds, which resulted in the Hospital purchasing a total of \$14,855,000 of the series 1988A bonds and the series 1994A bonds from bondholders. The series 1988A bonds and the series 1994A bonds that were tendered to the Hospital were subsequently purchased from the Hospital by Merrill Lynch. The Hospital used cash to redeem a total of \$2,755,000 of the outstanding series 1988A bonds and series 1994A bonds that were not tendered in the tender offer. The series 1988A bonds were callable at 100.5% starting March 6, 2004 and the series 1994A bonds were callable at 102% starting May 1, 2004. The Hospital is party to interest rate swap agreements with Merrill Lynch in connection with the series 1998A and the series 1994A bonds that were tendered to the Hospital and purchased by Merrill Lynch. Additionally, in 2005, the Hospital entered into an interest rate swap agreement with Merrill Lynch covering the \$30,000,000 Series 2005 Certificates of Participation. Under the swap agreements, the Hospital receives a fixed rate from Merrill Lynch and pays Merrill Lynch a floating rate. The swap agreements do not qualify for hedge

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

accounting under the provisions of FAS 133; therefore, changes in the fair value of the swap agreements are recorded in the Hospital's earnings. The Hospital recorded a loss of \$2,300 for the period ended December 31, 2006 and a gain of \$14,900 for the period ended December 31, 2005 related to these swaps. The swap agreements have various maturity dates from 2006 to 2009. Upon termination of the swap agreements, the Hospital is obligated to pay Merrill Lynch the difference, if any, between the price that Merrill Lynch paid for the tendered bonds and the market value of the tendered bonds at the time of termination of the swap agreements. The Hospital's payment obligations on the swap agreements are secured under the Hospital's Master Trust Indenture as joint and several obligations of each Member of the Obligated Group. At December 31, 2006 and December 31, 2005, the Hospital has recognized the fair value of the swap agreements of \$97,500 and \$95,200 in other long-term liabilities in the accompanying consolidated financial statements.

Aggregate principal maturities on long-term debt based on scheduled maturities, excluding debt discount, are as follow:

<u>Year Ending December 31,</u>	
2007	\$ 2,750,000
2008	4,205,000
2009	1,940,000
2010	2,135,000
2011	2,335,000
Thereafter	<u>85,530,000</u>
	<u><u>\$ 98,895,000</u></u>

Note 6 – Employee Retirement Plan

CHRCO has a noncontributory defined benefit pension plan (the Plan) that covers substantially all employees who are not covered by separate union-sponsored plans.

Benefits are based on years of service and the employee's compensation during the last five years of employment. CHRCO's annual funding policy is to contribute no less than the minimum actuarially determined. Based on available cash and the funding status of the Plan, management may decide to make additional discretionary contributions to the Plan. Contributions are intended to provide not only for benefits attributed to service to date, but also for those expected to be earned in the future.

The broad-based investment goals of the Plan are to: 1) at a minimum, preserve the inflation-adjusted value of the Pension assets after administrative cost and benefit payments; 2) prudently invest assets in a high-quality, diversified manner; 3) achieve the optimal return possible within the specified risk parameters; 4) achieve the actuarial earnings assumptions; and 5) adhere to the established guidelines.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

The Plan's assets are invested in common stocks, corporate and government bonds, convertible securities, and money market funds.

CHRCO uses a December 31 measurement date for its Plan. Changes in the benefit obligation and Plan assets for CHRCO's noncontributory defined benefit retirement plan are as follow:

	December 31,	
	2006	2005
Actuarial present value of benefit obligations:		
Projected benefit obligation at beginning of year	\$ 145,278,400	\$ 126,992,200
Service cost	10,786,800	10,508,200
Interest cost	8,620,500	7,710,600
Actuarial losses	1,436,000	2,023,800
Benefits paid	(3,016,100)	(2,557,200)
Plan change	868,100	600,800
Projected benefit obligation at end of year	163,973,700	145,278,400
Fair value of Plan assets:		
Fair value of Plan assets at beginning of year	103,146,100	90,191,200
Actual return on Plan assets	13,270,800	5,512,100
Employer contribution	12,000,000	10,000,000
Benefits paid	(3,016,100)	(2,557,200)
Fair value of Plan assets at end of year	125,400,800	103,146,100
Funding status of the Plan	(38,572,900)	(42,132,300)
Unrecognized net actuarial loss	24,679,900	28,604,700
Unrecognized prior service cost	4,334,500	4,068,100
Accrued retirement benefit cost	\$ (9,558,500)	\$ (9,459,500)

As of December 31, 2006 and 2005 the total accumulated benefit obligation for the Plan is \$128,646,200 and \$112,550,400 respectively. The components of CHRCO's net periodic benefit cost associated with its noncontributory defined benefit retirement plan are as follow:

	Years Ended December 31,	
	2006	2005
Service cost	\$ 10,786,800	\$ 10,508,200
Interest cost	8,620,500	7,710,600
Expected return on plan assets	(8,996,000)	(6,990,100)
Net loss recognition	1,086,000	585,200
Amortization of prior service cost	601,700	1,271,800
Net periodic pension cost	\$ 12,099,000	\$ 13,085,700

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Weighted-average assumptions used in the accounting for net periodic pension costs were:

	Years Ended December 31,	
	2006	2005
Net periodic retirement costs:		
Discount rate	6.00%	6.00%
Expected long-term rate of return on plan assets	8.25%	7.50%
Compensation increase rate	5.00%	5.00%
	December 31,	
	2006	2005
Benefit obligations and funded status:		
Discount rate	6.00%	6.00%
Compensation increase rate	5.00%	5.00%

The long-term rate of return reflects the average rate of earnings expected on the funds invested to provide for benefits in the future. In estimating this rate, appropriate consideration was given to the returns currently being earned by plan assets and the rates of return expected to be available for reinvestment. The present and expected asset mix was taken into account. The long-term rate is expected to be less volatile than the actual rate of return on assets, since the expected rate not only considers current returns, but also reinvestment rates in the future. This rate will generally be the same each year, unless the asset mix and/or asset returns are expected to significantly change in the future.

Expected benefit payments for the Plan are as follows:

Year Ending December 31,	
2007	\$ 3,662,700
2008	4,186,100
2009	4,809,900
2010	5,479,700
2011	6,229,400
Thereafter	48,629,600
	<u>\$ 72,997,400</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Note 7 – Related Organizations

The Hospital receives support from Children's Hospital Branches, Inc. (the Branches). The accounts of the Branches are not consolidated with those of the Hospital, as described in Note 1. Summarized financial information of the Branches is not presented as it is not significant.

Note 8 – Operating Leases

The Hospital has entered into operating lease arrangements for the lease of office space, facilities, vehicles, and equipment. The total amount of rental expense incurred during 2006 and 2005 under these operating leases was \$2,087,900 and \$1,312,700. The Hospital's future minimum lease payments under noncancelable operating leases with initial terms of one year or more consist of the following:

<u>Year Ending December 31,</u>	
2007	\$ 1,995,100
2008	1,665,400
2009	655,200
2010	<u>32,000</u>
	<u>\$ 4,347,700</u>

Note 9 – Commitments and Contingencies

CHRCO receives grant funds for various programs. These funds may be subject to program compliance audits by the grantor and possible disallowance of expenditures. The Hospital does not expect the amount of disallowance of expenditures, if any, to have a material adverse impact on the Hospital's financial position.

The Hospital is aware of certain asserted and unasserted legal claims. While the outcome cannot be determined at this time, it is management's opinion that the liability, if any, from these actions will not have a material adverse effect on the Hospital's financial position.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not limited to, accreditation, licensure, government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Government activity has continued with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs, together with the imposition of

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

significant fines and penalties, as well as significant repayment for previously billed patient services. While the Hospital is subject to similar regulatory reviews, there are no reviews currently underway and management believes that the outcome of any potential regulatory review will not have a material adverse effect on the Hospital's financial position.

Management believes that the Hospital is in compliance with government law and regulations related to fraud and abuse and other applicable areas. While no material regulatory inquiries have been made other than discussed in Note 2, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

The Hospital is directly liable under an irrevocable letter of credit with a bank, totaling \$11.5 million and \$11.1 million at December 31, 2006 and 2005, which is required as security for the workers' compensation self-insurance arrangement as described in Note 1. No amounts were drawn on the letter of credit as of December 31, 2006 and 2005.

As of December 31, 2006 and 2005, approximately 46% and 49% of the Hospital's employees are represented by collective bargaining units.

The Hospital is assessing its earthquake retrofit requirements for health care facilities under a State of California law that requires compliance with certain seismic standards by 2008. Based on studies performed, the total cost of bringing facilities into compliance is estimated to be between \$29 million and \$32 million (unaudited) before inflation, not including costs due to disruption and loss of business. Planning measures are under way that may result in certain of the seismically noncompliant facilities being withdrawn from use or replaced. The Hospital has requested and received an extension of time, to 2013, to comply with the requirements.

Note 10 – Functional Classification of Operating Expenses

CHRCO's operating expenses reflected by functional classification are as follows for the years ended December 31:

	<u>2006</u>	<u>2005</u>
Patient care - direct	\$ 195,900,600	\$ 170,967,800
Patient care - support	74,621,700	66,642,200
Research and special purpose grant expenses	48,886,400	47,050,200
Fundraising	5,138,400	5,599,900
Depreciation	13,325,000	12,594,100
Bad debts	13,937,700	9,149,700
Interest, net	3,794,100	3,156,100
Insurance	<u>3,072,900</u>	<u>3,939,300</u>
Total operating expenses	<u>\$ 358,676,800</u>	<u>\$ 319,099,300</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Note 11 – Fair Value of Financial Instruments

The following methods and assumptions were used by CHRCO in estimating the fair value of its financial instruments:

Cash and cash equivalents: The carrying amount reported in the balance sheet for cash and cash equivalents approximates its fair value.

Investments: Fair values, which are the amounts reported in the balance sheet, are based on quoted market prices, if available, or estimated using quoted market prices for similar securities.

Assets limited as to use: These assets consist primarily of long-term investments and interest receivable. The carrying amount reported in the balance sheet is fair value.

Accounts payable and accrued expenses: The carrying amount reported in the balance sheet for accounts payable and accrued expenses approximates its fair value.

Accrued payroll and payroll-related liabilities: The carrying amount reported in the balance sheet for accrued payroll and payroll-related liabilities approximates its fair value.

Estimated third-party payor settlements: The carrying amount reported in the balance sheet for estimated third-party payor settlements approximates its fair value.

Accrued professional liability: The carrying amount reported in the balance sheet for accrued professional liability approximates its fair value.

Accrued workers' compensation liability: The carrying amount reported in the balance sheet for accrued workers' compensation liability approximates its fair value.

Long-term obligations: Fair values of CHRCO's revenue notes are based on current traded value. The fair value of the CHRCO's remaining long-term debt is estimated using discounted cash flow analyses, based on the CHRCO's current incremental borrowing rates for similar types of borrowing arrangements.

Other long-term liabilities: The carrying amount reported in the balance sheet for other long-term liabilities approximates its fair value.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

The carrying amounts and fair values of the CHRCO's financial instruments at December 31, 2006 and 2005, are as follow:

	2006		2005	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	\$17,312,100	\$17,312,100	\$ 7,232,100	\$ 7,232,100
Investments, current portion	10,150,400	10,150,400	12,367,300	12,367,300
Assets limited as to use	53,142,100	53,142,100	58,777,200	58,777,200
Investments, less current portion	181,903,300	181,903,300	174,890,300	174,890,300
Accounts payable and accrued expenses	14,276,400	14,276,400	12,336,100	12,336,100
Accrued payroll and payroll related liabilities	23,494,100	23,494,100	23,523,200	23,523,200
Estimated third-party payor settlements receivable (payable)	(2,076,400)	(2,076,400)	253,700	253,700
Accrued professional liability	2,791,800	2,791,800	2,616,700	2,616,700
Accrued workers' compensation liability	15,327,600	15,327,600	14,471,000	14,471,000
Long-term obligations	99,001,000	99,001,000	101,923,500	101,923,500
Other long-term liabilities	15,445,700	15,445,700	17,116,200	17,116,200

Note 12 – Subsequent Events

BayChildren's Physicians-Subsequent to year-end, BayChildren's Physicians (BCP), a new medical practice foundation of which the Hospital is the sole member, was formed. BCP is a nonprofit corporation organized and operated in accordance with Internal Revenue Code Section 501(c)(3) and the California Franchise Tax Board and is generally not subject to federal or state taxes on income.

BCP has entered into a professional services agreement, effective January 1, 2007, with Pediatric Multispecialty Medical Group, Inc., dba BayChildren's Medical Group (BCMG), a multispecialty medical group. Under this agreement, BCMG, through its employed or subcontracted physicians, agrees to provide care to BCP's patients. After the first year, the compensation paid to BCMG includes certain incentives to increase productivity.

In turn, BCP provides the infrastructure to support BCMG's medical practice, including all facilities, equipment, supplies, administrative and management services, non-physician personnel, medical records systems, accounting and bookkeeping services, insurance and consultants. BCP also is the contracting entity for all third-party payor contracts.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006 AND 2005

Financing Plan-On January 30, 2007, CHRCO approved a financing plan that includes a refinancing of the Series 1999 Certificates of Participation using tax-exempt refunding bonds for the purpose of debt service savings, a defeasance and redemption of the Series 1988A Bonds and the Series 1994A Bonds using CHRCO's equity, a termination of the interest rate swap agreements with Merrill Lynch in connection with the Series 1988A and the Series 1994A Bonds that were tendered to the Hospital and purchased by Merrill Lynch in 2004, and the establishment of a new Master Indenture of Trust. The Series 1988A and the Series 1994A Bonds are currently callable at a redemption price of 100% and the Series 1999 Certificates of Participation will be callable beginning December 1, 2009 at a redemption price of 101%. CHRCO expects to execute the financing plan later in 2007, although the execution is subject to market conditions. The scheduled payment of principal and the coupon rates in connection with the refunding bonds will not be known until issuance.

SUPPLEMENTAL INFORMATION

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING BALANCE SHEETS
DECEMBER 31, 2006**

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
ASSETS					
CURRENT ASSETS					
Cash and cash equivalents	\$ 3,461,600	\$ 13,850,500	\$ 17,312,100	\$ -	\$ 17,312,100
Investments	10,150,400	-	10,150,400	-	10,150,400
Assets limited as to use, held by trustee	39,053,400	-	39,053,400	-	39,053,400
Patient accounts receivable, net	42,065,200	-	42,065,200	-	42,065,200
Due from Children's Hospital and Research Center Foundation	2,301,700	-	2,301,700	(2,301,700)	-
Grants and contract receivables	9,438,900	-	9,438,900	-	9,438,900
Other receivables	3,968,700	26,275,400	30,244,100	-	30,244,100
Supplies	2,882,000	-	2,882,000	-	2,882,000
Prepaid expenses	2,930,200	-	2,930,200	-	2,930,200
Total current assets	116,252,100	40,125,900	156,378,000	(2,301,700)	154,076,300
ASSETS LIMITED AS TO USE, HELD BY TRUSTEE, net of current portion					
	14,088,700	-	14,088,700	-	14,088,700
PROPERTY, PLANT, AND EQUIPMENT, net					
	149,604,700	3,313,300	152,918,000	-	152,918,000
INVESTMENTS, net of current portion					
	15,264,400	166,638,900	181,903,300	-	181,903,300
OTHER ASSETS					
	2,508,900	-	2,508,900	-	2,508,900
Total assets	<u>\$ 297,718,800</u>	<u>\$ 210,078,100</u>	<u>\$ 507,796,900</u>	<u>\$ (2,301,700)</u>	<u>\$ 505,495,200</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING BALANCE SHEETS
DECEMBER 31, 2006

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
LIABILITIES AND NET ASSETS					
CURRENT LIABILITIES					
Accounts payable and accrued expenses	\$ 13,815,000	\$ 2,763,100	\$ 16,578,100	\$ (2,301,700)	\$ 14,276,400
Accrued payroll and payroll related liabilities	23,494,100	-	23,494,100	-	23,494,100
Deferred revenue	5,184,300	-	5,184,300	-	5,184,300
Estimated third-party payor settlements	2,076,400	-	2,076,400	-	2,076,400
Current portion of long-term obligations	<u>2,750,000</u>	<u>-</u>	<u>2,750,000</u>	<u>-</u>	<u>2,750,000</u>
Total current liabilities	47,319,800	2,763,100	50,082,900	(2,301,700)	47,781,200
ACCRUED PROFESSIONAL LIABILITY	2,791,800	-	2,791,800	-	2,791,800
ACCRUED WORKERS' COMPENSATION LIABILITY	15,327,600	-	15,327,600	-	15,327,600
LONG-TERM OBLIGATIONS, net of current portion	99,001,000	-	99,001,000	-	99,001,000
OTHER LONG-TERM LIABILITIES	<u>10,022,300</u>	<u>5,423,400</u>	<u>15,445,700</u>	<u>-</u>	<u>15,445,700</u>
Total liabilities	<u>174,462,500</u>	<u>8,186,500</u>	<u>182,649,000</u>	<u>(2,301,700)</u>	<u>180,347,300</u>
COMMITMENTS AND CONTINGENCIES (Note 9)					
NET ASSETS					
Unrestricted	109,889,600	152,552,900	262,442,500	-	262,442,500
Temporarily restricted	13,366,700	32,066,500	45,433,200	-	45,433,200
Permanently restricted	<u>-</u>	<u>17,272,200</u>	<u>17,272,200</u>	<u>-</u>	<u>17,272,200</u>
Total net assets	<u>123,256,300</u>	<u>201,891,600</u>	<u>325,147,900</u>	<u>-</u>	<u>325,147,900</u>
Total liabilities and net assets	<u>\$ 297,718,800</u>	<u>\$ 210,078,100</u>	<u>\$ 507,796,900</u>	<u>\$ (2,301,700)</u>	<u>\$ 505,495,200</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING BALANCE SHEETS
DECEMBER 31, 2005

	<u>CHRCF</u>	<u>Foundation</u>	<u>Subtotal</u>	<u>Eliminations</u>	<u>Consolidated</u>
ASSETS					
CURRENT ASSETS					
Cash and cash equivalents	\$ 769,300	\$ 6,462,800	\$ 7,232,100	\$ -	\$ 7,232,100
Investments	12,367,300	-	12,367,300	-	12,367,300
Assets limited as to use, held by trustee	45,506,800	-	45,506,800	-	45,506,800
Patient accounts receivable, net	50,002,300	-	50,002,300	-	50,002,300
Estimated third-party payor settlements	253,700	-	253,700	-	253,700
Due from Children's Hospital and Research Center Foundation	3,504,600	-	3,504,600	(3,504,600)	-
Grants and contract receivables	7,950,200	-	7,950,200	-	7,950,200
Other receivables	3,236,100	26,973,700	30,209,800	-	30,209,800
Supplies	2,816,500	-	2,816,500	-	2,816,500
Prepaid expenses	2,711,600	68,600	2,780,200	-	2,780,200
Total current assets	129,118,400	33,505,100	162,623,500	(3,504,600)	159,118,900
ASSETS LIMITED AS TO USE, HELD BY TRUSTEE, net of current portion					
	13,270,400	-	13,270,400	-	13,270,400
PROPERTY, PLANT, AND EQUIPMENT, net	146,706,700	2,805,800	149,512,500	-	149,512,500
INVESTMENTS, net of current portion	20,438,200	154,452,100	174,890,300	-	174,890,300
OTHER ASSETS	3,194,900	-	3,194,900	-	3,194,900
Total assets	<u>\$ 312,728,600</u>	<u>\$ 190,763,000</u>	<u>\$ 503,491,600</u>	<u>\$ (3,504,600)</u>	<u>\$ 499,987,000</u>

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING BALANCE SHEETS
DECEMBER 31, 2005**

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
LIABILITIES AND NET ASSETS					
CURRENT LIABILITIES					
Accounts payable and accrued expenses	\$ 12,133,100	\$ 3,707,600	\$ 15,840,700	\$ (3,504,600)	\$ 12,336,100
Accrued payroll and payroll related liabilities	23,523,200	-	23,523,200	-	23,523,200
Deferred revenue	5,445,700	-	5,445,700	-	5,445,700
Current portion of long-term obligations	2,680,000	-	2,680,000	-	2,680,000
Total current liabilities	43,782,000	3,707,600	47,489,600	(3,504,600)	43,985,000
ACCRUED PROFESSIONAL LIABILITY	2,616,700	-	2,616,700	-	2,616,700
ACCRUED WORKERS' COMPENSATION LIABILITY	14,471,000	-	14,471,000	-	14,471,000
LONG-TERM OBLIGATIONS, net of current portion	101,923,500	-	101,923,500	-	101,923,500
OTHER LONG-TERM LIABILITIES	10,683,000	6,433,200	17,116,200	-	17,116,200
Total liabilities	173,476,200	10,140,800	183,617,000	(3,504,600)	180,112,400
COMMITMENTS AND CONTINGENCIES (Note 9)					
NET ASSETS					
Unrestricted	125,607,100	136,214,300	261,821,400	-	261,821,400
Temporarily restricted	13,645,300	28,742,300	42,387,600	-	42,387,600
Permanently restricted	-	15,665,600	15,665,600	-	15,665,600
Total net assets	139,252,400	180,622,200	319,874,600	-	319,874,600
Total liabilities and net assets	\$ 312,728,600	\$ 190,763,000	\$ 503,491,600	\$ (3,504,600)	\$ 499,987,000

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN UNRESTRICTED NET ASSETS
YEAR ENDED DECEMBER 31, 2006

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
UNRESTRICTED REVENUE, GAINS, AND OTHER SUPPORT					
Net patient service revenues	\$ 269,019,100	\$ -	\$ 269,019,100	\$ -	\$ 269,019,100
Other operating revenues	11,947,000	7,710,900	19,657,900	-	19,657,900
Net assets released from restrictions used for operations	49,928,300	7,865,200	57,793,500	(9,839,400)	47,954,100
Total unrestricted revenues, gains, and other support	<u>330,894,400</u>	<u>15,576,100</u>	<u>346,470,500</u>	<u>(9,839,400)</u>	<u>336,631,100</u>
EXPENSES					
Salaries and wages	149,510,000	2,128,000	151,638,000	-	151,638,000
Employee benefits	44,159,800	657,100	44,816,900	-	44,816,900
Supplies	32,187,400	57,900	32,245,300	-	32,245,300
Research and specific purpose grant expenses	48,886,400	-	48,886,400	-	48,886,400
Professional fees	19,903,000	-	19,903,000	-	19,903,000
Insurance and other direct expense	15,111,400	1,824,500	16,935,900	-	16,935,900
Depreciation and amortization	13,290,800	34,200	13,325,000	-	13,325,000
Purchased services	12,723,600	470,900	13,194,500	-	13,194,500
Provision for bad debts	13,937,700	-	13,937,700	-	13,937,700
Interest, net	3,794,100	-	3,794,100	-	3,794,100
Total expenses	<u>353,504,200</u>	<u>5,172,600</u>	<u>358,676,800</u>	<u>-</u>	<u>358,676,800</u>
Operating income (loss)	<u>(22,609,800)</u>	<u>10,403,500</u>	<u>(12,206,300)</u>	<u>(9,839,400)</u>	<u>(22,045,700)</u>
NONOPERATING GAINS AND (LOSSES)					
Contributions	-	-	-	-	-
Contributions to Children's Hospital & Research Center at Oakland	-	(9,839,400)	(9,839,400)	9,839,400	-
Investment income	2,006,500	7,958,100	9,964,600	10,742,000	20,706,600
Change in fair value of basis swap	793,600	-	793,600	-	793,600
Other income	553,800	-	553,800	-	553,800
Total nonoperating gains and (losses)	<u>3,353,900</u>	<u>(1,881,300)</u>	<u>1,472,600</u>	<u>20,581,400</u>	<u>22,054,000</u>
EXCESS (DEFICIENCY) OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES					
	(19,255,900)	8,522,200	(10,733,700)	10,742,000	8,300
Changes in net unrealized gains and (losses) on investments, net	(34,100)	7,816,500	7,782,400	(10,742,000)	(2,959,600)
State and county grants for capital additions	1,695,300	-	1,695,300	-	1,695,300
Net assets released from restrictions for capital additions	1,877,200	-	1,877,200	-	1,877,200
Increase in unrestricted net assets	<u>\$ (15,717,500)</u>	<u>\$ 16,338,700</u>	<u>\$ 621,200</u>	<u>\$ -</u>	<u>\$ 621,200</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN UNRESTRICTED NET ASSETS
YEAR ENDED DECEMBER 31, 2005

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
UNRESTRICTED REVENUE, GAINS, AND OTHER SUPPORT					
Net patient service revenues	\$ 253,700,000	\$ -	\$ 253,700,000	\$ -	\$ 253,700,000
Other operating revenues	10,303,600	5,075,600	15,379,200	-	15,379,200
Net assets released from restrictions used for operations	48,358,400	7,934,800	56,293,200	(11,909,500)	44,383,700
Total unrestricted revenues, gains, and other support	<u>312,362,000</u>	<u>13,010,400</u>	<u>325,372,400</u>	<u>(11,909,500)</u>	<u>313,462,900</u>
EXPENSES					
Salaries and wages	132,050,900	2,235,700	134,286,600	-	134,286,600
Employee benefits	42,133,000	709,600	42,842,600	-	42,842,600
Supplies	27,075,800	83,400	27,159,200	-	27,159,200
Research and specific purpose grant expenses	47,050,200	-	47,050,200	-	47,050,200
Professional fees	15,817,900	-	15,817,900	-	15,817,900
Insurance and other direct expense	12,649,700	2,071,200	14,720,900	-	14,720,900
Depreciation and amortization	12,557,800	36,300	12,594,100	-	12,594,100
Purchased services	11,822,000	500,000	12,322,000	-	12,322,000
Provision for bad debts	9,149,700	-	9,149,700	-	9,149,700
Interest, net	3,156,100	-	3,156,100	-	3,156,100
Total expenses	<u>313,463,100</u>	<u>5,636,200</u>	<u>319,099,300</u>	<u>-</u>	<u>319,099,300</u>
Operating income (loss)	<u>(1,101,100)</u>	<u>7,374,200</u>	<u>6,273,100</u>	<u>(11,909,500)</u>	<u>(5,636,400)</u>
NONOPERATING GAINS AND (LOSSES)					
Contributions	200,000	-	200,000	-	200,000
Contributions to Children's Hospital & Research Center at Oakland	-	(11,909,500)	(11,909,500)	11,909,500	-
Investment income	1,427,700	4,037,400	5,465,100	5,658,600	11,123,700
Change in fair value of basis swap	(7,900)	-	(7,900)	-	(7,900)
Other income	565,000	-	565,000	-	565,000
Total nonoperating gains and (losses)	<u>2,184,800</u>	<u>(7,872,100)</u>	<u>(5,687,300)</u>	<u>17,568,100</u>	<u>11,880,800</u>
EXCESS (DEFICIENCY) OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES					
	1,083,700	(497,900)	585,800	5,658,600	6,244,400
Changes in net unrealized gains and (losses) on investments, net	(117,500)	3,128,600	3,011,100	(5,658,600)	(2,647,500)
Net assets released from restrictions for capital additions	6,749,500	-	6,749,500	-	6,749,500
Increase in unrestricted net assets	<u>\$ 7,715,700</u>	<u>\$ 2,630,700</u>	<u>\$ 10,346,400</u>	<u>\$ -</u>	<u>\$ 10,346,400</u>

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING STATEMENT OF CHANGES OF NET ASSETS
YEAR ENDED DECEMBER 31, 2006**

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
EXCESS (DEFICIENCY) OF REVENUE , GAINS, AND OTHER SUPPORT OVER EXPENSES	\$ (19,255,900)	\$ 8,522,200	\$ (10,733,700)	\$ 10,742,000	\$ 8,300
Changes in net unrealized gains and (losses) on investments, net unrealized gains	(34,100)	7,816,500	7,782,400	(10,742,000)	(2,959,600)
State and county grants for capital additions	1,695,300	-	1,695,300	-	1,695,300
Net assets released from restrictions for capital additions	1,877,200	-	1,877,200	-	1,877,200
Increase in unrestricted net assets	<u>(15,717,500)</u>	<u>16,338,700</u>	<u>621,200</u>	<u>-</u>	<u>621,200</u>
CHANGE IN TEMPORARILY RESTRICTED NET ASSETS					
Contributions	2,018,400	10,544,100	12,562,500	-	12,562,500
Grants	49,452,800	-	49,452,800	(9,839,400)	39,613,400
Change in unrealized gains and (losses) on investments	-	205,900	205,900	-	205,900
Investment income	-	439,300	439,300	-	439,300
Net assets released from restrictions for operations	(49,928,300)	(7,865,200)	(57,793,500)	9,839,400	(47,954,100)
Net assets released from restrictions for capital additions	(1,877,200)	-	(1,877,200)	-	(1,877,200)
Other	55,700	-	55,700	-	55,700
(Decrease) increase in temporarily restricted net assets	<u>(278,600)</u>	<u>3,324,100</u>	<u>3,045,500</u>	<u>-</u>	<u>3,045,500</u>
CHANGE IN PERMANENTLY RESTRICTED NET ASSETS					
Contributions	-	1,185,800	1,185,800	-	1,185,800
Change in unrealized gains and (losses) on investments	-	420,800	420,800	-	420,800
Increase in permanently restricted net assets	<u>-</u>	<u>1,606,600</u>	<u>1,606,600</u>	<u>-</u>	<u>1,606,600</u>
Increase (Decrease) in net assets	<u>(15,996,100)</u>	<u>21,269,400</u>	<u>5,273,300</u>	<u>-</u>	<u>5,273,300</u>
Net assets, beginning of year	<u>139,252,400</u>	<u>180,622,200</u>	<u>319,874,600</u>	<u>-</u>	<u>319,874,600</u>
Net assets, end of year	<u>\$ 123,256,300</u>	<u>\$ 201,891,600</u>	<u>\$ 325,147,900</u>	<u>\$ -</u>	<u>\$ 325,147,900</u>

**CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATING STATEMENT OF CHANGES OF NET ASSETS
YEAR ENDED DECEMBER 31, 2005**

	CHRCO Before CHRCF	Children's Hospital & Research Center Foundation	Subtotal	Eliminations	Consolidated
EXCESS (DEFICIENCY) OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES	\$ 1,083,700	\$ (497,900)	\$ 585,800	\$ 5,658,600	\$ 6,244,400
Changes in net unrealized gains and (losses) on investments, net unrealized gains	(117,500)	3,128,600	3,011,100	(5,658,600)	(2,647,500)
Net assets released from restrictions for capital additions	<u>6,749,500</u>	<u>-</u>	<u>6,749,500</u>	<u>-</u>	<u>6,749,500</u>
Increase in unrestricted net assets	<u>7,715,700</u>	<u>2,630,700</u>	<u>10,346,400</u>	<u>-</u>	<u>10,346,400</u>
CHANGE IN TEMPORARILY RESTRICTED NET ASSETS					
Contributions	4,419,900	10,439,200	14,859,100	-	14,859,100
Grants	49,358,800	-	49,358,800	(11,909,500)	37,449,300
Change in unrealized gains and (losses) on investments	-	46,600	46,600	-	46,600
Investment income	-	185,200	185,200	-	185,200
Net assets released from restrictions for operations	(48,358,400)	(7,934,800)	(56,293,200)	11,909,500	(44,383,700)
Net assets released from restrictions for capital additions	(6,749,500)	-	(6,749,500)	-	(6,749,500)
Transfers	-	-	-	-	-
Other	<u>159,300</u>	<u>-</u>	<u>159,300</u>	<u>-</u>	<u>159,300</u>
(Decrease) increase in temporarily restricted net assets	<u>(1,169,900)</u>	<u>2,736,200</u>	<u>1,566,300</u>	<u>-</u>	<u>1,566,300</u>
CHANGE IN PERMANENTLY RESTRICTED NET ASSETS					
Contributions	-	3,598,200	3,598,200	-	3,598,200
Change in unrealized gains and (losses) on investments	<u>-</u>	<u>95,400</u>	<u>95,400</u>	<u>-</u>	<u>95,400</u>
Increase in permanently restricted net assets	<u>-</u>	<u>3,693,600</u>	<u>3,693,600</u>	<u>-</u>	<u>3,693,600</u>
Increase in net assets	6,545,800	9,060,500	15,606,300	-	15,606,300
Net assets, beginning of year	<u>132,706,600</u>	<u>171,561,700</u>	<u>304,268,300</u>	<u>-</u>	<u>304,268,300</u>
Net assets, end of year	<u>\$ 139,252,400</u>	<u>\$ 180,622,200</u>	<u>\$ 319,874,600</u>	<u>\$ -</u>	<u>\$ 319,874,600</u>

APPENDIX C

SUMMARY OF PRINCIPAL DOCUMENTS

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TABLE OF CONTENTS

	<u>Page</u>
DEFINITIONS OF CERTAIN TERMS.....	C-1
MASTER INDENTURE	C-13
General	C-13
Authorization, Issuance and Form of Obligations	C-14
Covenants of the Members.....	C-14
Payments of Required Payments.....	C-14
Covenants as to Maintenance of Properties, Etc.	C-14
Insurance Required.	C-15
Negative Pledge.	C-15
Limitations on Additional Indebtedness.	C-15
Restrictions on Guarantees.....	C-17
Calculation of Debt Service; Debt Service Coverage; Annual Rate Covenant	C-17
Sale, Lease or Other Disposition of Property.....	C-19
Consolidation, Merger, Acquisition, Sale or Conveyance.	C-19
Membership in Obligated Group.	C-20
Withdrawal from Obligated Group.	C-21
Filing of Financial Statements, Reports and Other Information.	C-22
Gross Revenue Account.....	C-23
Liquidity Covenant.	C-24
Defaults	C-24
Events of Default.	C-24
Acceleration; Annulment of Acceleration.....	C-25
Additional Remedies and Enforcement of Remedies.....	C-25
Application of Moneys After Default.	C-26
Holders’ Control of Proceedings.....	C-27
Waiver of Event of Default.	C-27
Supplements and Amendments	C-28
Supplements Not Requiring Consent of Holders.	C-28
Supplements Requiring Consent of Holders.	C-28
Satisfaction and Discharge of Master Indenture.....	C-29
FIRST SUPPLEMENTAL MASTER INDENTURE.....	C-29
General	C-29
Payments on Obligation No. 1; Credits.....	C-29
Prepayment of Obligation No. 1.	C-30
Registration, Number, Negotiability and Transfer of Obligation No. 1.....	C-30
Right to Redeem Obligation No. 1.....	C-30
Events of Default; Acceleration	C-30
Tax Exempt Status	C-31
Additional Covenants.....	C-31
BOND INDENTURE	C-34
General	C-34
Revenues	C-34
Establishment of Funds.....	C-34
Pledge and Assignment; Revenue Fund.....	C-34
Allocation of Revenues.....	C-34
Application of Interest Fund.	C-35
Application of Principal Fund.....	C-35
Application of Sinking Fund.....	C-35
Application of Redemption Fund.....	C-36
Rebate Fund.	C-36
Investment of Moneys in Funds and Accounts.	C-36
Bond Reserve Fund.....	C-37

Particular Covenants	C-38
Tax Covenants.	C-38
Other Covenants; Amendment of Loan Agreement	C-38
Events of Default and Remedies of Bondholders.....	C-39
Events of Default.	C-39
Acceleration of Maturities.....	C-39
Bond Trustee to Represent Bondholders.....	C-40
Bondholders’ Direction of Proceedings.	C-40
Limitation on Bondholders’ Right to Sue.	C-40
Modification or Amendment of the Bond Indenture	C-41
Amendments Permitted.	C-41
Defeasance	C-42
Discharge of Indenture.....	C-42
Miscellaneous.....	C-42
Liability of Authority Limited to Revenues.....	C-42
LOAN AGREEMENT	C-43
General	C-43
Payments	C-43
Loan of Proceeds; Loan Repayments.....	C-43
Additional Payments.	C-43
Obligations Unconditional.	C-43
Events of Default and Remedies	C-44
Events of Default.	C-44
Remedies on Default.....	C-44
DEED OF TRUST.....	C-45
General	C-45
Events of Default.....	C-46

The following is a summary of the legal documents which are not described elsewhere in this Official Statement. These summaries do not purport to be comprehensive and reference should be made to the Master Indenture, Supplement No. 1, Bond Indenture and Loan Agreement for a full and complete statement of their provisions. All capitalized terms not defined in this Official Statement have the meanings set forth in the Bond Indentures and the Loan Agreements.

DEFINITIONS OF CERTAIN TERMS

The following are definitions of certain terms used in this Official Statement including the summaries of the Master Indenture, Supplement No. 1, Bond Indenture and Loan Agreement.

“Accountant” means any firm of nationally recognized independent certified public accountants selected by the Obligated Group Representative and not objected to by the Master Trustee.

“Account Control Agreement” means an agreement providing for (i) control of deposit accounts within the meaning of Division 9 of the California Commercial Code, including Section 9104 of the California Commercial Code or (ii) control of securities accounts within the meaning of Divisions 8 and 9 of the California Commercial Code, including Sections 9106 and 8106 of the California Commercial Code, entered into by the Members of the Obligated Group, the Master Trustee and a Depository Bank.

“Additional Indebtedness” means as to the Corporation any Indebtedness incurred subsequent to the issuance of the Initial Obligations issued under the Initial Related Supplements executed pursuant to the Master Indenture and means as to any other Member, Indebtedness incurred subsequent to becoming a Member, including in either case Obligations issued to evidence, guarantee or secure Indebtedness previously incurred by the Corporation or any such other Member, respectively.

“Additional Payments” means the payments so designated and required to be made by the Corporation pursuant to the Loan Agreement.

“Adjusted Operating Revenues” means, as to any period, total operating and non-operating revenues of the Obligated Group, excluding net unrealized gains (losses) on the valuation of investments and net unrealized derivative contract gains (losses).

“Administrative Fees and Expenses” means any application, commitment, financing or similar fee charged, or reimbursement for administrative or other expenses incurred, by the Authority or the Bond Trustee.

“Affiliate” means: (1) a nonprofit corporation, a majority of the members of the Governing Body of which are (i) the same as the corporate members or directors of a Member, (ii) subject to election or appointment by a Member, (iii) subject to election or appointment by a corporation which has the power to elect or appoint at least 50% of the members of the Governing Body of a Member, or (iv) that has the power to elect or appoint a majority of the members of the Governing Body of a Member; or (2) a for-profit corporation, at least 50% of whose voting stock is owned by a Member or an Affiliate.

“Annual Debt Service” means for each Fiscal Year the aggregate amount (without duplication) of (1) principal and interest scheduled to become due (either by maturity or by mandatory redemption or mandatory prepayment, but excluding optional prepayments and redemptions) and sinking fund payments required to be paid in that Fiscal Year on all Long-Term Indebtedness, (2) all payments made on a Guaranty of Long-Term Indebtedness, and (3) the aggregate amount of Master Indenture Obligation Payments to be paid in that Fiscal Year, less any amounts of such principal, interest or sinking fund payments to be paid during such Fiscal Year from:

- (a) the proceeds of Indebtedness, or
- (b) moneys or Governmental Obligations, including moneys received from governmental bodies, deposited in an irrevocable escrow for the purpose of paying such principal, interest or sinking fund payments or Master Indenture Obligation Payments, provided such moneys (including, where appropriate, the earnings or other

increment to accrue thereon) are required to be applied to pay, and are sufficient to pay, such principal, interest or sinking fund payments, or;

(c) Capitalized Interest; provided that (i) the amount of such payments for a future period will be calculated in accordance with the Master Indenture; (ii) if a Financial Products Agreement has been entered into by any Member with respect to Long-Term Indebtedness, interest on such Long-Term Indebtedness will be included in the calculation of Annual Debt Service by including for each Fiscal Year an amount equal to the amount of interest payable on such Long-Term Indebtedness in such Fiscal Year at the rate or rates stated in such Long-Term Indebtedness plus any Financial Product Payments payable in such Fiscal Year minus any Financial Product Receipts receivable in such Fiscal Year; provided that in no event will any calculation made pursuant to this clause result in a number less than zero being included in the calculation of Annual Debt Service and provided further that any Financial Product Payments or Financial Product Receipts for any future period with respect to a Financial Product Agreement that is not based on a fixed interest rate will be calculated in accordance with the Master Indenture as if the Financial Product Agreement were Variable Rate Indebtedness; and (iii) with respect to any Long-Term Indebtedness for which the number of actual payments of principal in any Fiscal Year is greater than those in the immediately preceding and/or succeeding Fiscal Years solely by reason of the fact that such principal payments are scheduled to occur other than on a specified date or dates or by reasons of this clause (iii), the last principal payment in such Fiscal Year for which the number of payments is higher will be deemed to be required to be made in the next preceding or succeeding Fiscal Year, as appropriate and as designated by the Obligated Group Representative.

“Authority” means the ABAG Finance Authority for Nonprofit Corporation or its successors and assigns.

“Authorized Representative” means, with respect to the Authority, its Executive Director, Chief Financial Officer, Secretary or any other person as may be designated and authorized to sign for the Authority and, with respect to the Corporation, the Chair of its governing body or its chief executive officer or its chief financial officer or any other person or persons designated as an Authorized Representative of the Corporation by a Certificate of the Corporation signed by the Chair of its governing body or its chief executive officer or chief financial officer, and filed with the Bond Trustee.

“Balloon Indebtedness” means (a) Long-Term Indebtedness, 25% or more of the original principal of which matures during any consecutive twelve-month period, if such maturing principal amount is not required to be amortized below such percentage by mandatory redemption or prepayment prior to such twelve-month period, and (b) Commitment Indebtedness. Balloon Indebtedness does not include Indebtedness which otherwise would be classified under the Master Indenture as Put Indebtedness.

“Bond Indenture” means the Bond Indenture, as originally executed or as it may from time to time be supplemented, modified or amended by any Supplemental Bond Indenture.

“Bond Reserve Fund” means the fund by that name established pursuant to the Bond Indenture.

“Bond Reserve Requirement” means the least of (i) 10% of the principal amount of Bonds at any time Outstanding, (ii) Maximum Annual Bond Service on the Bonds and (iii) 125% of the average Annual Bond Service on all Bonds Outstanding to maturity or earlier mandatory redemption on the date on which such calculation is required in accordance with the terms of the Loan Agreement, calculated by the Corporation under the assumption that the principal amount of the Bonds are paid in accordance herewith.

“Bond Trustee” means The Bank of New York Trust Company, N.A., a national banking association organized and existing under and by virtue of the laws of the United States of America, as trustee under the Bond Indenture.

“Bonds” means ABAG Finance Authority for Nonprofit Corporations Refunding Revenue Bonds (Children’s Hospital & Research Center at Oakland) Series 2007A, authorized by, and at any time Outstanding pursuant to, the Bond Indenture.

“Bond Year” means the period of twelve consecutive months ending on December 1 in any year in which Bonds are Outstanding, except for the initial Bond Year which commences on the Date of the Bonds.

“Book-Entry Form or Book-Entry System” means a form or system, as applicable, under which physical bond certificates in fully registered form are registered only in the name of a Depository or its nominee as Bondholder, with the physical bond certificates held by and “immobilized” in the custody of the Depository and the book-entry system maintained by and the responsibility of others than the Authority or the Bond Trustee is the record that identifies and records the transfer of the interests of the owners of book-entry interests in those Bonds.

“Book Value” means, when used in connection with Property, Plant and Equipment or other Property of any Member, the value of such property, net of accumulated depreciation, as it is carried on the books of such Member and in conformity with generally accepted accounting principles, and when used in connection with Property, Plant and Equipment or other Property of the Obligated Group, means the aggregate of the values so determined with respect to such property of each Member determined in such a way that no portion of such value of property of any Member is included more than once.

“Business Day” means any day (other than a Saturday or Sunday) on which banking institutions in New York, New York, are open for business and on which the Bond Trustee is open for business at its Principal Corporate Trust Office.

“Certificate, Statement, Request, Order or Requisition of the Authority or the Corporation” mean, with respect to the summary of the Bond Indenture, respectively, a written certificate, statement, request, order or requisition signed in the name of the Authority by its Chairman, Secretary or any Member thereof or such other person as may be designated and authorized to sign for the Authority in writing to the Bond Trustee, or in the name of the Corporation by an Authorized Representative of the Corporation. Any such instrument and supporting opinions or representations, if any, may, but need not, be combined in a single instrument with any other instrument, opinion or representation, and the two or more so combined will be read and construed as a single instrument.

“Certificate, Statement, Request, Consent or Order of any Member or of the Master Trustee” mean, with respect to the summary of the Master Indenture, respectively, a written certificate, statement, request, consent or order signed in the name of such Member by its respective Authorized Representative or in the name of the Master Trustee by its Responsible Officer. Any such instrument and supporting opinions or certificates, if any, may, but need not, be combined in a single instrument with any other instrument, opinion or certificate and the two or more so combined will be read and construed as a single instrument.

“Code” means the Internal Revenue Code of 1986, as amended, or any successor statute thereto and any regulations promulgated thereunder.

“Collateral” means all of the following whether now existing or hereafter created or acquired: (a) all Gross Revenues, (b) all Gross Revenue Accounts, (c) all accounts and accounts receivable, including health-care-insurance receivables, and (d) all proceeds of any of the foregoing. The terms “accounts” and “health-care-insurance receivables” are used in the Master Indenture with meanings as defined in the California Commercial Code Division 9. Notwithstanding the foregoing, “Collateral” will not include Restricted Assets.

“Commitment Indebtedness” means the obligation of any Member (a) to repay amounts disbursed pursuant to a commitment from a financial institution to pay, refinance or purchase when due, when tendered or when otherwise required to be purchased or to make a loan for any such purpose (1) other Indebtedness of such Member, or (2) Indebtedness of a Person who is not a Member, which Indebtedness is guaranteed by a Guaranty of such Member or secured by or payable from amounts paid on Indebtedness of such Member, in either case which Indebtedness or Guaranty of such Member was incurred in accordance with the provisions of the Master Indenture, (b) to pay interest payable on amounts disbursed for such purposes, and (c) any fees, costs, expenses and penalties payable to such financial institution in connection with such commitment and enforcement thereof.

“Completion Indebtedness” means any Long-Term Indebtedness or Balloon Indebtedness incurred by any Obligated Group Member for the purpose of financing the completion of constructing or equipping facilities for which Long-

Term Indebtedness or Balloon Indebtedness had theretofore been incurred, to the extent necessary to provide a completed and equipped facility of the type and scope contemplated at the time, and in accordance with the general plans and specifications for such facility as originally prepared with only such changes as have been made in conformance with the documents pursuant to which such Long-Term Indebtedness or Balloon Indebtedness was originally incurred.

“Corporation” means Children’s Hospital & Research Center at Oakland, a nonprofit public benefit corporation duly organized and existing under the laws of the State of California, or any corporation which is the surviving, resulting or transferee corporation of the Corporation in any merger, consolidation or transfer of assets permitted under the Master Indenture.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the Authority or the Corporation and related to the authorization, issuance, sale and delivery of the Bonds, including but not limited to advertising and printing costs, costs of preparation and reproduction of documents, filing and recording fees, initial fees and charges of the Bond Trustee, initial and ongoing fees and charges of the Authority, legal fees and charges, fees and disbursements of consultants and professionals, bond insurance premiums, rating agency fees, fees and charges for preparation, execution, transportation and safekeeping of the Bonds, and any other cost, charge or fee in connection with the original issuance of Bonds.

“Costs of Issuance Fund” means the fund so designated and established pursuant to the Bond Indenture.

“Current Value” means: (a) with respect to Property, Plant and Equipment either (i) the aggregate fair market value of such Property, Plant and Equipment as reflected in the most recent written report of an appraiser not objected to by the Master Trustee and, in the case of real property, who is a member of the American Institute of Real Estate Appraisers (MAI), delivered to the Master Trustee (which report will be dated not more than three (3) years prior to the date as of which Current Value is to be calculated), plus the Book Value of any Property, Plant and Equipment acquired since the last such report, minus the greater of the Book Value or the fair market value (as reflected in such most recent appraiser’s report) of any Property, Plant and Equipment disposed of since the last such report, or (ii) the value equal to a bona fide offer for the purchase of such Property, Plant and Equipment made on an arm’s length basis within six (6) months of the date of the valuation as set forth in an Officer’s Certificate; and (b) with respect to any other Property, the fair market value of such Property, which fair market value will be evidenced in a manner not objected to by the Master Trustee.

“Date of the Bonds” means October 16, 2007.

“Debt Service Coverage Ratio” means, for any period of time, the ratio determined by dividing Income Available for Debt Service for that period by the Annual Debt Service for such period.

“Depository” means any securities depository that is a clearing agency under federal law operating and maintaining, with its participants or otherwise, a book entry-system to record ownership of book-entry interests in Bonds, and to effect transfers of book-entry interests in Bonds in book-entry form, and includes and means initially The Depository Trust Company.

“Depository Bank” means a financial institution which has entered into an Account Control Agreement with one or more Members and the Master Trustee.

“Event of Default” means any of the events specified in the Master Indenture, Supplement No. 1, Bond Indenture or Loan Agreement.

“Favorable Opinion of Bond Counsel” means a written Opinion of Counsel from a firm of recognized standing in the field of obligations, the interest on which is excluded from gross income for purposes of federal income taxation, addressed to the Authority and the Bond Trustee to the effect that the action proposed to be taken is authorized or permitted by the Bond Indenture and will not result in the inclusion of interest on the Bonds in gross income for federal income tax purposes.

“Financial Products Agreement” means a written agreement for the purpose of managing or reducing the Obligated Group’s exposure to fluctuations in interest rates or for any other interest rate, investment, asset or liability managing purposes, entered into either on a current or forward basis by a Member and a Qualified Provider, that provides for an exchange of payments based on interest rates, ceilings or floors on such payments, options on such payments or any combination thereof, or any similar device and that does not constitute an obligation to repay money borrowed, credit extended or the equivalent thereof.

“Financial Product Payments” means payments periodically required to be paid to a counterparty by a Member pursuant to a Financial Products Agreement, including, without limitation, any regularly scheduled payments and any payments due upon termination of such Financial Products Agreement.

“Financial Product Receipts” means amounts periodically required to be paid to a Member by a counterparty pursuant to a Financial Products Agreement.

“Fiscal Year” means that period adopted by the Obligated Group Representative as the annual accounting period for which the Obligated Group Financial Statements will be prepared pursuant to the Master Indenture.

“Fitch” means Fitch Ratings, a corporation organized and existing under the laws of the State of New York, its successors and their assigns, or, if such corporation will be dissolved or liquidated or will no longer perform the functions of a securities rating agency, any other nationally recognized securities rating agency designated by the Corporation by notice to the Authority and the Bond Trustee.

“Government Obligations” means: (1) any bonds or other obligations which as to principal and interest constitute direct obligations of, or are unconditionally guaranteed by, the United States of America, including obligations of the Federal National Mortgage Association, the Government National Mortgage Association, Federal Home Loan Banks, Farmers Home Administration, Federal Home Loan Mortgage Corporation, Private Export Funding Corporation, Student Loan Marketing Association and Government Trust Certificates, and any obligation of any other agency or instrumentality of the government of the United States of America hereafter created, provided such obligation of any agency or instrumentality created is approved for investment by a nationally recognized rating agency, and including interest strips of bonds issued by the Resolution Funding Corporation and held in book-entry form by the Federal Reserve Bank of New York; and (2) any certificates, receipts, securities or other obligations evidencing ownership of, or the right to receive, a specified portion of one or more interest payments or principal payments, or any combination thereof, to be made on any bond, note, or other obligation described in clause (1) above.

“Gross Revenues” means all revenues, income, receipts and money now existing or hereafter received by each Member, including (a) gross revenues collected from its operations and possession of and pertaining to its properties, (b) gifts, grants, bequests, donations and contributions, (c) proceeds derived from (i) condemnation, (ii) insurance, (iii) accounts and accounts receivable, including health-care-insurance receivables, (iv) payment intangibles, (v) securities and other investment property, (vi) inventory and other tangible and intangible property, (vii) medical reimbursement programs and agreements, (viii) contract rights and other rights and assets now or hereafter owned, held or possessed by or on behalf of any Member, and (d) rentals received from the lease of real estate. The terms “accounts,” “health-care-insurance receivables,” “inventory,” “payment intangibles,” “securities” and “investment property” are used in the Master Indenture with meanings as defined in the California Commercial Code Divisions 8 and 9. Notwithstanding the foregoing, “Gross Revenues” will not include Restricted Assets.

“Gross Revenue Accounts” means the deposit accounts or securities accounts now or hereafter designated as “Gross Revenue Accounts” and established pursuant to the Master Indenture.

“Guaranty” means all loan commitments and all obligations of any Member guaranteeing in any manner whatever, whether directly or indirectly, any obligation of any other Person which would, if such other Person were a Member, constitute Indebtedness.

“Holder” means, with respect to the Master Indenture, the registered owner of any Obligation in registered form or the bearer of any Obligation in coupon form which is not registered or is registered to bearer, and, whenever used in the Bond Indenture, means the Person in whose name such Bond is registered.

“Immaterial Affiliates” means Persons whose combined total net assets, as shown on their financial statements for their most recently completed fiscal year, were less than 10% of the combined or consolidated net assets of the Obligated Group (including the net assets of such Persons) for the most recently completed Fiscal Year.

“Indebtedness” means any indebtedness or obligation of any Member for borrowed money as determined in accordance with generally accepted accounting principles, including, without limitation, obligations under conditional sales contracts or other title retention contracts, and rental obligations under leases which are considered capital leases under generally accepted accounting principles, except for obligations of a Member to another Member; provided, however, that if more than one Member will be obligated to pay any obligation, for purposes of any computations or calculations under the Master Indenture, such obligation will be included only one time.

“Interest Fund” means the fund by that name established pursuant to the Bond Indenture.

“Interest Payment Date” means June 1 and December 1 of each year, commencing December 1, 2007.

“Investment Securities” means any of the following that at the time are legal investments under the laws of the State of California for moneys held under the Bond Indenture and then proposed to be invested therein:

(A) United States Government Obligations;

(B) bonds, debentures, notes or other evidences of indebtedness issued by any of the following agencies or any other like governmental or government-sponsored agencies that are hereafter created: Federal Farm Credit Bank; Federal Intermediate Credit Banks; Federal Financing Bank; Federal Home Loan Bank System; Federal Home Loan Mortgage Corporation; Federal National Mortgage Association; Tennessee Valley Authority; Student Loan Marketing Association; Export-Import Bank of the United States; Farmers Home Administration; Small Business Administration; Inter-American Development Bank; International Bank for Reconstruction and Development; Federal Land Banks; and Government National Mortgage Association;

(C) direct and general obligations of any state of the United States of America or any municipality or political subdivision of such state, or obligations of any corporation, if such obligations are rated in one of the two highest Rating Categories by each Rating Agency then rating both the Bonds and such obligations (but in all cases by at least one Rating Agency then rating the Bonds);

(D) commercial paper rated at the time of investment in the highest Rating Category by each Rating Agency then rating both the Bonds and such obligations (but in all cases by at least one Rating Agency then rating the Bonds);

(E) negotiable or non-negotiable certificates of deposit, time deposits, or other similar banking arrangements, issued by any bank or trust company (including the Bond Trustee and its affiliates) or any savings and loan association, and either

(i) the long-term obligations of such bank or trust company are rated in the highest Rating Category by each Rating Agency then rating the Bonds and such obligations (but in all cases by at least one Rating Agency then rating the Bonds), or

(ii) the deposits or other arrangements are continuously secured as to principal, but only to the extent not insured by the Federal Deposit Insurance Corporation or similar corporation chartered by the United States of America, (a) by depositing with a bank or trust company, as collateral security, obligations described in paragraph (A) or (B) above in an aggregate principal amount equal to a least 105% of the amount so deposited or, with the approval of the Bond Trustee, other marketable securities eligible as securities for the deposit of trust funds under applicable regulations of the Comptroller of the Currency of

the United States or applicable state law or regulations, having a market value (exclusive of accrued interest) not less than the amount of such deposit, or (b) if the furnishing of security as provided in clause (a) of this paragraph is not permitted by applicable law, in such other manner as may then be required or permitted by applicable state or federal laws and regulations regarding the security for, or granting a preference in the case of, the deposit of trust funds;

(F) repurchase agreements with respect to obligations listed in paragraph (A) or (B) above if entered into with a bank, a trust company or a broker or dealer (as defined by the Securities Exchange Act of 1934) that is a dealer in government bonds, that reports to, trades with and is recognized as a primary dealer by a Federal Reserve Bank, if such obligations that are the subject of such repurchase agreement are delivered to the Bond Trustee or are supported by a safekeeping receipt issued by a depository (other than the Bond Trustee) satisfactory to the Bond Trustee, provided that such repurchase agreement must provide that the value of the underlying obligations will be maintained at a current market value, calculated no less frequently than monthly, of not less than the repurchase price;

(G) shares or certificates in any short-term investment fund that is maintained or utilized by the Bond Trustee and which fund invests solely in other Investment Securities, including money market funds for which the Bond Trustee and its affiliates provide investment advisory or other management services;

(H) investment agreements with any financial institution that at the time of investment has long-term obligations rated in one of the three highest Rating Categories by each Rating Agency then rating both the Bonds and such obligations (but in all cases by at least one Rating Agency then rating the Bonds);

(I) shares or certificates in any registered mutual fund invested solely in Investment Securities described in clauses (A) – (H) of this definition; and

(J) obligations (including asset-backed and mortgage-backed obligations) of any corporation, partnership, trust or other entity which are rated in one of the two highest Rating Categories by each Rating Agency then rating both the Bonds and such obligations (but in all cases by at least one Rating Agency then rating the Bonds).

“Lien” means any mortgage or pledge of, or security interest in, or lien or encumbrance on, any Property, excluding Liens applicable to Property in which any Member has only a leasehold interest unless the Lien is with respect to such leasehold interest.

“Loan Agreement” means that certain loan agreement by and between the Authority and the Corporation, dated as of October 1, 2007, as originally executed and as it may from time to time be supplemented, modified or amended in accordance with the terms thereof and of the Bond Indenture.

“Loan Default Event” means any of the events specified in the Loan Agreement.

“Loan Repayments” means the payments so designated and required to be made by the Corporation pursuant to the Loan Agreement.

“Long-Term Indebtedness” means Indebtedness (which also may constitute Balloon Indebtedness or Put Indebtedness) having an original maturity greater than 1 year or renewable at the option of a Member for a period greater than 1 year from the date of original incurrence or issuance thereof unless, by the terms of such Indebtedness, no Indebtedness is permitted to be outstanding thereunder for a period of at least 30 consecutive days during each calendar year.

“Management Consultant” means a firm (but not an individual), which (1) is in fact independent, (2) does not have any direct financial interest or any material indirect financial interest in any Member or any Affiliate and (3) is not connected with any Member or any Affiliate as a director, officer, partner, employee, trustee, promoter or person performing similar functions, designated by the Obligated Group Representative, not objected to by the Master

Trustee, and having the skill and experience necessary to render the particular report or certification required by the provision of the Master Indenture in which such requirement appears.

“Mandatory Sinking Account Payment” means the amount required by the Bond Indenture to be paid by the Authority on any single date for the retirement of Bonds of any Series.

“Master Indenture” means that certain master indenture of trust, dated as of October 1, 2007, among the Corporation, the other Member of the Obligated Group named therein and the Master Trustee, as originally executed and as it may from time to time be supplemented, modified or amended in accordance with the terms thereof.

“Master Indenture Obligation Payments” means payments (however designated) required under any Obligation then Outstanding that does not constitute Indebtedness.

“Master Trustee” means The Bank of New York Trust Company, N.A., or its successor, as successor master trustee under the Master Indenture.

“Material Members” means the Members whose combined total net assets, as shown on their financial statements for their most recently completed fiscal year, were equal to or greater than 90% of the combined or consolidated net assets of the entire Obligated Group for the most recently completed Fiscal Year of the Obligated Group.

“Maximum Annual Debt Service” means the highest total Annual Debt Service for the current or any succeeding Fiscal Year.

“Maximum Debt Service Coverage Ratio” means, for any period of time, the ratio determined by dividing Income Available for Debt Service for that period by Maximum Annual Debt Service.

“Maximum Annual Bond Service” means, as of any date of calculation, the highest Annual Bond Service for the current or any succeeding Bond Year for all then Outstanding Bonds.

“Member” or “Members” means the Corporation and each other Person that is then obligated under the Master Indenture.

“Non-Recourse Indebtedness” means any Indebtedness (i) which is secured by a Lien, liability for which is effectively limited to the real property, improvements or equipment acquired with such Non-Recourse Indebtedness and the income therefrom, with no recourse directly or indirectly to any Member, and (ii) which is not a general obligation of any Member.

“Obligated Group” means the Corporation and each other Person that becomes and is a Member of the Obligated Group pursuant to the terms of the Master Indenture.

“Obligated Group Financial Statements” has the meaning set forth in the Master Indenture.

“Obligated Group Representative” means the Corporation or such other Member (or Members acting jointly) as may have been designated pursuant to written notice to the Master Trustee executed by all of the Members.

“Obligation” means any obligation of the Obligated Group issued under the Master Indenture, as a joint and several obligation of each Member, which has been authenticated by the Master Trustee, and which may be in any form set forth in a Related Supplement, including but not limited to bonds, debentures, notes, reimbursement agreements, loan agreements, guarantees, leases and Financial Products Agreements. Reference to a Series of Obligations or to Obligations of a Series means a Series of Obligations or Obligations of a Series issued pursuant to a single Related Supplement.

“Obligation No. 1” means the obligation issued under the Master Indenture and Supplement No. 1 evidencing the Obligated Group’s obligation to make Loan Repayments.

“Opinion of Bond Counsel” means a written opinion signed by an attorney or firm of attorneys not objected to by the Master Trustee and experienced in the field of public finance whose opinions are generally accepted by purchasers of obligations issued by or on behalf of a Government Issuer.

“Opinion of Counsel” means a written opinion of counsel (who may be counsel for the Authority) selected by the Authority. If and to the extent required by the provisions of the Bond Indenture, each Opinion of Counsel will include the statements provided for in the Bond Indenture.

“Optional Redemption Account” means the account by that name in the Redemption Fund established pursuant to the Bond Indenture.

“Outstanding,” when used with reference to Obligations or Indebtedness, means, as of any date of determination, all Obligations or Indebtedness, as appropriate, theretofore issued or incurred and not paid and discharged other than (a) Obligations theretofore cancelled by the Master Trustee or delivered to the Master Trustee for cancellation, (b) Obligations in lieu of which other Obligations have been authenticated and delivered or have been paid pursuant to the provisions of a Related Supplement regarding mutilated, destroyed, lost or stolen Obligations unless proof satisfactory to the Master Trustee has been received that any such Obligation is held by a bona fide purchaser, (c) any Obligation held by any Member, (d) any Obligation that secures Related Bonds, if the Related Bonds are no longer outstanding under the terms of the Related Bond Indenture, and (e) Indebtedness deemed paid and no longer outstanding pursuant to the terms thereof; provided, however, that if two or more obligations which constitute Indebtedness represent the same underlying obligation (as, for example, when an Obligation secures an issue of Related Bonds and another Obligation secures repayment obligations to a bank under a letter of credit which secures such Related Bonds), for purposes of the various financial covenants contained in the Master Indenture, but only for such purposes, only one of such Obligations will be deemed Outstanding and the Obligation so deemed to be Outstanding will be that Obligation that produces the greater amount of debt service to be included in the calculation being made.

“Permitted Encumbrances” means and include:

(a) Any judgment lien or notice of pending action against any Member so long as such judgment or pending action is being contested and execution thereon is stayed or while the period for responsive pleading has not lapsed;

(b) (i) Rights reserved to or vested in any municipality or public authority by the terms of any right, power, franchise, grant, license, permit or provision of law, affecting any Property; (ii) any liens on any Property for taxes, assessment, levies, fees, water and sewer charges, and other governmental and similar charges and any liens of mechanics, materialmen, laborers, suppliers or vendors for work or services performed or materials furnished in connection with such Property, which are not due and payable or which are not delinquent, or the amount or validity of which, are being contested and execution thereon is stayed or for which adequate reserves have been set aside, or, with respect to liens of mechanics, materialmen and laborers, have been due for less than sixty (60) days or which have been bonded for; (iii) easements, rights-of-way, servitudes, restrictions and other minor defects, encumbrances, and irregularities in the title to any Property which do not materially impair the use of such Property or materially and adversely affect the value thereof; (iv) rights reserved to or vested in any municipality or public authority to control or regulate any Property or to use such Property in any manner, which rights do not materially impair the use of such Property in any manner, or materially and adversely affect the value thereof; (v) present or future valid ongoing laws and ordinances; and (vi) to the extent that it affects title to any Property, the Master Indenture and any Related Bond Indenture;

(c) Any Lien described in the Master Indenture which is existing on the date of execution of the Master Indenture, provided that no such Lien or the amount of Indebtedness secured thereby (other than Liens described in clause (b) of this definition) may be increased, extended, renewed or modified to apply to any Property of any Member not subject to such Lien on such date, unless such Lien as so extended, renewed or modified otherwise qualifies as a Permitted Encumbrance under the Master Indenture;

(d) Any Lien in favor of the Master Trustee securing all Obligations (other than Non-Recourse Indebtedness) on a parity basis;

(e) Liens arising by reason of good faith deposits with any Member in connection with leases of real estate, bids or contracts (other than contracts for the payment of money), deposits by any Member to secure public or statutory obligations, or to secure, or in lieu of, surety, stay or appeal bonds, and deposits as security for the payment of taxes or assessments or other similar charges;

(f) Any Lien arising by reason of deposits with, or the giving of any form of security to, any governmental agency or any body created or approved by law or governmental regulation for any purpose at any time as required by law or governmental regulation as a condition to the transaction of any business or the exercise of any privilege or license, or to enable any Member to maintain self-insurance or to participate in any funds established to cover any insurance risks or in connection with workers' compensation, unemployment insurance, pension or profit sharing plans or other similar social security plans, or to share in the privileges or benefits required for companies participating in such arrangements, and any Lien in the nature of a banker's lien or right of setoff with respect to deposits which any Member is required to maintain with the bank in question;

(g) Any Lien arising by reason of any escrow established to pay debt service with respect to Indebtedness;

(h) Any Lien on the proceeds of Indebtedness in favor of the trustee with respect to such Indebtedness prior to the application of such proceeds;

(i) Liens on moneys deposited by patients or others with any Member as security for or as prepayment for the cost of patient care;

(j) Liens on Property received by any Member through gifts, grants or bequests, such Liens being due to restrictions on such gifts, grants or bequests of Property or the income thereon, up to the fair market value of such Property;

(k) Statutory rights of the United States of America by reason of federal funds made available under 42 U.S.C. Section 291 et seq. and similar rights under other federal and state statutes or regulations by reason of federal or state funds being made available to the Obligated Group Representative or any other Member under such federal or state statutes or regulations;

(l) Liens securing Non-Recourse Indebtedness;

(m) Liens on Property acquired by a Member if an Officer's Certificate is delivered to the Master Trustee certifying that (i) the Lien and the Indebtedness secured thereby were created and incurred by a Person other than a Member prior to the acquisition of such Property by a Member, and (ii) the Lien was created prior to the decision of the Member to acquire the Property and was not created for the purpose of enabling a Member to avoid the limitations of the Master Indenture on creation of Liens on Property of the Obligated Group;

(n) Liens resulting from a Person's becoming a Member pursuant to the Master Indenture or from a consolidation, merger or acquisition of assets;

(o) Liens on accounts receivable and the proceeds thereof securing Secured Short-Term Indebtedness incurred in accordance with the Master Indenture;

(p) Any leases entered into in the ordinary course of business, any leases entered into in accordance with the provisions set forth in the Master Indenture, any leases, licenses or similar rights existing as of the date of the initial execution and delivery of the Master Indenture and any renewals and extensions thereof; and any leases, licenses or similar rights to use Property whereunder a Member is lessee, licensee or the equivalent thereof;

(q) Liens on Property due to rights of third party payors for recoupment of excess reimbursement amounts paid to any Member;

(r) Purchase money security interests, whether existing at the time of execution and delivery of the Master Indenture or hereafter created;

(s) Liens securing the interest of a vendor or lessor under any conditional sale agreement, capital lease or other title agreement entered into in connection with the acquisition of the Property subject to such Lien;

(t) Liens which would be permitted by the Master Indenture if the creation of such Lien were treated as a disposition of the Property subject to such Lien;

(u) (i) Lien securing obligations of a Member to repay amounts owing under a Financial Products Agreement; and (ii) Liens on Property of a Member delivered as collateral to secure amounts payable under a Financial Products Agreement; and

(v) any other Lien on Property provided that:

(i) the Current Value of all Property encumbered by all Liens incurred pursuant to this clause (v) does not exceed 10% of the Current Value of all Property of the Obligated Group at the time of creation of such Lien; or

(ii) the Book Value of all Property encumbered by all Liens incurred pursuant to this clause (v) does not exceed 10% of the Book Value of all Property of the Obligated Group at the time of creation of such Lien; or

(iii) the principal amount of Indebtedness secured by all Liens incurred pursuant to this clause (v) does not exceed 10% of the lesser of the Current Value and the Book Value of all Property of the Obligated Group at the time of creation of such Lien.

“Person” means an individual, corporation, firm, association, partnership, trust or other legal entity or group of entities, including a governmental entity or any agency or political subdivision thereof.

“Pledged Assets” means, with respect to Supplement No. 1, the property described in the Deed of Trust, including but not limited to land, facilities, appurtenances, equipment, rents, proceeds, accounts, inventory, approvals and intangibles.

“Primary Obligor” means the Person who is primarily obligated on an obligation.

“Principal Fund” means the fund by that name established pursuant to the Bond Indenture.

“Prior Bonds” means the Insured Certificates of Participation (Children’s Hospital Medical Center of Northern California), Series 1999.

“Property” means: (i) any and all rights, titles and interests in and to any and all real property of any Member of the Obligated Group; (ii) all buildings and structures thereon and fixtures and improvements thereto, whether now existing or hereafter constructed, installed or acquired; (iii) all tangible personal property, whether now existing or hereafter acquired, and used in, around or about the real property of any Member of the Obligated Group; (iv) cash and investments; and (v) intangible personal property, wherever situated.

“Put Date” means (a) any date on which an owner of Put Indebtedness may elect to have such Put Indebtedness paid, purchased or redeemed by or on behalf of the underlying obligor prior to the stated maturity date or (b) any date on which Put Indebtedness is required to be paid, purchased or redeemed from the owner by or on behalf of the underlying obligor (other than at the option of the owner) prior to the stated maturity date, other than pursuant to any mandatory sinking fund or other similar fund or other than by reason of acceleration upon the occurrence of an event of default.

“Put Indebtedness” means Indebtedness that is (a) payable or required to be purchased or redeemed by or on behalf of the underlying obligor, at the option of the owner thereof, prior to its stated maturity date or (b) payable or required to be purchased or redeemed from the owner by or on behalf of the underlying obligor (other than at the option of the owner) prior to its stated maturity date, other than pursuant to any mandatory sinking fund or other similar fund or other than by reason of acceleration upon the occurrence of an event of default.

“Rating Agency” means S&P and Fitch.

“Rebate Fund” means the Rebate Fund established pursuant to the Bond Indenture.

“Redemption Fund” means the fund by that name established pursuant to the Bond Indenture.

“Redemption Price” means, with respect to any Bond (or portion thereof), the principal amount of such Bond (or portion) plus the applicable premium, if any, payable upon redemption thereof pursuant to the provisions of such Bond and the Bond Indenture.

“Related Bonds” means the revenue bonds, certificates of participation or other obligations issued or authorized to be executed and delivered by any Government Issuer, pursuant to a single Related Bond Indenture, the proceeds of which are loaned or otherwise made available to a Member in consideration of the execution, authentication and delivery of an Obligation or Obligations to or for the order of such Government Issuer or a Related Bond Trustee.

“Related Bond Indenture” means any indenture, bond resolution, trust agreement or other comparable instrument pursuant to which a series of Related Bonds is issued or executed and delivered.

“Related Bond Issuer” means the Government Issuer of any issue of Related Bonds.

“Related Bond Trustee” means the trustee and its successors in the trusts created under any Related Bond Indenture, and if there is no such trustee, means the Related Bond Issuer.

“Related Supplement” means an indenture supplemental to, and authorized and executed pursuant to the terms of, the Master Indenture.

“Required Payment” means any payment required to be made by any Member under the Master Indenture, any Related Supplement or any Obligation, whether at maturity, by acceleration, upon proceeding for redemption or otherwise.

“Revenues” means all amounts received by the Authority or the Bond Trustee for the account of the Authority pursuant or with respect to the Loan Agreement or Obligation No. 1, including, without limiting the generality of the foregoing, Loan Repayments (including both timely and delinquent payments and any late charges, and whether paid from any source), prepayments, insurance proceeds, condemnation proceeds, and all interest, profits or other income derived from the investment of amounts in any fund or account established pursuant to the Bond Indenture, but not including any Administrative Fees and Expenses, any moneys required to be deposited in the Rebate Fund or any interest, profits or other income required to be retained in the Rebate Fund.

“S&P” means Standard & Poor’s, a division of The McGraw-Hill Companies, Inc., a corporation organized and existing under the laws of the State of New York, its successors and their assigns, or, if such corporation will be dissolved or liquidated or will no longer perform the functions of a securities rating agency, any other nationally recognized securities rating agency designated by the Corporation by notice to the Authority and the Bond Trustee.

“Secured Short-Term Indebtedness” means Short-Term Indebtedness secured by a Lien on accounts receivable of the Members.

“Serial Bonds” means the Bonds falling due by their terms in specified years, for which no Mandatory Sinking Account Payments are provided.

“Short-Term Indebtedness” means all Indebtedness which has an original term less than or equal to 1 year and which is not renewable or extendable at the option of a Member to a date or for a term greater than 1 year from the date of original incurrence or issuance unless, by the terms of such Indebtedness, no Indebtedness is permitted to be outstanding thereunder for a period of at least 30 consecutive days during each calendar year.

“Special Redemption Account” means the account by that name in the Redemption Fund established pursuant to the Bond Indenture.

“Subordinated Indebtedness” means Indebtedness that by its terms is specifically subordinated to all Outstanding Obligations with respect to any security therefor and with respect to right of payment upon default of all Outstanding Obligations and all other obligations of a Member not containing such subordination provision.

“Supplemental Bond Indenture” means any indenture hereafter duly authorized and entered into between the Authority and the Bond Trustee, supplementing, modifying or amending the Bond Indenture; but only if and to the extent that such Supplemental Bond Indenture is specifically authorized under the Bond Indenture.

“Supplement No. 1” means that certain first supplemental master trust indenture, dated as of October 1, 2007, between the Members of the Obligated Group and the Master Trustee, pursuant to which Obligation No. 1 is issued.

“Tax Agreement” means the Tax Agreement delivered by the Authority and the Corporation at the time of issuance and delivery of the Bonds, as the same may be amended or supplemented in accordance with its terms.

“Term Bonds” means the Bonds payable at or before their specified maturity date or dates from Mandatory Sinking Account Payments established for that purpose and calculated to retire such Bonds on or before their specified maturity date or dates.

“United States Government Obligations” means:

(A) direct obligations of the United States of America (including obligations issued or held in book-entry form on the books of the Department of the Treasury of the United States of America) or obligations the timely payment of which are fully guaranteed by the United States of America;

(B) certificates or other instruments that evidence direct ownership of future principal and/or interest on obligations described in clause (A), provided that such obligations are held in the custody of a bank or trust company acceptable to the Bond Trustee in a special account separate from the general assets of such custodian; and

(C) obligations (1) the interest on which is excluded from gross income for federal income tax purposes pursuant to Section 103 of the Code, (2) the timely payment of the principal of and interest on which is fully provided for by the deposit in trust or escrow of cash or obligations described in clauses (A) or (B), and (3) that are rated in the highest Rating Category by each Rating Agency then rating the Bonds.

“Variable Rate Indebtedness” means any portion of Indebtedness the interest rate on which may vary or adjust pursuant to a predetermined formula or otherwise, whether by the terms of such Indebtedness or as a result of a Financial Products Agreement that has been entered into by any Member with respect to such Indebtedness.

MASTER INDENTURE

General

The Master Indenture authorizes the issuance of Obligations by the Obligated Group, which may be unsecured general obligations or, to the extent permitted by the Master Indenture, secured by a claim on Property. Certain provisions of the Master Indenture are summarized below. This summary does not purport to be complete or definitive and is qualified by reference to the full terms of the Master Indenture.

Authorization, Issuance and Form of Obligations

From time to time when authorized by the Master Indenture and subject to the terms, conditions and limitations established in the Master Indenture, the Obligated Group Representative may authorize the issuance of an Obligation or a Series of Obligations by entering into a Related Supplement. The Obligation or the Obligations of any such Series may be issued and delivered to the Master Trustee for authentication upon compliance with the provisions of the Master Indenture and of any Related Supplement.

Each Related Supplement authorizing the issuance of an Obligation or a Series of Obligations will specify and determine the principal amount of such Obligation or Series of Obligations, the purposes for which such Obligation or Series of Obligations are being issued, the form, title, designation, and the manner of numbering or denominations, if applicable, of such Obligation or Series of Obligations, the date or dates of maturity of such Obligation or Series of Obligations, the date of issuance of such Obligations, the rate or rates of interest (or method of determining the rate or rates of interest) borne by such Obligation or Series of Obligations, if applicable, and any other provisions deemed advisable or necessary by the Obligated Group Representative.

Covenants of the Members

Payments of Required Payments.

Each Member jointly and severally covenants to pay or cause to be paid promptly all Required Payments, including the principal of and premium, if any, and interest on each Obligation issued under the Master Indenture, at the place, on the dates and in the manner provided in the Master Indenture, in any Related Supplement and in said Obligations whether at maturity, upon proceedings for redemption, by acceleration or otherwise.

Covenants as to Maintenance of Properties, Etc.

Each Member, respectively, covenants and agrees:

(a) That it will operate and maintain its Property, Plant and Equipment in accordance with all valid and applicable governmental laws, ordinances, approvals and regulations including, without limitation, such zoning, sanitary, pollution and safety ordinances and laws and such rules and regulations thereunder as may be binding upon it; provided, however, that no Member will be required to comply with any law, ordinance, approval or regulation as long as it will in good faith contest the validity thereof. Each Member, respectively, further covenants and agrees that it will maintain and operate its Property, Plant and Equipment and all engines, boilers, pumps, machinery, apparatus, fixtures, fittings and equipment of any kind in or that will be placed in any building or structure now or hereafter at any time constituting part of its Property, Plant and Equipment in good repair, working order and condition, and that it will from time to time make or cause to be made all necessary and proper replacements, repairs, renewals and improvements so that the operations of such Members will not be materially and adversely impaired.

(b) That it will pay and discharge all applicable taxes, assessments, governmental charges of any kind whatsoever, water rates, meter charges and other utility charges which may be or have been assessed or which may have become liens upon the Property, Plant and Equipment, and will make such payments or cause such payments to be made, respectively, in due time to prevent any delinquency thereon or any forfeiture or sale of the Property, Plant and Equipment or any part thereof, and, upon request, will furnish to the Master Trustee receipts for all such payments, or other evidences satisfactory to the Master Trustee; provided, however, that no Member will be required to pay any tax, assessment, rate or charge as provided in the Master Indenture as long as it will in good faith contest the validity thereof, provided that such Member will have set aside reserves with respect thereto that, in the opinion of the Governing Body of the Obligated Group Representative, are adequate.

(c) That it will pay or otherwise satisfy and discharge all of its obligations and Indebtedness and all demands and claims against it as and when the same become due and payable, other than any thereof (exclusive of the Obligations issued and Outstanding under the Master Indenture) whose validity, amount or collectibility is being contested in good faith.

(d) That it will at all times comply with all terms, covenants and provisions of any Liens applicable to such Member at such time existing upon its Properties or any part thereof or securing any of its Indebtedness, the failure to comply with which would have a material adverse effect on the operations of the Obligated Group or its Properties.

(e) That it will use its best efforts (as long as it is in its best interests consistent with prudent business practice) to maintain all permits, licenses and other governmental approvals necessary for the operation of its Properties.

(f) That it will not take any action or suffer any action to be taken by others that would result in the interest on any Related Bond issued as a tax-exempt obligation becoming subject to federal income taxation.

Insurance Required.

(a) Each Member, respectively, covenants and agrees that, it will keep the Property, Plant and Equipment and all of its operations adequately insured at all times and carry and maintain such insurance in amounts which are customarily carried, subject to customary deductibles, and against such risks as are customarily insured against by other corporations in connection with the ownership and operation of facilities of similar character and size.

(b) The Obligated Group Representative will employ an Insurance Consultant at least once every two (2) years to review the insurance requirements of the Members. If the Insurance Consultant makes recommendations for the increase of any of the Obligated Group's insurance coverage, the Obligated Group Representative will increase or cause to be increased such coverage in accordance with such recommendations, subject to a good faith determination of the Governing Body of the Obligated Group Representative that such recommendations, in whole or in part, are in the best interests of the Obligated Group. In lieu of maintaining insurance coverage, the Members will have the right to adopt alternative risk management programs which the Governing Body of the Obligated Group Representative determines to be reasonable, including, without limitation, to self-insure in whole or in part individually or in connection with other institutions, to participate in programs of captive insurance companies, to participate with other health care institutions in mutual or other cooperative insurance or other risk management programs, to participate in state or federal insurance programs, to take advantage of state or federal laws now or hereafter in existence limiting medical and malpractice liability, or to establish or participate in other alternative risk management programs; all as will be approved, in writing, as reasonable and appropriate risk management by the Insurance Consultant and reviewed each year thereafter.

Negative Pledge.

Each Member, respectively, covenants and agrees that it will not create, assume or suffer to exist any Lien upon the Property and each Member, respectively, further covenants and agrees that if such a Lien is created or assumed, such Member will make or cause to be made effective a provision whereby all Obligations will be secured prior to or equally and ratably with any such Indebtedness or other obligation secured by such Lien; provided, however, that, notwithstanding the provisions of the Master Indenture, each Member may create, assume or suffer to exist Permitted Encumbrances.

Limitations on Additional Indebtedness.

Each Member, respectively, agrees that it will not incur any Additional Indebtedness except as follows:

(a) Long-Term Indebtedness, if, prior to the incurrence of any Long-Term Indebtedness, one of the following two conditions will be met: (i) there is delivered to the Master Trustee an Officer's Certificate, accompanied by the certificate of an Accountant confirming the contents thereof, certifying the Maximum Debt Service Coverage Ratio (taking into account all Outstanding Long-Term Indebtedness and the Long-Term Indebtedness then to be incurred) for the most recent Fiscal Year for which audited financial statements are available and that such Maximum Debt Service Coverage Ratio is not less than 1.25; or (ii) (A) there is delivered to the Master Trustee an Officer's Certificate certifying the Debt Service Coverage Ratio (taking into account all

Outstanding Long-Term Indebtedness, but not the Long-Term Indebtedness then to be incurred) for the most recent Fiscal Year for which audited financial statements are available and that such Debt Service Coverage Ratio is not less than 1.50; and (B) there will be filed with the Master Trustee the report of a Management Consultant to the effect that the forecast Maximum Debt Service Coverage Ratio, taking the proposed Long-Term Indebtedness into account, for (i) in the case of Long-Term Indebtedness (other than a Guaranty) to finance capital improvements, each of the two Fiscal Years succeeding the date on which such capital improvements are expected to be in operation, or (ii) in the case of Long-Term Indebtedness not financing capital improvements or in the case of a Guaranty, each of the two Fiscal Years succeeding the date on which the Indebtedness is incurred, is not less than 1.50, as shown by forecast statements of revenue and expense for each such period, accompanied by a statement of the relevant assumptions upon which such forecasted statements are based.

(b) Completion Indebtedness without limit.

(c) Long-Term Indebtedness for the purpose of refunding any Outstanding Long-Term Indebtedness so as to render it no longer Outstanding if the Master Trustee receives an Officer's Certificate to the effect that Maximum Annual Debt Service following such refunding does not exceed 115% of Maximum Annual Debt Service prior to such refunding.

(d) Short-Term Indebtedness incurred in the ordinary course of business if immediately after the incurrence of such Short-Term Indebtedness: (i) the Outstanding principal amount of all such Short-Term Indebtedness does not exceed 15% of the Adjusted Operating Revenues for the most recent Fiscal Year for which audited financial statements are available; and (ii) the aggregate of the Outstanding Short-Term Indebtedness incurred under the Master Indenture and the Outstanding liabilities under capitalized leases and other Indebtedness incurred will not exceed 25% of the Adjusted Operating Revenues for the most recent Fiscal Year for which audited financial statements are available; provided, however, that, for a period of thirty (30) consecutive calendar days in each such Fiscal Year, the amount of Short-Term Indebtedness Outstanding must be reduced to an amount not greater than 3% of the maximum amount of Adjusted Operating Revenues for the most recent Fiscal Year for which audited financial statements are available.

(e) Non-Recourse Indebtedness provided that the aggregate principal amount of such Non-Recourse Indebtedness does not exceed 25% of the Adjusted Operating Revenues for the most recent Fiscal Year for which audited financial statements are available.

(f) Balloon Indebtedness, provided that, at the time such Balloon Indebtedness is to be incurred the conditions described in the Master Indenture are met with respect to such Balloon Indebtedness, assuming such Balloon Indebtedness to be Long-Term Indebtedness, as if it were being repaid in substantially equal annual installments of principal and interest over a term equal to the longer of 30 years or the number of years from the date of calculation to the date of maturity of such Indebtedness under the terms of such Indebtedness, and bearing interest at an interest rate equal to the rate at which the Obligated Group or, if not Indebtedness of the Obligated Group, the Primary Obligor could reasonably be expected to borrow for such term; provided that there will be delivered to the Master Trustee, together with any Officer's Certificate or report of a Management Consultant required by the Master Indenture, a letter of a Management Consultant or a banking or investment banking institution knowledgeable in matters of health care finance, confirming that the interest rate assumption set forth in such certificate complies with the requirements of the Master Indenture.

(g) Put Indebtedness, provided that, at the time such Put Indebtedness is to be incurred, the conditions described in the Master Indenture are met with respect to such Put Indebtedness, assuming such Put Indebtedness to be Long-Term Indebtedness, as if it were being repaid in substantially equal annual installments of principal and interest over a term equal to the longer of 30 years, commencing with the next succeeding Put Date, or the number of years from the next succeeding Put Date to the date of maturity of such Indebtedness under the terms of such Indebtedness, and bearing interest at an interest rate equal to the rate at which the Obligated Group or, if not, Indebtedness of the Obligated Group, the Primary Obligor could reasonably be expected to borrow for such term; provided that there will be delivered to the Master Trustee, together with any Officer's Certificate or report of a Management Consultant required by the Master Indenture, a letter of a Management Consultant or a banking or investment banking institution knowledgeable in matters of health care finance, confirming that the interest rate assumption set forth in such certificate complies with the requirements of the Master Indenture.

(h) Variable Rate Indebtedness incurred pursuant to the Master Indenture, provided that the interest rate on such Variable Rate Indebtedness for periods when the actual interest rate cannot yet be determined will be assumed to be equal to 120% of the average interest rate calculated, in a manner acceptable to the Master Trustee, pursuant to the provisions of the agreement pursuant to which such Variable Rate Indebtedness was incurred, during the one calendar year prior to the date of calculation or the interest rate that would have been the average interest rate calculated during the one year prior to the date of calculation had such Variable Rate Indebtedness been outstanding for the previous year.

(i) Reimbursement or other repayment obligations arising under reimbursement or similar agreements with banks or other financial institutions relating to letters or lines of credit or similar credit facilities used to secure Indebtedness.

(j) Liabilities under capitalized lease agreements for the lease of, or indebtedness for money borrowed or liabilities under instruments evidencing deferred payment arrangements for the purchase of, equipment, tangible personal property or real property and other Indebtedness for any purpose, provided that: (i) the aggregate amount incurred by the Obligated Group will not exceed at the time of incurrence 15% of the Adjusted Operating Revenues of the Obligated Group for the most recent Fiscal Year for which audited financial statements are available; and (ii) the aggregate of the Outstanding liabilities under capitalized leases and other Indebtedness for any purpose incurred under the Master Indenture, the Outstanding Long-Term Indebtedness and the Outstanding Short-Term Indebtedness incurred under the Master Indenture will not exceed at the time of incurrence 25% of the Adjusted Operating Revenues for the most recent Fiscal Year for which audited financial statements are available.

(k) Subordinated Indebtedness if, prior to the incurrence of any Subordinated Indebtedness, there is delivered to the Master Trustee (i) an Officer's Certificate, accompanied by the certificate of an Accountant confirming the contents thereof, certifying the Maximum Debt Service Coverage Ratio, taking into account all Outstanding Long-Term Indebtedness and the Subordinated Indebtedness then to be incurred, for the most recent Fiscal Year for which audited financial statements are available and that such Maximum Debt Service Coverage Ratio is not less than 1.10, and (ii) an opinion of counsel to the Obligated Group to the effect that the proposed Subordinated Indebtedness satisfies the requirements contained in the definition thereof.

(l) Commitment Indebtedness without limit.

Restrictions on Guarantees.

Each Member, respectively, covenants and agrees that it will not enter into or become liable in respect of any Guaranty after the date of execution and delivery of the Master Indenture, except:

(a) Guaranties of Indebtedness of another Obligated Group Member;

(b) Guaranties of Obligations issued under the Master Indenture; and

(c) Any other Guaranty, provided that the test for incurring Long-Term Indebtedness is met as if such Guaranty were Long-Term Indebtedness of the type represented by the obligation subject to the Guaranty with a principal amount equal to 100% of the obligation subject to such Guaranty.

Calculation of Debt Service; Debt Service Coverage; Annual Rate Covenant.

(a) The calculation of the amount of Indebtedness or Guaranties, the amortization schedule of such Indebtedness or Guaranties and the debt service payable with respect to such Indebtedness or Guaranties required under the Master Indenture will be made in a manner consistent with the provisions of the Master Indenture:

(i) In the case of Balloon Indebtedness, Put Indebtedness and Variable Rate Indebtedness:

(A) the total amount of principal and interest paid for any prior period will be calculated based on amounts scheduled to become due and to be paid in such prior period, in

accordance with the terms of such Indebtedness and the actual interest rate on such Indebtedness during such period, and in accordance with the definition of Annual Debt Service in the Master Indenture; and

(B) the total amount of principal and interest to be paid in any future period, including Maximum Annual Debt Service, will be calculated in accordance with the Master Indenture on the assumption that such Indebtedness is incurred on the date of such calculation.

(ii) In the case of a Guaranty under the Master Indenture on which the Member(s) providing the Guaranty has not been required under the terms of the Guaranty to make any payment on the obligation subject to the Guaranty in the two Fiscal Years prior to the date of calculation:

(A) the total amount of principal and interest paid for any prior period will be calculated as zero; and

(B) the total amount of principal and interest to be paid in any future period, including Maximum Annual Debt Service, will be calculated in accordance with the Master Indenture as if such Guaranty were Long-Term Indebtedness with an aggregate principal amount equal to 20% of the obligation subject to such Guaranty.

(iii) In the case of a Guaranty under the Master Indenture on which the Member(s) providing the Guaranty has been required under the terms of the Guaranty to make a payment in either of the two Fiscal Years prior to the date of calculation:

(A) the total amount of principal and interest paid for any prior period will be calculated based on amounts required to be paid by the Member(s) in such prior period, in accordance with the terms of such Indebtedness and the actual interest rate on such Indebtedness during such period, and in accordance with the definition of Annual Debt Service in the Master Indenture; and

(B) the total amount of principal and interest to be paid in any future period, including Maximum Annual Debt Service, will be calculated in accordance with the Master Indenture as if such Guaranty were Long-Term Indebtedness with an aggregate principal amount equal to 100% of the obligation subject to such Guaranty.

(b) (i) Within 150 days after the end of each Fiscal Year, the Obligated Group Representative will compute Income Available for Debt Service, Annual Debt Service, and the Debt Service Coverage Ratio for such Fiscal Year and will promptly furnish to the Master Trustee an Officer's Certificate setting forth the results of such computation. The Obligated Group Representative covenants and agrees that, if at the end of such Fiscal Year the Debt Service Coverage Ratio will have been less than 1.10:1.0, it will promptly employ a Management Consultant to make recommendations as to a revision of the methods of operation of the Members to increase the Debt Service Coverage Ratio to at least 1.10:1.0. Copies of a statement of the recommendations of the Management Consultant will be filed with the Master Trustee. Each Member will, promptly upon its receipt of such recommendations, subject to applicable requirements or restrictions imposed by law and contract, and subject to a good faith determination of the Governing Body of the Obligated Group Representative that implementation of such recommendations (in whole or in part) are in the best interests of the Obligated Group, revise its methods of operation and will take such other action as will be in conformity with such recommendations. If the Obligated Group Representative determines not to comply with such recommendations, it will file with the Master Trustee a certified copy of a resolution of its Governing Body determining not to so comply and stating in reasonable detail the reasons therefor.

If either (A) the Members comply in all material respects with the recommendations of the Management Consultant or (B) the Master Trustee receives a certified copy of a resolution of the Governing Body of the Obligated Group Representative determining not to comply with such recommendations and stating in reasonable detail the reasons therefor, the Members will be deemed to have complied with the covenants described under the Master Indenture for

such Fiscal Year and the next succeeding Fiscal Year notwithstanding that the Debt Service Coverage Ratio will be less than 1.25:1.0; provided that the Members will not be excused from taking any other action or performing any other duty required under the Master Indenture, including, without limitation, payment of all Required Payments.

(ii) In any event, the Obligated Group will maintain a Debt Service Coverage Ratio for any Fiscal Year of at least 1.0:1.0, calculated in accordance with and at the times required by the Master Indenture.

(iii) Notwithstanding the foregoing, a Member may permit the rendering of service at, or the use of, its facilities without charge or at reduced charges, at the discretion of the Governing Body of such Member, to the extent necessary for maintaining its tax exempt status and its eligibility for grants, loans, subsidies or payments from the United States of America, any instrumentality thereof, or any State or any political subdivision or instrumentality thereof, or in compliance with any recommendation for free services that may be made by a Management Consultant.

Sale, Lease or Other Disposition of Property.

Each Member, respectively, covenants and agrees that it will not, in any consecutive 12-month period, sell, lease, grant a lien, or otherwise dispose of any of the Property that, the value of which, together with all other Property transferred by Members during such 12-month period in transactions other than those described in the Master Indenture, totals for any consecutive 12-month period an amount in excess of 5% of the Property of the Obligated Group (calculated on the basis of the greater of the Current Value or the Book Value of the assets as shown on the most recent Obligated Group Financial Statements), except for transfers of Property:

(a) To any Person if prior to such sale, lease or other disposition, the Master Trustee receives an Officer's Certificate to the effect that such assets will be or within the next two (2) Fiscal Years are reasonably expected to become inadequate, obsolete, unsuitable, undesirable or unnecessary for the operation and functioning of the primary business of the Obligated Group;

(b) To another Member;

(c) In the ordinary course of business, or for the fair market value of the Property so disposed of, or for fair market rent in the case of property leased, or in return for other Property of equal or greater value and usefulness;

(d) To a Person that is not a Member if such Person will become a Member pursuant to the Master Indenture substantially simultaneously with such sale, lease or other disposition;

(e) To any Person, if such Property consists solely of assets that are specifically restricted by the donor or grantor to a particular purpose which is inconsistent with their use for payment of an Obligation or Long-Term Indebtedness or operating expenses; or

(f) The Master Trustee will have received an Officer's Certificate to the effect that the Obligated Group would, immediately after such sale, lease or other disposition and taking into account such sale, lease or other disposition as if it had occurred on the first day of the full Fiscal Year preceding the date of such Officer's Certificate, be able to incur \$1.00 of Long-Term Indebtedness pursuant to the Master Indenture.

Consolidation, Merger, Acquisition, Sale or Conveyance.

Each Member, respectively, covenants that it will not consolidate or merge with any other corporation not a Member or acquire substantially all of the assets of a Person not a Member or sell or convey all or substantially all of its assets to any Person not a Member unless:

(a) After giving effect to the consolidation, merger, acquisition, sale or conveyance, the successor or Surviving Corporation will be a Member, or, if not, the Surviving Corporation will be a corporation organized and

existing under the laws of the United States of America or a State thereof and such Surviving Corporation will become a Member and will expressly assume in writing the due and punctual payment of all Required Payments of the disappearing corporation under the Master Indenture, according to their tenor, and the due and punctual performance and observance of all of the covenants and conditions of the Master Indenture by the execution of a Related Supplement satisfactory to the Master Trustee, delivered to the Master Trustee by such Surviving Corporation;

(b) There will have been delivered to the Master Trustee an Officer's Certificate to the effect that no Member, immediately after the date of the proposed consolidation, merger, acquisition, sale or conveyance, would be in default as a result of such consolidation, merger, acquisition, sale or conveyance in the performance or observance of any covenant or condition of the Master Indenture;

(c) So long as any Related Bonds which are tax-exempt obligations are Outstanding, there will have been delivered to the Master Trustee an Opinion of Bond Counsel, in form and substance satisfactory to the Master Trustee, to the effect that, under then existing law, the consummation of such consolidation, merger, acquisition, sale or conveyance, in and of itself, would not cause interest payable thereon to be includable in gross income for federal income tax purposes and that such consolidation, merger, acquisition, sale or conveyance, and the assumption of rights and obligations thereafter, complies with the provisions of the Master Indenture;

(d) The Master Trustee will have received an Opinion of Counsel, in form and substance satisfactory to the Master Trustee, to the effect that (i) all conditions in the Master Indenture relating to such merger, consolidation, sale or conveyance have been complied with and it is proper for the Master Trustee to join in the execution of any instrument required to be executed and delivered; (ii) the Surviving Corporation meets the conditions set forth in the Master Indenture and is liable on all Master Indenture Obligations then Outstanding; and (iii) such merger, consolidation, sale or conveyance will not cause the Master Indenture or any Obligations to be subject to registration under federal or state securities laws or the Trust Indenture Act of 1939, as amended (or, that any such registration, if required, has occurred); and

(e) The Master Trustee will have received an Officer's Certificate to the effect that the Obligated Group would, immediately after such consolidation, merger, acquisition, sale or conveyance and taking into account such consolidation, merger, acquisition, sale or conveyance as if it had occurred on the first day of the full Fiscal Year preceding the date of such Officer's Certificate be able to incur \$1.00 of Long-Term Indebtedness pursuant to the Master Indenture.

In case of any such consolidation, merger, acquisition, sale or conveyance, and upon such assumption of obligations, the Surviving Corporation will be substituted for its predecessor in interest in all agreements, indentures, and Obligations then in effect, and the Surviving Corporation will, upon the request of the Master Trustee, execute and deliver to the Master Trustee such documents and endorsements as will be necessary in order to effect said substitution. From and after the effective date of such substitution as determined by the Master Trustee, the Surviving Corporation will, subject to the terms, conditions and limitations prescribed in the Master Indenture, be treated as though it were a Member at the date of the execution of the Master Indenture and will thereafter have the right to participate in transactions permitted under the Master Indenture to the same extent as the Members; and all transactions undertaken on behalf of a Surviving Corporation in all respects have the same legal rank and benefit under the Master Indenture as though undertaken by the Obligated Group in the absence of such consolidation, merger, sale or conveyance.

Membership in Obligated Group.

Additional Members may be added to the Obligated Group from time to time provided that:

(a) There will have been delivered to the Master Trustee a copy of a resolution of the proposed new Member which authorizes the execution of the Related Supplement referred to below and authorizes compliance with the terms of the Master Indenture;

(b) There will have been delivered to the Master Trustee a Related Supplement pursuant to which the proposed new Member agrees to become a Member, to be bound by the terms and restrictions imposed by the Master Indenture, and to be bound by Indebtedness represented by the Obligations;

(c) There will have been delivered to the Master Trustee an irrevocable power of attorney of the proposed new Member authorizing the execution of Obligations by the Obligated Group Representative;

(d) There will be delivered to the Master Trustee a written Opinion of Counsel to the proposed new Member, which opinion states that (i) the proposed new Member has taken all necessary action to become a Member, (ii) upon execution of a Related Supplement, the Master Indenture will constitute a valid and binding obligation of the proposed new Member enforceable in accordance with its terms, (iii) upon execution of a Related Supplement, such proposed new Member will be bound by the terms of the Master Indenture and (iv) the addition of such Member will not cause the Master Indenture or any Obligations to be subject to registration under federal or state securities laws or the Trust Indenture Act of 1939, as amended (or, that any such registration, if required, has occurred);

(e) There will be delivered to the Master Trustee a description of any existing Long-Term Indebtedness of the proposed new Member and a description of any Indebtedness which the proposed new Member plans to incur simultaneously with the execution of the Related Supplement;

(f) The Master Trustee will have received an Officer's Certificate to the effect that the Obligated Group would, immediately after the addition of the new Member to the Obligated Group and taking into account such addition as if it had occurred on the first day of the full Fiscal Year preceding the date of such Officer's Certificate be able to incur \$1.00 of Long-Term Indebtedness pursuant to the Master Indenture;

(g) There will have been delivered to the Master Trustee an Officer's Certificate to the effect that no Member, immediately after the addition of such new Member, would be in default in the performance or observance of any covenant or condition of the Master Indenture; and

(h) There will be delivered to the Master Trustee an Opinion of Bond Counsel to the effect that the addition of such Member will not, in and of itself, cause interest payable on any Related Bonds which are tax-exempt obligations to be includable in gross income for federal income tax purposes, nor cause the Master Indenture nor the Obligations issued under the Master Indenture to be subject to registration under federal securities laws (unless such registration, if required, has occurred) nor subject to qualification under the Trust Indenture Act of 1939, as amended, (unless such qualification, if required, has occurred).

Withdrawal from Obligated Group.

Neither the Corporation nor the Foundation may withdraw from the Obligated Group. Any other Member may withdraw from the Obligated Group and be released from further liability or obligation under the provisions of the Master Indenture, provided that:

(a) The Master Trustee will have received an Officer's Certificate to the effect that, immediately following withdrawal of such Member, no Member would be in default in the performance or observance of any covenant or condition of the Master Indenture;

(b) The Master Trustee will have received an Officer's Certificate to the effect that immediately after the withdrawal of such Member from the Obligated Group and taking into account such withdrawal as if it had occurred on the first day of the full Fiscal Year preceding the date of such Officer's Certificate, the Obligated Group would be able to incur \$1.00 of Long-Term Indebtedness pursuant to the Master Indenture; and

(c) The Master Trustee will have received an Opinion of Bond Counsel to the effect that the withdrawal of such Member will not cause the interest payable on any Related Bonds which are tax-exempt obligations to be includable in gross income for federal income tax purposes, nor cause the Master Indenture nor the Obligation issued under the Master Indenture to be subject to registration under federal securities laws (unless such

registration, if required, has occurred) nor subject to qualification under the Trust Indenture Act of 1939, as amended (unless such qualification, if required, has occurred).

Filing of Financial Statements, Reports and Other Information.

(a) Each Member covenants that it will keep adequate records and books of accounts in which complete and correct entries will be made (said books will be subject to the inspection of the Master Trustee during regular business hours after reasonable notice).

(b) The Obligated Group Representative covenants that it will furnish to the Master Trustee and any Related Bond Issuer that will request the same in writing:

(i) As soon as practicable, but in no event more than six months after the last day of each Fiscal Year beginning with the Fiscal Year ending December 31, 2006, one or more financial statements which, in the aggregate, will include the Material Members. Such financial statements: (A) may consist of financial statements reporting the financial results of Persons for disparate fiscal years; (B) may consist of (1) consolidated or combined financial results including one or more Members and one or more other Persons required to be consolidated or combined with such Member(s) under generally accepted accounting principles or (2) special purpose financial statements including only Members; (C) will be audited by a firm of nationally recognized independent certified public accountants approved by the Obligated Group Representative as having been prepared in accordance with generally accepted accounting principles (except, in the case of special purpose financial statements, for required consolidations); (D) will include a balance sheet, statement of operations and changes in net assets; and (E) if more than one financial statement is delivered to the Master Trustee pursuant to the Master Indenture, each such financial statement will contain, as "other financial information," a combining or consolidating schedule from which financial information solely relating to the Members may be derived.

(ii) At the time of the delivery of the Obligated Group Financial Statements, a certificate of the chief financial officer of the Obligated Group Representative stating that (A) the Obligated Group Financial Statements were prepared in accordance with generally accepted accounting principles (except for the inclusion of Members that are not permitted to be consolidated in accordance with generally accepted accounting principles and the exclusion of entities that are not Members that are required to be consolidated in accordance with generally accepted accounting principles), (B), subject to the following paragraphs, the Obligated Group Financial Statements reflect the results of the operations of only Members, (C) the Obligated Group Financial Statements reflect the results of the operations of the Material Members, and (D) the combined net assets of the Material Members for which financial statements have been delivered to the Master Trustee and that are included in the Obligated Group Financial Statements are equal to or greater than 90% of the combined or consolidated net assets of the Obligated Group for the most recently completed Fiscal Year of the Obligated Group.

(iii) At the time of the delivery of the Obligated Group Financial Statements, a certificate of the chief financial officer of the Obligated Group Representative, stating that the Obligated Group Representative has made a review of the activities of the Material Members during the preceding Fiscal Year for the purpose of determining whether or not the Material Members have complied with all of the terms, provisions and conditions of the Master Indenture and that each Material Member has kept, observed, performed and fulfilled each and every covenant, provision and condition of the Master Indenture on its part to be performed and none of such Material Members is in default in the performance or observance of any of the terms, covenants, provisions or conditions, or if any Material Member will be in default such certificate will specify all such defaults and the nature thereof.

(iv) Notwithstanding the foregoing, the results of operation and financial position of Immaterial Affiliates need not be excluded from financial statements delivered to the Master Trustee pursuant to the Master Indenture, and such results of operation and financial position may be considered as if they were a portion of the results of operation and financial position of the Material Members for all purposes of the Master Indenture notwithstanding the inclusion of the results of operation and financial position of such Immaterial Affiliates.

Gross Revenue Account.

(a) Each Member agrees that, as long as any of the Obligations remain Outstanding, all of the Gross Revenues will be deposited as soon as practicable upon receipt in a deposit account or securities account designated as the Gross Revenue Accounts which the Obligated Group Representative will establish and maintain, subject to the provisions of the Master Indenture, at such banking institution as the Obligated Group Representative will from time to time designate, in writing, for such purpose and which has entered into an Account Control Agreement with the Members of the Obligated Group and the Master Trustee. As security for the payment of Required Payments and the performance by each of the Members of its other obligations under the Master Indenture, each Member pledges and assigns to the Master Trustee, and grants to the Master Trustee a security interest in, all its right, title and interest, whether now owned or hereafter acquired, in and to all Collateral, including the Gross Revenues and the Gross Revenue Accounts. Each of the Members will execute the Account Control Agreement, will execute and cause to be filed Uniform Commercial Code financing statements, and will execute and deliver such other documents (including, but not limited to, amendments to such Uniform Commercial Code financing statements) as may be necessary or reasonably requested by the Master Trustee in order to perfect or maintain the perfection of such security interest. Each Member irrevocably authorizes the Master Trustee to execute and file any financing statements and amendments thereto as may be required to perfect or to continue the perfection of the security interest in the Collateral. Each Member also ratifies its authorization for the Master Trustee to have filed in any jurisdiction any like financing statements or amendments thereto if filed prior to the date of the Master Indenture. Each Member represents and warrants that it is a nonprofit public benefit corporation organized solely under the laws of the State of California and that its complete legal name is as set forth on the signature page of the Master Indenture or Related Supplement, as applicable, executed by such Member. Each Member covenants that it will not change its name or its type or jurisdiction of organization unless (i) it gives 30 days' notice of such change to the Master Trustee and (ii) before such change occurs it takes all actions as are necessary or advisable to maintain and continue the first priority perfected security interest of the Master Trustee in the Collateral.

(b) Gross Revenues and amounts in the Gross Revenue Accounts may be used and withdrawn by each Member at any time for any lawful purpose, except as otherwise provided in the Master Indenture. If an Event of Default has occurred and is then continuing, the Master Trustee will notify the Obligated Group Representative of such delinquency, and will be entitled to deliver an Order (as such term is defined in the Account Control Agreement) to each Depository Bank. Upon delivery of an Order with respect to the Gross Revenue Accounts, exclusive control over the Gross Revenue Accounts will be exercised by the Master Trustee as provided in the Account Control Agreement. All Gross Revenues will continue to be deposited in the Gross Revenue Accounts as described above and the Master Trustee will continue to exercise exclusive control over the Gross Revenue Accounts until the amounts on deposit in said account are sufficient to pay in full (or have been used to pay in full) all Required Payments in default and until all other then-existing Events of Default known to the Master Trustee will have been made good or cured to the satisfaction of the Master Trustee or provision deemed by the Master Trustee to be adequate will have been made therefor. During any period that the Gross Revenue Accounts are subject to the exclusive control of the Master Trustee, the Master Trustee will use and withdraw from time to time amounts in said fund, to make Required Payments as such payments become due (whether by maturity, prepayment, redemption, acceleration or otherwise), and, if such amounts will not be sufficient to pay in full all such payments due on any date, then to the payment of debt service on Obligations, ratably, without any discrimination or preference, and to such other payments in the order which the Master Trustee, in its discretion, will determine to be in the best interests of the Holders of the Obligations, without discrimination or preference. During any period that the Gross Revenue Accounts are subject to the exclusive control of the Master Trustee, no Member will be entitled to use or withdraw any of the Gross Revenues unless (and then only to the extent that) the Master Trustee in its sole discretion so directs for the payment of current or past due operating expenses of such Member; provided, however, that Members may submit requests to the Master Trustee as to which expenses to pay and in which order. Each Member agrees to execute and deliver all instruments as may be required. Each Member further agrees that a failure to comply with the terms of the Master Indenture will cause irreparable harm to the Master Trustee from time to time of the Obligations, and will entitle the Master Trustee, with or without notice to the Obligated Group Representative, to take immediate action to compel the specific performance of the obligations of each of the Members as provided in the Master Indenture.

(c) Upon receipt of Gross Revenues, each Member covenants and agrees: (i) to deposit in all Gross Revenues in the Gross Revenue Accounts and not in any other fund or account; (ii) that the Gross Revenue

Accounts will be held as a deposit or securities account at the Depository Bank; and (iii) that the Gross Revenue Accounts will not be moved from the Depository Bank without the prior written consent of the Master Trustee, which consent will not be unreasonably withheld.

Liquidity Covenant.

If as of any June 30 or December 31, the Obligated Group does not have Liquid Unencumbered Assets in an amount at least equal to 75 Days' Operating Expenses, the Obligated Group will, at its expense, retain a Management Consultant to make recommendations (within 60 days of the date of the calculation which indicated that the required amount had not been maintained) to increase Liquid Unencumbered Assets to an amount at least equal to 75 Days' Operating Expenses. The Management Consultant's report will be delivered to the Master Trustee. The Master Trustee will be entitled to consult with the Management Consultant, attend the Management Consultant's briefings with management of the Obligated Group and receive all written reports of the Management Consultant. Each Member will, promptly upon its receipt of such recommendations, subject to applicable requirements or restrictions imposed by law and contract and subject to a good faith determination of the Governing Body of the Obligated Group Representative that implementation of such recommendations (in whole or in part) are in the best interests of the Obligated Group, revise its methods of operation and will take such other action as will be in conformity with such recommendations. If the Obligated Group Representative determines not to comply with such recommendations, it will file with the Master Trustee a certified copy of a resolution of its Governing Body determining not to so comply and stating in reasonable detail the reasons therefor.

In any event, the Obligated Group will maintain Liquid Unencumbered Assets in an amount at least equal to 50 Days' Operating Expenses, calculated in accordance with and at the times required by the Master Indenture.

The Obligated Group Representative will deliver to the Master Trustee an Officer's Certificate containing a calculation of Liquid Unencumbered Assets and Days' Operating Expenses for: (a) each June 30, not later than 60 days after each June 30, calculated on the basis of unaudited financial statements for the six-month period ended on such date; and (b) each December 31, not later than five months after the end of such Fiscal Year, calculated on the basis of the audited financial statements for the Fiscal Year ended as of such December 31.

Defaults

Events of Default.

Event of Default means any of the following events:

(a) Failure on the part of the Obligated Group to make due and punctual payment of any Required Payment on an Obligation;

(b) Any Member will default in the payment of any Indebtedness (other than Non-Recourse Indebtedness or an Obligation) with an aggregate principal amount then Outstanding in excess of 5% of unrestricted net assets of the Obligated Group for the most recent Fiscal Year for which Obligated Group Financial Statements are available, whether such Indebtedness now exists or will hereafter be created, and any period of grace with respect thereto will have expired, or an event of default as defined in any mortgage, indenture or instrument under which there may be secured or evidenced any Indebtedness, whether such Indebtedness now exists or will hereafter be created, will occur and any period of grace with respect thereto will have expired; provided, however, that such default will not constitute an Event of Default within the meaning of the Master Indenture if within 30 days, or within the time allowed for service of a responsive pleading if any proceeding to enforce payment of the Indebtedness is commenced (i) any Member in good faith commences proceedings to contest the existence or payment of such Indebtedness, and (ii) sufficient moneys are escrowed with a bank or trust company or a bond not objected to by the Master Trustee is posted for the payment of such Indebtedness;

(c) Any Member will fail duly to observe or perform any other covenant or agreement under the Master Indenture for a period of 30 days after the date on which written notice of such failure, requiring the same to be remedied, will have been given to the Obligated Group Representative by the Master Trustee or to the Obligated

Group Representative and the Master Trustee by the Holders of 25% in aggregate principal amount of Outstanding Obligations except that, if such failure can be remedied but not within such 30 day period, such failure will not become an Event of Default for so long as the Obligated Group Representative will diligently proceed to remedy same in accordance with and subject to any directions or limitations of time established by the Master Trustee;

(d) A court having jurisdiction will enter a decree or order for relief in respect of any Member in an involuntary case under any applicable federal or state bankruptcy, insolvency or other similar law now or hereafter in effect, or appointing a receiver, liquidator, assignee, custodian, trustee, sequestrator (or similar official) of any Member or for any substantial part of the property of any Member, or ordering the winding up or liquidation of its affairs, and such decree or order will remain unstayed and in effect for a period of 60 consecutive days;

(e) Any Member will commence a voluntary case under any applicable federal or state bankruptcy, insolvency or other similar law now or hereafter in effect, or will consent to the entry of an order for relief in an involuntary case under any such law, or will consent to the appointment of or taking possession by a receiver, liquidator, assignee, trustee, custodian, sequestrator (or similar official) of any Member or for any substantial part of its property, or will make any general assignment for the benefit of creditors, or will fail generally to pay its debts as they become due or will take any corporate action in furtherance of the foregoing; or

(f) An event of default will exist under any Related Bond Indenture.

Acceleration; Annulment of Acceleration.

(a) Upon the occurrence and during the continuation of an Event of Default under the Master Indenture, the Master Trustee may, and upon (i) the written request of the Holders of not less than 25% in aggregate principal amount of Outstanding Obligations or of any Holder if an Event of Default has occurred or (ii) the acceleration of any Obligation pursuant to the terms of the Related Supplement under which such Obligation was issued, the Master Trustee will, by notice to the Members, declare all Outstanding Obligations immediately due and payable. In such event, there will be due and payable on the Obligations an amount equal to the aggregate principal amount of all such Obligations, plus all interest accrued thereon and, to the extent permitted by applicable law, interest which accrues on such principal and interest to the date of payment.

(b) At any time after all Obligations will have been so declared to be due and payable and before the entry of final judgment or decree in any suit, action or proceeding instituted on account of such default, if (i) the Obligated Group has paid or caused to be paid or deposited with the Master Trustee moneys sufficient to pay all matured installments of interest and interest on installments of principal and interest and principal or redemption prices and other payments then due (other than the principal or other payments then due only because of such declaration) of all Outstanding Obligations, (ii) the Obligated Group has paid or caused to be paid or deposited with the Master Trustee moneys sufficient to pay the charges, compensation, expenses, disbursements, advances and liabilities of the Master Trustee and any paying agents, (iii) all other amounts then payable by the Obligated Group under the Master Indenture will have been paid or a sum sufficient to pay the same will have been deposited with the Master Trustee, and (iv) every Event of Default (other than a default in the payment of the principal or other payments of such Obligations then due only because of such declaration) will have been remedied, then the Master Trustee may annul such declaration and its consequences with respect to any Obligations or portions thereof not then due by their terms. No such annulment will extend to or affect any subsequent Event of Default or impair any right consequent thereon.

Additional Remedies and Enforcement of Remedies.

(a) Upon the occurrence and continuance of any Event of Default, the Master Trustee may, and upon the written request of the Holders of not less than 25% in aggregate principal amount of the Obligations Outstanding or of any Holder if an Event of Default has occurred, upon being indemnified to its satisfaction therefor, will, proceed forthwith to protect and enforce its rights and the rights of the Holders under the Master Indenture by such suits, actions or proceedings as the Master Trustee, being advised by counsel, will deem expedient, including but not limited to:

- (i) Enforcement of the right of the Holders to collect and enforce the payment of amounts due or becoming due under the Obligations;
- (ii) Suit upon all or any part of the Obligations;
- (iii) Civil action to require any person holding moneys, documents or other property pledged to secure payment of amounts due or to become due on the Obligations to account as if it were the trustee of an express trust for the Holders of Obligations;
- (iv) Civil action to enjoin any acts or things which may be unlawful or in violation of the rights of the Holders of Obligations; and
- (v) Enforcement of any other right or remedy of the Holders conferred by law or by the Master Indenture.

(b) Regardless of the happening of an Event of Default, the Master Trustee, if requested in writing by the Holders of not less than 25% in aggregate principal amount of the Obligations then Outstanding, will, upon being indemnified to its satisfaction therefor, institute and maintain such suits and proceedings as it may be advised will be necessary or expedient (i) to prevent any impairment of the security given under the Master Indenture by any acts which may be unlawful or in violation of the Master Indenture, or (ii) to preserve or protect the interests of the Holders, provided that such request and the action to be taken by the Master Trustee are not in conflict with any applicable law or the provisions of the Master Indenture and, in the sole judgment of the Master Trustee, not unduly prejudicial to the interest of the Holders of Obligations not making such request.

Application of Moneys After Default.

During the continuance of an Event of Default, all moneys received by the Master Trustee pursuant to any right given or action taken under the provisions of the Master Indenture, after payment of any expenses necessary in the opinion of the Master Trustee to protect the interests of the Holders of the Obligations and payment of reasonable charges and expenses of the Master Trustee (including reasonable fees and disbursements of its counsel) incurred in and about the performance of its powers and duties under the Master Indenture, will be applied as follows:

- (a) Unless all Outstanding Obligations will have become or have been declared due and payable:

First: To the payment to the Persons entitled thereto of all installments of interest and, in the case of Financial Products Agreements, regularly scheduled payments then due on the Obligations in the order of the maturity or payment date of such installments, and, if the amount available will not be sufficient to pay in full any installment, installments, payment or payments maturing or coming due on the same date, then to the payment thereof ratably, according to the amounts due thereon to the Persons entitled thereto, without any discrimination or preference; and

Second: To the payment to the Persons entitled thereto of the unpaid principal installments, termination and other payments (in the case of Financial Products Agreements), and any other Required Payments of any Obligations that will have become due, whether at maturity or by call for redemption, in the order of their due dates, and, if the amounts available will not be sufficient to pay in full all the principal installments, termination and other payments and other Required Payments due on any date, then to the payment thereof ratably, according to the amounts of such installments or other payments due on such date, to the Persons entitled thereto, without any discrimination or preference.

(b) If all Outstanding Obligations will have become or have been declared due and payable, to the payment of the principal and interest and other Required Payments then due and unpaid upon the Obligations without preference or priority of any installment or payment over any other installment or payment, or of any Obligation over any other Obligation, ratably, according to the amounts due, to the Persons entitled thereto, without any discrimination or preference.

(c) If all Outstanding Obligations will have been declared due and payable, and if such declaration will thereafter be rescinded and annulled under the provisions of the Master Indenture, then, subject to the provisions of the Master Indenture in the event that the principal of all Outstanding Obligations will later become due or be declared due and payable, the moneys will be applied in accordance with the provisions of the Master Indenture.

Whenever moneys are to be applied by the Master Trustee pursuant to the provisions of the Master Indenture, such moneys will be applied by it at such times, and from time to time, as the Master Trustee will determine, having due regard for the amount of such moneys available for application and the likelihood of additional moneys becoming available for such application in the future. Whenever the Master Trustee will apply such moneys, it will fix the date upon which such application is to be made and upon such date interest on the amounts of principal to be paid on such dates will cease to accrue. The Master Trustee will give such notices as it may deem appropriate of the deposit with it of any such moneys and of the fixing of any such date, and will not be required to make payment to the Holder of any unpaid coupon or Obligation until such coupon or such Obligation and all unmatured coupons, if any, appertaining to such Obligation will be presented to the Master Trustee for appropriate endorsement of any partial payment or for cancellation if fully paid.

Whenever all Obligations and interest thereon have been paid under the provisions of the Master Indenture and all expenses and charges of the Master Trustee have been paid, any balance remaining will be paid to the Person entitled to receive the same; if no other Person will be entitled thereto, then the balance will be paid to the Members, their successors, or as a court of competent jurisdiction may direct.

Holders' Control of Proceedings.

If an Event of Default will have occurred and be continuing, notwithstanding anything in the Master Indenture to the contrary, the Holders of at least a majority in aggregate principal amount of Obligations then Outstanding will have the right, at any time, by any instrument in writing executed and delivered to the Master Trustee, to direct the method and place of conducting any proceeding to be taken in connection with the enforcement of the terms and conditions of the Master Indenture or for the appointment of a receiver or any other proceedings under the Master Indenture, provided that such direction is not in conflict with any applicable law or the provisions of the Master Indenture (including indemnity to the Master Trustee) and, in the sole judgment of the Master Trustee, is not unduly prejudicial to the interest of Holders not joining in such direction and provided further that nothing in the Master Indenture will impair the right of the Master Trustee in its discretion to take any other action under the Master Indenture that it may deem proper and that is not inconsistent with such direction by Holders which it may deem proper and which is not inconsistent with such direction by Holders.

Waiver of Event of Default.

(a) No delay or omission of the Master Trustee or of any Holder of the Obligations to exercise any right or power accruing upon any Event of Default will impair any such right or power or will be construed to be a waiver of any such Event of Default or an acquiescence therein. Every power and remedy given by the Master Indenture to the Master Trustee and the Holders of the Obligations, respectively, may be exercised from time to time and as often as may be deemed expedient by them.

(b) The Master Trustee may waive any Event of Default which in its opinion will have been remedied before the entry of final judgment or decree in any suit, action or proceeding instituted by it under the provisions of the Master Indenture, or before the completion of the enforcement of any other remedy under the Master Indenture.

(c) The Master Trustee, upon the written request of the Holders of at least a majority of the aggregate principal amount of Obligations then Outstanding, will waive any Event of Default under the Master Indenture and its consequences; provided, however, that, except under the circumstances set forth in the Master Indenture, a default in the payment of the principal of, premium, if any, or interest on or other payment with respect to any Obligation, when the same will become due and payable by the terms thereof or upon call for redemption, may not be waived without the written consent of the Holders of all the Obligations at the time Outstanding.

(d) In case of any waiver by the Master Trustee of an Event of Default under the Master Indenture, the Members, the Master Trustee and the Holders will be restored to their former positions and rights under the Master Indenture, respectively, but no such waiver will extend to any subsequent or other Event of Default or impair any right consequent thereon.

Supplements and Amendments

Supplements Not Requiring Consent of Holders.

The Obligated Group Representative, acting for itself and as agent for each Member, and the Master Trustee may, without the consent of or notice to any of the Holders, enter into one or more Related Supplements for one or more of the following purposes:

- (a) To cure any ambiguity or formal defect or omission in the Master Indenture;
- (b) To correct or supplement any provision in the Master Indenture which may be inconsistent with any other provision within the Master Indenture, or to make any other provisions with respect to matters or questions arising under the Master Indenture and which will not materially and adversely affect the interests of the Holders;
- (c) To grant or confer ratably upon all of the Holders any additional rights, remedies, powers or authority, or to add to the covenants of and restrictions on the Members;
- (d) To qualify the Master Indenture under the Trust Indenture Act of 1939, as amended, or corresponding provisions of federal laws from time to time in effect;
- (e) To create and provide for the issuance of an Obligation or Series of Obligations as permitted under the Master Indenture;
- (f) To obligate a successor to any Member as provided in the Master Indenture; or
- (g) To add a new Member as provided in the Master Indenture; or
- (h) To make any other change that does not materially adversely affect the interests of the Holders of any Obligation.

Supplements Requiring Consent of Holders.

(a) Other than Related Supplements and subject to the terms and provisions and limitations contained in the Master Indenture and not otherwise, the Holders of not less than a majority in aggregate principal amount of the Obligations then Outstanding will have the right, from time to time, to consent to and approve the execution, by the Master Trustee and by the Obligated Group Representative, acting for itself and as agent for each Member (provided that each Member will have received written notice not less than fifteen (15) days prior to execution), of such Related Supplements as will be deemed necessary and desirable for the purpose of modifying, altering, amending, adding to or rescinding, in any particular, any of the terms or provisions contained in the Master Indenture; provided, however, that nothing in the Master Indenture will permit or be construed as permitting a Related Supplement which would:

- (i) Extend the stated maturity of or time for paying interest on any Obligation or reduce the principal amount of or the redemption premium or rate of interest or method of calculating interest payable on any Obligation, without the consent of the Holder of such Obligation;
- (ii) Modify, alter, amend, add to or rescind any of the terms or provisions contained in the Master Indenture so as to affect the right of the Holders of any Obligations in default as to payment to compel the Master Trustee to declare the principal of all Obligations to be due and payable, without the consent of the Holders of all Obligations then Outstanding; or

(iii) Reduce the aggregate principal amount of Obligations then Outstanding the consent of the Holders of which is required to authorize such Related Supplement, without the consent of the Holders of all Obligations then Outstanding.

Satisfaction and Discharge of Master Indenture

If (i) the Members will deliver to the Master Trustee for cancellation all Obligations theretofore authenticated (other than any Obligations which will have been mutilated, destroyed, lost or stolen and which will have been replaced or paid as provided in any Related Supplement) and not theretofore cancelled, or (ii) upon payment of all Obligations not theretofore cancelled or delivered to the Master Trustee for cancellation which have become due and payable, or (iii) the Members or any Person on behalf thereof will deposit with the Master Trustee (or with a bank or trust company pursuant to an agreement between a Member and such bank or trust company) as trust funds the amount of cash or Governmental Obligations or both, sufficient to pay at maturity or upon redemption all Obligations not theretofore cancelled or delivered to the Master Trustee for cancellation, including principal, interest and other Required Payments due or to become due to such date of maturity or redemption date, as the case may be, such sufficiency to be evidenced by a report of an Accountant, and, if in any case the Members will also pay or cause to be paid all other sums payable under the Master Indenture by the Members, then the Master Indenture will cease to be of further effect, and the Master Trustee, on demand of the Members and at the cost and expense of the Members, will execute proper instruments acknowledging satisfaction of and discharging the Master Indenture. Each Member, respectively, agrees to reimburse the Master Trustee for any costs or expenses theretofore and thereafter reasonably and properly incurred by the Master Trustee in connection with the Master Indenture or such Obligations.

FIRST SUPPLEMENTAL MASTER INDENTURE

General

Supplement No. 1 provides for the issuance of Obligation No. 1 pursuant to the Master Indenture, and proves the terms and form thereof.

Payments on Obligation No. 1; Credits.

(a) Principal of and interest and any applicable redemption premium on Obligation No. 1 is payable in any coin or currency of the United States of America which, on the respective dates of payment of such principal and interest, is legal tender for the payment of public and private debts. Except as provided in Supplement No. 1, payments of the principal of and premium, if any, and interest on Obligation No. 1 and any other payments required to be made with respect to Obligation No. 1 will be made at the times and in the amounts specified in Obligation No. 1 by the Obligated Group depositing the same in immediately available funds with or to the account of the Trustee on or before 10:00 a.m., California time, on the day such payments will become due or payable and giving notice to the Master Trustee and the Trustee of each payment of principal, interest or premium on Obligation No. 1, specifying the amount paid and identifying such payment as a payment on Obligation No. 1.

(b) The Corporation will receive credit for payments on Obligation No. 1, in addition to any credits resulting from payment or prepayment from other sources, as follows: (i) On installments of interest on Obligation No. 1 in an amount equal to moneys deposited in the Interest Fund created under the Indenture, which amounts are available to pay interest on the Bonds and to the extent such amounts have not previously been credited against payments on Obligation No. 1; (ii) On installments of principal on Obligation No. 1 in an amount equal to moneys deposited in the Principal Fund, the Sinking Fund and the Redemption Fund created under the Indenture, which amounts are available to pay principal of the Bonds and to the extent such amounts have not previously been credited against payments on Obligation No. 1; (iii) On installments of principal and interest, respectively, on Obligation No. 1 in an amount equal to the principal amount of Bonds and the interest thereon for which sufficient amounts (as determined by the Bond Indenture) in money or United States Government Obligations (as defined in the Indenture) have been irrevocably deposited with the Trustee in an amount sufficient to pay the principal of, premium, if any, and interest thereon when due to the extent such amounts have not been previously credited against payments on Obligation No. 1; such credits will be made against the installments of principal of and interest on Obligation No. 1 which would have been used, but for such deposit, to pay principal of and interest, on such Bonds

when due at maturity or called for mandatory redemption; and (iv) On installments of principal and interest, respectively, on Obligation No. 1 in an amount equal to the principal amount of Bonds acquired by the Corporation and surrendered to the Trustee for cancellation or purchased by the Trustee and cancelled and the interest on such Bonds from and after the date interest thereon has been paid prior to cancellation. Such credits will be made against the installments of principal of and interest on Obligation No. 1 which would have been used, but for such cancellation, to pay principal of and interest on such Bonds when due.

Prepayment of Obligation No. 1.

So long as all amounts which have become due under Obligation No. 1 have been paid, the Corporation will have the right, at any time and from time to time, to prepay all or any part of the amounts to become due and payable under Obligation No. 1 and the Authority agrees that the Trustee will accept such prepayments when the same are tendered by the Corporation. Prepayments may be made by payments of cash, deposits of Investment Securities, or surrender of Bonds, as contemplated by Supplement No. 1. All such prepayments (and the additional payment of any amount necessary to pay the applicable premium, if any, payable upon the redemption of Bonds) will be deposited upon receipt in the Optional Redemption Account of the Redemption Fund (or the Special Redemption Account of the Redemption Fund if the Bonds are to be redeemed under the circumstances described in the Bond Indenture) and, at the request of and as determined by the Corporation, credited against payments due under Obligation No. 1 or used for the redemption or purchase of Outstanding Bonds in the manner and subject to the terms and conditions set forth in the Indenture. The Corporation will have the right to surrender Bonds acquired by it in any manner whatsoever to the Trustee for cancellation, and such Bonds, upon such surrender and cancellation, will be deemed to be paid and retired, and the principal amount thereof will be applied as set forth in the Bond Indenture. Notwithstanding any such prepayment or surrender of Bonds, as long as any Bonds remain Outstanding or any additional payments required to be made under the Loan Agreement remain unpaid, the Corporation will not be relieved of its obligations under Supplement No. 1.

Registration, Number, Negotiability and Transfer of Obligation No. 1.

Except as provided in the following paragraph, so long as any Bond remains Outstanding (as that term is defined in the Indenture), Obligation No. 1 will be issuable only as a single Obligation without coupons registered in the name of the Trustee on behalf of the Authority and no transfer of Obligation No. 1 will be registered under Supplement No. 1 or be recognized by the Corporation except for transfers to a successor Trustee.

Upon the principal of all Obligations issued under the Master Indenture Outstanding being declared immediately due and payable and during the continuance of an Event of Default, Obligation No. 1 may be transferred and such transfer registered if and to the extent the Trustee requests that the restrictions of Supplement No. 1 on transfers be terminated.

Right to Redeem Obligation No. 1.

Obligation No. 1 will be subject to redemption, in whole or in part, prior to maturity at the times and in the amounts specified in the Bonds issued under the Indenture and in the manner provided in Supplement No. 1; provided that in no event will Obligation No. 1 be redeemed unless a corresponding amount of Bonds is also redeemed. Notice of any redemption of Obligation No. 1 will be given to the Master Trustee and mailed by the Master Trustee to the Holder of Obligation No. 1 at the address shown on the books of the Master Trustee not less than 15 nor more than 45 days prior to the date set for redemption, but failure to so mail such notice will not be a condition precedent to, nor will such failure affect the validity of the proceedings for, the redemption of Obligation No. 1.

Events of Default; Acceleration

Any of the following will constitute an Event of Default under Supplement No. 1 and under the Master Indenture:

- (a) A "Loan Default Event" under the Loan Agreement.

- (b) An event of default under the Deed of Trust.

Upon the occurrence and during the continuation of an Event of Default under the Master Indenture, the Master Trustee will, if requested by the Authority, regardless of whether the Outstanding principal amount of Obligation No. 1 equals at least 25% of the aggregate principal amount of all Obligations issued under the Master Indenture then Outstanding, give notice pursuant to the Master Indenture to the Obligated Group declaring the principal of all Obligations issued under the Master Indenture then Outstanding to be due and immediately payable, and upon any such declaration the same will become and will be immediately due and payable, anything in the Master Indenture or in such Obligations contained to the contrary notwithstanding.

Upon the occurrence and during the continuation of an Event of Default under the Master Indenture described above, the Master Trustee and, upon the request of the Holders of not less than 25% in aggregate Outstanding principal amount of Obligation No. 1, will, upon being indemnified to its satisfaction therefor, proceed forthwith to protect and enforce its rights and the rights of the Holders under Supplement No. 1 by such suits, actions or proceedings as the Master Trustee, being advised by counsel, will deem expedient, including exercising any and all remedies under the Deed of Trust. Anything to the contrary notwithstanding, the Master Trustee will not be required to exercise any remedies with respect to the Deed of Trust unless the Master Trustee is satisfied that the Master Trustee will not be subject to any liability under any local, state or federal environmental laws or regulations of any kind whatsoever or from any circumstances present at the Pledged Assets related to such Deed of Trust, relating to the presence, use, management, disposal of, or contamination by any environmentally hazardous materials or substances of any kind whatsoever.

Tax Exempt Status

The Corporation covenants that so long as the Master Indenture will remain in force and effect and so long as all amounts due or to become due on any Bond have not been fully paid to the Holder thereof, that it will not take any action or suffer any action to be taken by others, including any action that would result in the alteration or loss of its status as a Tax Exempt Organization, which, in the Opinion of Bond Counsel, would result in the interest payable on any Bond being includable in gross income of the registered owner thereof for purposes of federal income taxation.

Additional Covenants

For so long as Obligation No. 1 shall remain Outstanding, the following covenants will apply to the Corporation and the Obligated Group, as applicable.

- (a) To secure the Obligated Group's obligations under this First Supplemental Master Indenture and all Obligations issued under the Master Indenture on a parity basis, the Corporation has executed that certain Deed of Trust, dated October 1, 2007 (as it may be amended and supplemented from time to time in accordance with the terms hereof, the "Deed of Trust"), in favor of First American Title Insurance Company, for the benefit of the Master Trustee. Each Member covenants and agrees to execute and cause to be filed Uniform Commercial Code financing statements and to execute and deliver such other documents as the Master Trustee may reasonably require in order to perfect or maintain as perfected the security interest granted under the Deed of Trust.

- (b) The definition of "Non-Recourse Indebtedness" is amended as follows:

Non-Recourse Indebtedness will mean any Indebtedness (i) which is secured by a Lien on Property other than the Pledged Assets, liability for which Lien is effectively limited to the real property, improvements or equipment acquired with such Non-Recourse Indebtedness and the income therefrom, with no recourse directly or indirectly to any Member, and (ii) which is not a general obligation of any Member.

- (c) The definition of "Permitted Encumbrances" is amended as follows:

- (i) A new subsection (v) is added:
 - (v) Liens created by the Deed of Trust; and

(ii) Subsection (v) is redesignated (w), and the introductory phrase of Subsection (w) is amended to read:

(w) any other Lien on Property (other than the Pledged Assets) provided that:

(d) Each Member, respectively, covenants and agrees that it will not create, assume or suffer to exist any Lien upon the Pledged Assets, except for Permitted Encumbrances. Each Member, respectively, further covenants and agrees that, if such a Lien is nonetheless created by someone other than an Obligated Group Member and is assumed by any Obligated Group Member, the Obligated Group Representative will make or cause to be made effective a provision whereby Obligation No. 1 will be secured prior to any such Indebtedness or other obligation secured by such Lien.

(e) Each Member covenants and agrees that it will not, in any Fiscal Year, sell, lease or otherwise dispose of any part of the Pledged Assets unless:

(i) Such sale, lease or other disposition is part of a merger or consolidation as permitted by the Master Indenture;

(ii) the net proceeds of such sale, lease or other disposition is applied to the redemption of Obligation No. 1 in the principal amount then outstanding; or

(iii) to another Member.

(f) The Members may sell, lease or otherwise dispose of any part of the Pledged Assets so long as one or more Members contemporaneously with such lease, sale or other disposition executes, delivers and records an additional deed of trust in favor of the deed trustee under the Deed of Trust, as deed trustee under such additional deed of trust, and the Master Trustee, as beneficiary, on other real property owned by such Member or Members which is of at least equivalent Fair Market Value to the Pledged Assets so sold, leased or otherwise disposed of, as evidenced by an Officer's Certificate so stating and stating that the title policy then in effect continues to comply with Supplement No. 1, "Fair Market Value" means, with respect to Supplement No. 1, the fair market value of the Pledged Assets as determined by either:

(i) an appraisal of the portion of such Pledged Assets which is real property (including buildings and any permanent fixtures thereon) made within five years of the date of determination by a "Member of the Appraisal Institute" and by an appraisal of the portion of such Pledged Assets which is not real property made within five years of the date of determination by any expert qualified in relation to the subject matter, provided that any such appraisal will be performed by a person or firm which (1) is in fact independent, (2) does not have any direct financial interest or any material indirect financial interest in any Obligated Group Member or any Affiliate and (3) is not connected with any Obligated Group Member or any Affiliate as an officer, employee, promoter, trustee, partner, director or person performing similar functions, adjusted for the period, not in excess of five years, from the date of the last such appraisal for changes in the implicit price deflator for the gross national product as reported by the United States Department of Commerce or its successor agency, or if such index is no longer published, such other index certified to be comparable and appropriate in an Officer's Certificate delivered to the Master Trustee;

(ii) a bona fide offer for the purchase of such Pledged Assets made on an arm's-length basis within six months of the date of determination, as established by an Officer's Certificate; or

(iii) an established market for such Pledged Assets, including, without limitation, securities and other obligations.

(g) Any property that is sold or otherwise disposed of (but not leased) pursuant to Supplement No. 1 will, immediately upon such sale or other disposition, be automatically released and removed from the definition of Pledged Assets and will no longer be deemed subject to the terms of Supplement No. 1 or the Deed of Trust. Subject to the Members' compliance with Supplement No. 1, the Master Trustee agrees to execute any releases, consents or other documents necessary or convenient to evidence such release and removal and allow for the valid

sale or other disposition of any part of the Pledged Assets by the Members in accordance with Supplement No. 1, and no additional consideration will be required for any such release, removal or substitution.

(h) Upon the written request of the Obligated Group Representative, the Master Trustee will execute and deliver such releases, subordinations, requests for reconveyance, termination statements or other instruments as may be reasonably requested by the Obligated Group Representative in connection with (1) the redemption of Obligation No. 1 in accordance with Supplement No. 1 and (2) the granting by an Obligated Group Member of any Lien which constitutes a Permitted Encumbrance under Supplement No. 1.

(i) The Obligated Group Representative agrees to obtain, at the cost and expense of the Members, an American Land Title Association policy of title insurance, or an endorsement to such policy, at the time of and dated as of the delivery of Obligation No. 1, in an aggregate amount not less than the aggregate principal amount of Obligation No. 1, payable to the Master Trustee for the benefit of the Holders of Obligation No. 1, insuring the title of the Corporation to the Pledged Assets, subject only to Permitted Encumbrances, issued by a title insurance company qualified to do business in the State of California.

(j) Notwithstanding anything in the Master Indenture or the Deed of Trust to the contrary, the Master Trustee will not be required to initiate foreclosure proceedings with respect to the Pledged Assets and will not otherwise be required to acquire possession of, or take other action with respect to the Pledged Assets which could cause it to be considered an “owner” or “operator” within the meaning of the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended from time to time, or any other law dealing with environmental matters or hazardous substances, unless the Master Trustee has sufficient comfort, based on previous determinations by experts on which the Master Trustee can rely, including an environmental report (any expense of a new report will be paid from funds under the Master Indenture if moneys are available or will be paid by the Holder or Holders), that:

(i) the Pledged Assets are in compliance with all environmental laws, rules or regulations or, if the Pledged Assets are not in compliance, that it would nevertheless be in the best economic interest of the Master Trustee and the Holder or Holders to take such actions as are necessary for the Pledged Assets to comply therewith; and

(ii) there are no circumstances present at the Pledged Assets relating to the use, management or disposal of any hazardous substances, hazardous materials, hazardous wastes, or petroleum-based materials for which investigation, testing, monitoring, contaminant clean up or remedial action could be required under any environmental laws or that, if any such materials are present for which such action could be required, that it would nevertheless be in the best economic interest of the Master Trustee and the Holder or Holders to take such actions with respect to the Pledged Assets; and

(iii) if the Master Trustee has determined that it would be in the best economic interest of the Master Trustee and the Holder or Holders, the Master Trustee must be satisfied that it will suffer no unreimbursed liabilities and will be adequately reimbursed for all liabilities, expenses and costs from available funds in the Master Trustee’s possession and control or from funds made available to the Master Trustee from the Holder or Holders; and

(iv) if the Master Trustee has determined that it would be in the best economic interest of the Master Trustee and the Holder or Holders to take any such action and its aforementioned liabilities, expenses and costs will be adequately reimbursed the Master Trustee has so notified the Holder or Holders and has not received, within 30 days of such notification, instructions from the Holder or the Holders of a majority of the Bonds Outstanding directing it not to take such action .

If the foregoing conditions are not satisfied and the Master Trustee is not willing to waive such conditions and initiate foreclosure proceedings, then the Master Trustee will take such actions as are reasonably necessary or appropriate in order to facilitate the appointment of a co-trustee, being a person or entity designated by the Holder or Holders and to assign to such person or entity (subject, however, to the trusts created pursuant to the Master Indenture) the beneficial interest under the Deed of Trust which secures the obligations under Supplement No. 1 for the limited purpose of conducting a foreclosure of such Deed of Trust and receiving and holding any title to real

estate obtained as a result of such foreclosure. Persons or entities appointed as co-trustees will not be required to meet the criteria of the Master Indenture or any other criteria in order to serve as such. The Master Trustee will not be responsible for the acts of a co-trustee appointed pursuant to Supplement No. 1.

Notwithstanding anything in the Master Indenture, the Deed of Trust or any document to the contrary, only moneys held under the Master Indenture or funds provided by the Holder or Holders, may be used to remedy an environmental contamination and the Master Trustee will not have personal liability for clean-up costs, unless the environmental contamination is a result of negligent acts of the Master Trustee in its fiduciary capacity.

BOND INDENTURE

General

The Bond Indenture sets forth the terms of the Bonds, the nature and extent of the security, various rights of the Bondholders, rights, duties and immunities of the Bond Trustee and the rights and obligations of the Authority. Certain provisions of the Bond Indenture are summarized below. Other provisions are summarized in this Official Statement under the caption "THE BONDS." This summary does not purport to be complete or definitive and is qualified in its entirety by reference to the full terms of the Bond Indenture.

Revenues

Establishment of Funds.

The Indenture creates an Interest Fund, a Principal Fund, a Sinking Fund, a Sinking Accounts within the Sinking Fund, a Redemption Fund, an Optional Redemption Account and a Special Redemption Account within the Redemption Fund, a Costs of Issuance Fund, a Bond Reserve Fund, a Revenue Fund and a Rebate Fund, all of which are to be held by the Trustee.

Pledge and Assignment; Revenue Fund.

(a) Subject only to the provisions of the Bond Indenture permitting the application thereof for the purposes and on the terms and conditions set forth in the Bond Indenture, there are pledged to secure the payment of the principal of, premium, if any, and interest on the Bonds in accordance with their terms and the provisions of the Bond Indenture, all of the Revenues and any other amounts (including proceeds of the sale of Bonds) held in any fund or account established pursuant to the Bond Indenture (other than the Rebate Fund). Said pledge will constitute a lien on and security interest in such assets and will attach, be perfected and be valid and binding from and after delivery by the Bond Trustee of the Bonds, without any physical delivery thereof or further act.

(b) The Authority transfers in trust, grants a security interest in and assigns to the Bond Trustee, for the benefit of the Holders from time to time of the Bonds, all of the Revenues and other assets pledged in the Bond Indenture and all of the right, title and interest of the Authority in the Loan Agreement (except for (i) the right to receive any Administrative Fees and Expenses to the extent payable to the Authority, and (ii) any rights of the Authority or its officers, directors, agents or employees to reimbursement or indemnification) and Obligation No. 1. The Bond Trustee will be entitled to and will collect and receive all of the Revenues, and any Revenues collected or received by the Authority will be deemed to be held, and to have been collected or received, by the Authority as the agent of the Bond Trustee and will forthwith be paid by the Authority to the Bond Trustee. The Bond Trustee also will be entitled to and will take all steps, actions and proceedings reasonably necessary in its judgment to enforce all of the rights of the Authority and all of the obligations of the Corporation under the Loan Agreement and of the Corporation and the other Member under Obligation No. 1.

Allocation of Revenues.

On or before the Business Day immediately preceding each Interest Payment Date (with respect to payments of interest) and each Principal Payment Date (with respect to payments of principal or Mandatory Sinking Account Payments), the Bond Trustee will transfer from the Revenue Fund and deposit into the following respective

funds (each of which the Bond Trustee will establish and maintain) and then to the Rebate Fund, the following amounts, in the following order of priority, the requirements of each such fund (including the making up of any deficiencies in any such fund resulting from lack of Revenues sufficient to make any earlier required deposit) at the time of deposit to be satisfied before any transfer is made to any account subsequent in priority:

First: To the Interest Fund, an amount sufficient to bring the amount on deposit up to the aggregate amount of interest becoming due and payable on the Outstanding Bonds on the next succeeding Interest Payment Date;

Second: To the Principal Fund, an amount sufficient to bring the amount on deposit up to the aggregate amount of principal becoming due and payable on the Outstanding Bonds on the next succeeding Principal Payment Date; and

Third: To the Sinking Fund, the aggregate amount of Mandatory Sinking Account Payments required to be paid into the Sinking Fund to redeem the Outstanding Term Bonds on the next Principal Payment Date, less the amount by which the aggregate amount of such Mandatory Sinking Account Payments may be reduced pursuant to the provisions of the Bond Indenture.

As long as no Event of Default has occurred and is continuing, any moneys remaining in the Revenue Fund after the foregoing transfers will be transferred to the Optional Redemption Account.

Application of Interest Fund.

All amounts in the Interest Fund will be used and withdrawn by the Bond Trustee solely for the purpose of paying interest on the Bonds as it will become due and payable (including accrued interest on any Bonds purchased or redeemed prior to maturity pursuant to the Bond Indenture).

Application of Principal Fund.

All amounts in the Principal Fund will be used and withdrawn by the Bond Trustee solely for the purpose of paying principal of the Serial Bonds when due and payable.

Application of Sinking Fund.

Amounts in the Sinking Fund will be used and withdrawn by the Bond Trustee solely to purchase Term Bonds or redeem Term Bonds or pay Term Bonds at maturity. The Bond Trustee will establish and maintain within the Sinking Fund separate Sinking Accounts for the respective Term Bonds. With respect to each Sinking Account, on each Mandatory Sinking Account Payment date, as established for such Sinking Account pursuant to the Bond Indenture, the Bond Trustee will apply the Mandatory Sinking Account Payment required pursuant to the Bond Indenture, on that date to the redemption (or payment at maturity, as the case may be) of Term Bonds for which such Sinking Account was established, upon the notice and in the manner provided in the Bond Indenture; provided that, at any time prior to selection of Bonds for redemption, the Bond Trustee may apply moneys in such Sinking Account to the purchase of Term Bonds at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Fund) as the Bond Trustee may be directed in writing by the Corporation or the Authority, except that the purchase price (excluding accrued interest) will not exceed the par value of such Bonds. If, during the twelve-month period immediately preceding said Mandatory Sinking Account Payment date, the Bond Trustee has purchased Term Bonds with moneys in such Sinking Account, or, during said period and prior to the selection of Bonds for redemption, the Corporation has deposited Term Bonds with the Bond Trustee, or Term Bonds were at any time purchased or redeemed by the Bond Trustee from the Redemption Fund and allocable to said Mandatory Sinking Account Payment, such Bonds so purchased or deposited or redeemed will be applied, to the extent of the full principal amount thereof, first to reduce said Mandatory Sinking Account Payment, and then as a credit against such future Mandatory Sinking Account Payments as the Corporation may specify in a Certificate of the Corporation. All Bonds purchased or deposited pursuant to the Bond Indenture will be cancelled and delivered by the Bond Trustee to or upon the Order of the Authority. Any amounts remaining in a Sinking Account when all of the Term Bonds

for which such account was established are no longer Outstanding will be withdrawn by the Bond Trustee and deposited in the Revenue Fund.

Application of Redemption Fund.

The Bond Trustee will establish a Redemption Fund, in which the Bond Trustee will further establish an Optional Redemption Account and a Special Redemption Account. All amounts deposited in the Optional Redemption Account and in the Special Redemption Account will be used and withdrawn by the Bond Trustee solely for the purpose of redeeming Bonds, in the manner and upon the terms and conditions specified in the Bond Indenture, at the next succeeding date of redemption for which notice has not been given and at the Redemption Prices then applicable to redemptions from the Optional Redemption Account and the Special Redemption Account, respectively; provided that, at any time prior to giving such notice of redemption, the Bond Trustee may apply such amounts to the purchase of Bonds at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Fund) as the Corporation may direct, except that the purchase price (exclusive of accrued interest) may not exceed the Redemption Price then applicable to such Bonds; and provided further that in the case of the Optional Redemption Account, in lieu of redemption at such next succeeding date of redemption or in combination therewith, amounts in such account may be transferred to the Revenue Fund and credited against Loan Repayments in order of their due date as set forth in a Request of the Corporation.

Rebate Fund.

The Bond Trustee will establish and maintain a fund separate from any other fund established and maintained under the Bond Indenture, designated as the Rebate Fund. All amounts at any time on deposit in the Rebate Fund will be held by the Bond Trustee in trust, to the extent required to satisfy the requirements to make rebate payments to the United States pursuant to Section 148 of the Code and the Treasury Regulations promulgated thereunder. Such amounts will be free and clear of any lien under the Bond Indenture and will be governed by the Bond Indenture and by the Tax Agreement. The Bond Trustee will be deemed conclusively to have complied with such provisions if it follows the directions of the Corporation and will not be required to take any actions thereunder in the absence of written directions by the Corporation.

Investment of Moneys in Funds and Accounts.

All moneys in any of the funds and accounts established pursuant to the Bond Indenture will be invested by the Bond Trustee, upon written direction of the Corporation, solely in Investment Securities. Investment Securities will be purchased at such prices as the Corporation may direct. All Investment Securities will be acquired subject to the limitations set forth in the Bond Indenture, the limitations as to maturities set forth in the Bond Indenture and such additional limitations or requirements consistent with the foregoing as may be established by Request of the Corporation. No Request of the Corporation will impose any duty on the Bond Trustee inconsistent with its fiduciary responsibilities. The Bond Trustee may purchase from or sell to itself or to its affiliate, as principal or agent, any of the Investment Securities. In the absence of directions from the Corporation, the Bond Trustee will invest in Investment Securities as specified in the Bond Indenture. The Bond Trustee is specifically authorized to implement its automated cash investment system to assure that cash on hand is invested and to charge its normal cash management fees, which may be deducted from income earned on such investments.

Investment Securities acquired as an investment of moneys in any fund or account established under the Bond Indenture will be credited to such fund or account. For the purpose of determining the amount in any such fund or account (other than the Bond Reserve Fund, which will be governed by the Bond Indenture) all Investment Securities credited to such fund or account will be valued by the Bond Trustee at their market value and marked to market at least once each year on or before September 1. All interest, profits and other income received from the investment of moneys in any fund established pursuant to the Bond Indenture will be deposited in the fund or account which gave rise to the investment earnings.

Bond Reserve Fund.

(a) The Bond Trustee will establish, maintain and hold in trust for the benefit of the Holders a separate fund designated as the Bond Reserve Fund. The Bond Trustee will transfer from the prior reserve fund for the Prior Bonds and deposit in the Bond Reserve Fund the sum of \$4,025,362.50, equal to the Bond Reserve Requirement as of the Date of the Bonds. All amounts in the Bond Reserve Fund will be used and withdrawn by the Bond Trustee solely for the purpose of making up any deficiency in the Interest Fund, the Principal Fund or the Sinking Fund or (together with any other money available therefor) for the redemption of all Bonds then Outstanding. Prior to making a withdrawal from the Bond Reserve Fund to make up a deficiency in the Interest Fund, the Bond Trustee will notify the Corporation of such deficiency and the Corporation may deposit with the Bond Trustee all or part of such deficiency. The Bond Reserve Fund will be funded in connection with the issuance of the Bonds in an amount equal to the Bond Reserve Requirement. Any amount in the Bond Reserve Fund in excess of the Bond Reserve Requirement will be transferred on the second Business Day following the calculation required pursuant to the Bond Indenture (i) to the Sinking Fund or the Principal Fund whenever and to the extent necessary to increase the balance in said funds to the aggregate amount of principal and Mandatory Sinking Account Payments scheduled to be paid from said funds, respectively, on the next Principal Payment Date and (ii) otherwise to the Optional Redemption Account or the Corporation, as directed by the Corporation. The Bond Trustee is authorized to sell Investment Securities if necessary to make such transfers.

(b) Amounts on deposit in the Bond Reserve Fund will be valued by the Bond Trustee at their market value as of each February 1, May 1, August 1 and November 1, and the Bond Trustee will notify the Corporation of the results of such valuation. In making such valuations, the Bond Trustee may utilize computerized securities pricing services that may be available to it, including those available through its regular accounting system and rely thereon. If the amount on deposit in the Bond Reserve Fund on any day following such valuation is less than ninety-eight percent of the Bond Reserve Requirement, the Corporation will make the deposits to the Bond Reserve Fund required by the Bond Indenture.

(c) The Corporation will deposit, on the first calendar day of each month, to the Bond Reserve Fund, (i) one-twelfth of the aggregate amount of each prior withdrawal from the Bond Reserve Fund for the purpose of making up a deficiency in the Interest Fund, Principal Fund or Sinking Fund (until deposits on account of such withdrawal are sufficient to fully restore the amount withdrawn), provided that no deposit need be made into the Bond Reserve Fund so long as the balance in said fund will be at least equal to the Bond Reserve Requirement, and (ii) in the event the balance in said fund will be less than ninety-eight percent of the Bond Reserve Requirement due to valuation of the Investment Securities deposited therein in accordance with the Bond Indenture, one-third of the amount necessary to fully restore the amount on deposit in the Bond Reserve Fund to the Bond Reserve Requirement.

(d) In lieu of maintaining and depositing moneys in the Bond Reserve Fund, the Corporation may deposit with the Bond Trustee a letter of credit, (i) which is issued by a bank with, a credit rating at the time of deposit of such letter of credit into the Bond Reserve Fund of at least investment grade from each Rating Agency rating the Bonds, (ii) the repayment obligation with respect to which is not secured by a lien on assets of any Member senior to any lien which secures the Bonds and (iii) which has a term of at least five years from the date of issuance thereof. If the credit rating of the bank issuing such letter of credit falls below investment grade, the Corporation will within twelve months of such downgrading either (i) substitute a new letter of credit satisfying the requirements of this paragraph, (ii) fund the Bond Reserve Fund through the deposit of cash or an irrevocable surety bond policy satisfying the requirements of the immediately succeeding paragraph or (iii) fund the Bond Reserve Fund through a combination of (i) and (ii). At least six months prior to the expiration date of a letter of credit on deposit in the Bond Reserve Fund, the Corporation will either (i) substitute a new letter of credit satisfying the requirements of this paragraph, (ii) fund the Bond Reserve Fund through the deposit of cash or an irrevocable surety bond policy satisfying the requirements of the immediately succeeding paragraph or (iii) fund the Bond Reserve Fund through a combination of (i) and (ii). Any such letter of credit will permit the Bond Trustee to draw amounts thereunder for deposit in the Bond Reserve Fund which, together with any moneys on deposit in, or surety bond policy available to fund, the Bond Reserve Fund, are not less than the Bond Reserve Requirement and which may be applied to any purpose for which moneys in the Bond Reserve Fund may be applied. The Bond Trustee will make a drawing on such letter of credit (i) whenever moneys are required for the purposes for which Bond Reserve Fund moneys may be applied, and (ii) prior to any expiration or termination thereof; provided, however, that no such

drawing need be made if other moneys or an irrevocable surety bond are available in the Bond Reserve Fund in the amount of the Bond Reserve Requirement.

(e) In lieu of maintaining and depositing moneys in the Bond Reserve Fund, the Corporation also may maintain in effect an irrevocable surety bond policy, (i) which is issued by a bond insurance company with a claims-paying ability rating at the time of deposit of such surety bond policy into the Bond Reserve Fund of at least investment grade from each Rating Agency rating the Bonds, (ii) the repayment obligation with respect to which is not secured by a lien on assets of any Member senior to any lien which secures the Bonds and (iii) has a term of at least five years from the date of issuance thereof. If the credit rating of the bond insurance company issuing such surety bond policy falls below investment grade, the Corporation will within twelve months of such downgrading either (i) substitute a new surety bond policy satisfying the requirements of this paragraph, (ii) fund the Bond Reserve Fund through the deposit of cash or a letter of credit satisfying the requirements of the immediately preceding paragraph or (iii) fund the Bond Reserve Fund through a combination of (i) and (ii). At least six months prior to the expiration date of a surety bond policy on deposit in the Bond Reserve Fund, the Corporation will either (i) substitute a new surety bond policy satisfying the requirements of this paragraph, (ii) fund the Bond Reserve Fund through the deposit of cash or a letter of credit satisfying the requirements of the immediately preceding paragraph or (iii) fund the Bond Reserve Fund through a combination of (i) and (ii). Any such surety bond policy will permit the Bond Trustee to obtain amounts thereunder for deposit in the Bond Reserve Fund which, together with any moneys on deposit in, or letter of credit available to fund, the Bond Reserve Fund, are not less than the Bond Reserve Requirement and which may be applied to any purpose for which moneys in the Bond Reserve Fund may be applied. The Bond Trustee will make a drawing on such surety bond policy (i) whenever moneys are required for the purposes for which Bond Reserve Fund moneys may be applied, and (ii) prior to any expiration or termination thereof; provided, however, that no such drawing need be made if other moneys or a letter of credit are available in the Bond Reserve Fund in the amount of the Bond Reserve Requirement.

Particular Covenants

Tax Covenants.

(a) The Authority covenants that it will not take any action, or fail to take any action, if such action or such failure to take action would result in the interest on the Bonds not being excluded from gross income for federal income tax purposes under Section 103 of the Code. Without limiting the generality of the foregoing, the Authority covenants that it will comply with the requirements of the Tax Agreement, which is incorporated in the Bond Indenture as if fully set forth in the Bond Indenture. This covenant will survive the payment in full or the defeasance of the Bonds.

(b) In the event that at any time the Authority is of the opinion that it is necessary or helpful to restrict or limit the yield on the investment of any moneys held by the Bond Trustee under the Bond Indenture, the Authority will so instruct the Bond Trustee and the Corporation in a Written Request of the Authority accompanied by a supporting Favorable Opinion of Bond Counsel, and the Bond Trustee will take such action as may be directed by the Corporation.

(c) Notwithstanding any provisions of the Bond Indenture, if the Authority will provide to the Bond Trustee a Favorable Opinion of Bond Counsel to the effect that any specified action required under the Bond Indenture is no longer required or that some further or different action is required to maintain the exclusion from federal income tax of interest on the Bonds, the Bond Trustee may conclusively rely on such opinion in complying with the requirements of the Bond Indenture and the Tax Agreement, and the covenants under the Bond Indenture will be deemed to be modified to that extent.

Other Covenants; Amendment of Loan Agreement.

(a) Subject to the provisions of the Bond Indenture, the Bond Trustee will upon receipt of amounts due from the Corporation pursuant to the Loan Agreement, perform such duties as are expressly provided for under the Bond Indenture which are imposed upon the Authority under the Loan Agreement and assigned to it pursuant to the Bond Indenture and will enforce and take all steps, actions and proceedings reasonably necessary for the enforcement of the rights of the Authority under the Loan Agreement as assigned to the Bond Trustee.

(b) The Authority will not amend, modify or terminate any of the terms of the Loan Agreement, or consent to any such amendment, modification or termination, without the prior written consent of the Bond Trustee. The Bond Trustee will give such written consent if but only if (1) it will make a determination that such amendment or modification will not materially and adversely affect the interests of the Holders of the Bonds (provided that, in making such determination, the Bond Trustee may conclusively rely on written representations of financial consultants or advisors or the opinion or advice of counsel), or (2) the Holders of a majority in aggregate principal amount of the Bonds then Outstanding consent in writing to such amendment, modification or termination, provided that no such amendment, modification or termination will reduce the amount of Loan Repayments to be made to the Authority or the Bond Trustee by the Corporation pursuant to the Loan Agreement, or extend the time for making such payments, without the written consent of all of the Holders of the Bonds then Outstanding. The Bond Trustee will mail a copy of such amendment as executed to each Rating Agency then rating the Bonds promptly after execution by the Authority and the Corporation.

Events of Default and Remedies of Bondholders

Events of Default.

The following events will be Events of Default: (a) default in the due and punctual payment of the principal or Redemption Price of any Bond when and as the same will become due and payable, whether at maturity as therein expressed, by proceedings for redemption from Mandatory Sinking Account Payments, by declaration of acceleration or otherwise; (b) default in the due and punctual payment of any installment of interest on any Bond when and as such interest installment will become due and payable; (c) default by the Authority in the observance of any of the other covenants, agreements or conditions on its part contained in the Bond Indenture or in the Bonds, if such default will have continued for a period of thirty (30) days after written notice thereof, specifying such default and requiring the same to be remedied, will have been given to the Authority and the Corporation by the Bond Trustee, or to the Authority, the Corporation and the Bond Trustee by the Holders of not less than 25% in aggregate principal amount of the Bonds at the time Outstanding; or (d) a Loan Default Event. See “LOAN AGREEMENT—Events of Default” in this Appendix C.

Acceleration of Maturities.

Whenever any Event of Default referred to in the Bond Indenture will have happened and be continuing, the Bond Trustee may take the following remedial steps:

(a) In the case of an Event of Default described in the Bond Indenture, the Bond Trustee may notify the Master Trustee of such Event of Default, may make a demand for payment under Obligation No. 1 and request the Master Trustee in writing to give notice pursuant to the Master Indenture to the Members of the Obligated Group declaring the principal of all Obligations and other obligations issued under the Master Indenture then outstanding to be due and immediately payable. Upon such declaration by the Master Trustee, the Bond Trustee will declare the principal of all the Bonds then Outstanding, and the interest accrued thereon, to be due and payable immediately, and upon any such declaration by the Bond Trustee the same will become and will be immediately due and payable, anything in the Bond Indenture to the contrary notwithstanding. In addition, the Bond Trustee may take whatever action at law or in equity is necessary or desirable to collect the payments due under Obligation No. 1;

(b) In the case of an Event of Default described in the Bond Indenture, the Bond Trustee may take whatever action at law or in equity is necessary or desirable to enforce the performance, observance or compliance by the Authority with any covenant, condition or agreement by the Authority under the Bond Indenture; and

(c) In the case of an Event of Default described in the Bond Indenture, the Bond Trustee may take whatever action the Authority would be entitled to take, and will take whatever action the Authority would be required to take, pursuant to the Loan Agreement in order to remedy the Loan Default Event.

Any such declaration, however, is subject to the condition that if, at any time after such declaration and before any judgment or decree for the payment of the moneys due will have been obtained or entered, the Authority or the Corporation will deposit with the Bond Trustee a sum sufficient to pay all the principal or redemption price of

and installments of interest on the Bonds, payment of which is overdue, with interest on such overdue principal at the rate borne by the respective Bonds, and the reasonable charges and expenses of the Bond Trustee, and if the Bond Trustee has received notification from the Master Trustee that the declaration of acceleration of Obligation No. 1 has been annulled pursuant to the Master Indenture and any and all other defaults known to the Bond Trustee (other than in the payment of principal of and interest on the Bonds due and payable solely by reason of such declaration) will have been made good or cured to the satisfaction of the Bond Trustee or provision deemed by the Bond Trustee to be adequate will have been made therefor, then, and in every such case, the Bond Trustee will, on behalf of the Holders of all of the Bonds, rescind and annul such declaration and its consequences and waive such default; but no such rescission and annulment will extend to or will affect any subsequent default, or will impair or exhaust any right or power consequent thereon.

Bond Trustee to Represent Bondholders.

The Bond Trustee is irrevocably appointed (and the successive respective Holders of the Bonds, by taking and holding the same, will be conclusively deemed to have so appointed the Bond Trustee) as trustee and true and lawful attorney-in-fact of the Holders of the Bonds for the purpose of exercising and prosecuting on their behalf such rights and remedies as may be available to such Holders under the provisions of the Bonds, the Bond Indenture, the Loan Agreement, Obligation No. 1, the Act and applicable provisions of any other law. Upon the occurrence and continuance of an Event of Default or other occasion giving rise to a right in the Bond Trustee to represent the Bondholders, the Bond Trustee in its discretion may and, upon the written request of the Holders of not less than 25% in aggregate principal amount of the Bonds then Outstanding and upon being indemnified to its satisfaction therefor, will proceed to protect or enforce its rights or the rights of such Holders by such appropriate action, suit, mandamus or other proceedings as it will deem most effectual to protect and enforce any such right, at law or in equity, either for the specific performance of any covenant or agreement contained in the Bond Indenture, or in aid of the execution of any power granted in the Bond Indenture, or for the enforcement of any other appropriate legal or equitable right or remedy vested in the Bond Trustee or in such Holders under the Bond Indenture, the Loan Agreement, Obligation No. 1, the Act or any other law; and upon instituting such proceeding, the Bond Trustee will be entitled, as a matter of right, to the appointment of a receiver of the Revenues and other assets pledged under the Bond Indenture, pending such proceedings. If more than one such request is received by the Bond Trustee from the Holders, the Bond Trustee will follow the written request executed by the Holders of the greater percentage of Bonds then Outstanding in excess of 25%. All rights of action under the Bond Indenture or the Bonds or otherwise may be prosecuted and enforced by the Bond Trustee without the possession of any of the Bonds or the production thereof in any proceeding relating thereto, and any such suit, action or proceeding instituted by the Bond Trustee will be brought in the name of the Bond Trustee for the benefit and protection of all the Holders of such Bonds, subject to the provisions of the Bond Indenture.

Bondholders' Direction of Proceedings.

The Holders of a majority in aggregate principal amount of the Bonds then Outstanding will have the right, by an instrument or concurrent instruments in writing executed and delivered to the Bond Trustee, and upon indemnifying the Bond Trustee to its satisfaction therefor, to direct the method of conducting all remedial proceedings taken by the Bond Trustee under the Bond Indenture, provided that such direction will not be otherwise than in accordance with law and the provisions of the Bond Indenture, and that the Bond Trustee will have the right to decline to follow any such direction which in the opinion of the Bond Trustee would be unjustly prejudicial to Bondholders not parties to such direction.

Limitation on Bondholders' Right to Sue.

No Holder of any Bond will have the right to institute any suit, action or proceeding at law or in equity, for the protection or enforcement of any right or remedy under the Bond Indenture, the Loan Agreement, Obligation No. 1, the Act or any other applicable law with respect to such Bond, unless (1) such Holder will have given to the Bond Trustee written notice of the occurrence of an Event of Default; (2) the Holders of not less than 25% in aggregate principal amount of the Bonds then Outstanding will have made written request upon the Bond Trustee to exercise the powers granted before the date of the Bond Indenture or to institute such suit, action or proceeding in its own name; provided, however, that if more than one such request is received by the Bond Trustee from the Holders, the Bond Trustee will follow the written request executed by the Holders of the greater percentage of Bonds then

Outstanding in excess of 25%; (3) such Holder or said Holders will have tendered to the Bond Trustee indemnity satisfactory to it against the costs, expenses and liabilities to be incurred in compliance with such request; and (4) the Bond Trustee will have refused or omitted to comply with such request for a period of 60 days after such written request will have been received by, and said tender of indemnity will have been made to, the Bond Trustee.

Such notification, request, tender of indemnity and refusal or omission are declared, in every case, to be conditions precedent to the exercise by any Holder of Bonds of any remedy under the Bond Indenture or under law; it being understood and intended that no one or more Holders of Bonds will have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Bond Indenture or the rights of any other Holders of Bonds, or to enforce any right under the Bond Indenture, the Loan Agreement, Obligation No. 1, the Act or other applicable law with respect to the Bonds, except in the manner provided in the Bond Indenture, and that all proceedings at law or in equity to enforce any such right will be instituted, had and maintained in the manner provided in the Bond Indenture and for the benefit and protection of all Holders of the Outstanding Bonds, subject to the provisions of the Bond Indenture.

Modification or Amendment of the Bond Indenture

Amendments Permitted.

(a) The Bond Indenture and the rights and obligations of the Authority and of the Holders of the Bonds and of the Bond Trustee may be modified or amended from time to time and at any time by an indenture or indentures supplemental to the Bond Indenture, which the Authority and the Bond Trustee may enter into when the written consent of the Holders of a majority in aggregate principal amount of the Bonds then Outstanding will have been filed with the Bond Trustee. No such modification or amendment will (i) extend the fixed maturity of any Bond, or reduce the amount of principal thereof, or extend the time of payment or reduce the amount of any Mandatory Sinking Account Payment, or reduce the rate of interest thereon, or extend the time of payment of interest thereon, or reduce any premium payable upon the redemption thereof, without the consent of the Holder of each Bond so affected, or (ii) reduce the aforesaid percentage of Bonds the consent of the Holders of which is required to effect any such modification or amendment, or permit the creation of any lien on the Revenues and other assets pledged under the Bond Indenture prior to or on a parity with the lien created by the Bond Indenture, or deprive the Holders of the Bonds of the lien created by the Bond Indenture on such Revenues and other assets (except as expressly provided in the Bond Indenture), without the consent of the Holders of all Bonds then Outstanding.

It will not be necessary for the consent of the Bondholders to approve the particular form of any Supplemental Bond Indenture, but it will be sufficient if such consent will approve the substance thereof. Promptly after the execution by the Authority and the Bond Trustee of any Supplemental Bond Indenture, the Bond Trustee will mail a notice, setting forth in general terms the substance of such Supplemental Bond Indenture to the Bondholders at the addresses shown on the registration books maintained by the Bond Trustee. Any failure to give such notice, or any defect therein, will not, however, in any way impair or affect the validity of any such Supplemental Bond Indenture.

(b) The Bond Indenture and the rights and obligations of the Authority, of the Bond Trustee and of the Holders of the Bonds may also be modified or amended from time to time and at any time by an indenture or indentures supplemental to the Bond Indenture, which the Authority and the Bond Trustee may enter into without the necessity of obtaining the consent of any Bondholders, only to the extent permitted by law and only for any one or more of the following purposes: (i) to add to the covenants and agreements of the Authority contained in the Bond Indenture other covenants and agreements thereafter to be observed, to pledge or assign additional security for the Bonds (or any portion thereof), or to surrender any right or power reserved under the Bond Indenture to or conferred upon the Authority, provided, that no such covenant, agreement, pledge, assignment or surrender will materially adversely affect the interests of the Holders of the Bonds; (ii) to make such provisions for the purpose of curing any ambiguity, inconsistency or omission, or of curing or correcting any defective provision, contained in the Bond Indenture, or in regard to matters or questions arising under the Bond Indenture, as the Authority or the Bond Trustee may deem necessary or desirable and not inconsistent with the Bond Indenture, and which will not materially adversely affect the interests of the Holders of the Bonds; (iii) to modify, amend or supplement the Bond Indenture in such manner as to permit the qualification of the Bond Indenture under the Trust Indenture Act of 1939,

as amended, or any similar federal statute hereafter in effect, if required by such act or statute, and to add such other terms, conditions and provisions as may be permitted by said act or similar federal statute, and which will not materially adversely affect the interests of the Holders of the Bonds; (iv) to provide any additional procedures, covenants or agreements to maintain the exclusion from gross income for federal income tax purposes of interest on the Bonds; (v) facilitate (i) the transfer of Bonds from one Depository to another in the succession of Securities Depositories, or (ii) the withdrawal from a Depository of Bonds held in a Book-Entry System and the issuance of replacement Bonds in fully registered form to Persons other than a Depository; (vi) to authorize different authorized denominations of the Bonds and to make correlative amendments and modifications to the Bond Indenture regarding exchangeability of Bonds of different authorized denominations, redemptions of portions of Bonds of particular authorized denominations and similar amendments and modifications of a technical nature; (vii) to make any amendments appropriate or necessary to provide for any insurance policy, letter of credit, guaranty, surety bond, line of credit, revolving credit agreement, standby bond purchase agreement or other agreement or security device delivered to the Bond Trustee and providing for payment of the principal, interest and redemption premium on the Bonds or a portion thereof; (viii) to make any changes required by a Rating Agency in order to obtain or maintain a rating for the Bonds; or (ix) to modify, alter, amend or supplement the Bond Indenture in any other respect which is not materially adverse to the Bondholders.

Defeasance

Discharge of Indenture.

The Bonds of any Series may be paid by the Authority or the Bond Trustee on behalf of the Authority in any of the following ways:

- (a) by paying or causing to be paid the principal or Redemption Price of and interest on all Bonds Outstanding, as and when the same become due and payable;
- (b) by depositing with the Bond Trustee, in trust, at or before maturity, moneys or securities in the necessary amount to pay when due or redeem all Bonds then Outstanding; or
- (c) by delivering to the Bond Trustee, for cancellation by it, all Bonds then Outstanding.

If the Authority will also pay or cause to be paid all other sums payable under the Bond Indenture by the Authority and the Corporation will have paid all Administrative Fees and Expenses payable to the Authority pursuant to the Loan Agreement, then and in that case at the election of the Authority (evidenced by a Certificate of the Authority filed with the Bond Trustee signifying the intention of the Authority to discharge all such indebtedness and the Bond Indenture), and notwithstanding that any Bonds will not have been surrendered for payment, the Bond Indenture and the pledge of Revenues and other assets made under the Bond Indenture and all covenants, agreements and other obligations of the Authority under the Bond Indenture (except as otherwise provided in the Bond Indenture) will cease, terminate, become void and be completely discharged and satisfied.

Miscellaneous

Liability of Authority Limited to Revenues.

Notwithstanding anything in the Bond Indenture or in the Bonds contained, the Authority will not be required to advance any moneys derived from any source other than the Revenues and other assets pledged under the Bond Indenture for any of the purposes in the Bond Indenture mentioned, whether for the payment of the principal or Redemption Price of or interest on the Bonds or for any other purpose of the Bond Indenture. Nevertheless, the Authority may, but will not be required to, advance for any of the purposes any funds of the Authority which may be made available to it for such purposes.

LOAN AGREEMENT

General

The Loan Agreement provides the terms of the loan of the proceeds of the Bonds and any Additional Bonds to the Corporation and the repayment of and security for such loan by the Corporation. Certain provisions of the Loan Agreement are summarized below; this summary does not purport to be complete or definitive and is qualified in its entirety by reference to the full terms of the Loan Agreement.

Payments

Loan of Proceeds; Loan Repayments.

The Authority loans and advances to the Corporation, and the Corporation borrows and accepts from the Authority (solely from the proceeds of the sale of the Bonds), the net proceeds received from the sale of the Bonds, such proceeds to be applied under the terms and conditions of the Loan Agreement and the Bond Indenture. In consideration of the loan of such proceeds to the Corporation, as long as any of the Bonds remain Outstanding, the Corporation agrees to make payments, or cause payments to be made, at the times and in the amounts required to be paid as principal or Redemption Price of and interest on the Bonds from time to time Outstanding under the Bond Indenture and other amounts required to be paid under the Bond Indenture, as the same will become due whether at maturity, upon redemption, by declaration of acceleration or otherwise.

Additional Payments.

In addition to the Loan Repayments, the Corporation will also pay to the Authority or to the Bond Trustee, as the case may be, Additional Payments, including all taxes and assessments charged to the Authority or to the Bond Trustee, all reasonable fees, charges and expenses of the Bond Trustee for services rendered under the Bond Indenture, as and when the same become due and payable, the reasonable fees and expenses of experts engaged by the Issuer or the Trustee. In addition, the Corporation agrees to make any and all payments of all other reasonable and necessary fees and expenses attributable to the Loan Agreement or Obligation No. 1.

Obligations Unconditional.

The obligations of the Corporation under the Loan Agreement and pursuant to Obligation No. 1, including the obligation of the Corporation to pay the principal of and interest on Obligation No. 1, are absolute and unconditional, notwithstanding any other provision of the Loan Agreement, Supplement No. 1, the Master Indenture or the Bond Indenture. Until the Loan Agreement is terminated and all payments under the Loan Agreement are made, the Corporation: (a) will pay all amounts required under the Loan Agreement and under Obligation No. 1 without abatement, deduction or setoff except as otherwise expressly provided in the Loan Agreement; (b) will not suspend or discontinue any payments due under the Loan Agreement or under Obligation No. 1 for any reason whatsoever, including, without limitation, any right of setoff or counterclaim; (c) will perform and observe all its other agreements contained in the Loan Agreement; and (d) except as provided in the Loan Agreement, will not terminate the Loan Agreement for any cause including, without limiting the generality of the foregoing, damage, destruction or condemnation of the Corporation's facilities or any part thereof, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State of California, or any political subdivision of either thereof or any failure of the Authority to perform and observe any agreement, whether express or implied, or any duty, liability or obligation arising out of or connected with the Loan Agreement. Nothing contained in the Loan Agreement will be construed to release the Authority from the performance of any of the agreements on its part contained in the Loan Agreement; and in the event the Authority should fail to perform any such agreement on its part, the Corporation may institute such action against the Authority as the Corporation may deem necessary to compel performance.

The rights of the Bond Trustee or any party or parties on behalf of whom the Bond Trustee is acting will not be subject to any defense, setoff, counterclaim or recoupment whatsoever, whether arising out of any breach of any duty or obligation of the Authority, the Master Trustee or the Bond Trustee owing to the Corporation, or by

reason of any other indebtedness or liability at any time owing by the Authority or by the Master Trustee or Bond Trustee to the Corporation.

Events of Default and Remedies

Events of Default.

Each of the following events will constitute a Loan Default Event:

(a) Failure by the Corporation to pay in full any payment required under the Loan Agreement or under Obligation No. 1 when due, whether at maturity, upon a date fixed for prepayment, by declaration or otherwise pursuant to the terms of the Loan Agreement;

(b) If any material representation or warranty made by the Corporation in the Loan Agreement or made by the Corporation or any Member in any document, instrument or certificate furnished to the Bond Trustee or the Authority in connection with the issuance of Obligation No. 1 or the Bonds will at any time prove to have been incorrect in any respect as of the time made;

(c) If the Corporation will fail to observe or perform any covenant, condition, agreement or provision in the Loan Agreement on its part to be observed or performed, other than as referred to in the above paragraphs, including any covenant, condition or agreement in the Master Indenture applicable to any Obligated Group Member, or will breach any warranty by the Corporation contained in the Loan Agreement, and will fail to cure such breach within 60 days after written notice, specifying such failure or breach and requesting that it be remedied, has been given to the Corporation by the Authority or the Bond Trustee; except that, if such failure or breach can be remedied but not within such 60 day period and if the Corporation has taken all action reasonably possible to remedy such failure or breach within such 60 day period, such failure or breach will not become a Loan Default Event for so long as the Corporation will diligently proceed to remedy such failure or breach in accordance with and subject to any directions or limitations of time established by the Bond Trustee;

(d) If the Corporation files a petition in voluntary bankruptcy, for the composition of its affairs or for its corporate reorganization under any state or federal bankruptcy or insolvency law, or makes an assignment for the benefit of creditors, or admits in writing to its insolvency or inability to pay debts as they mature, or consents in writing to the appointment of a trustee or receiver for itself or for the whole or any substantial part of the Corporation's facilities;

(e) If a court of competent jurisdiction will enter an order, judgment or decree declaring the Corporation an insolvent, or adjudging it bankrupt, or appointing a trustee or receiver of the Corporation or of the whole or any substantial part of the Corporation's facilities, or approving a petition filed against the Corporation seeking reorganization of the Corporation under any applicable law or statute of the United States of America or any state thereof, and such order, judgment or decree will not be vacated or set aside or stayed within 60 days from the date of the entry thereof;

(f) If, under the provisions of any other law for the relief or aid of debtors, any court of competent jurisdiction will assume custody or control of the Corporation's facilities, and such custody or control will not be terminated within 60 days from the date of assumption of such custody or control;

(g) Any Event of Default as defined in and under the Bond Indenture; or

(h) Any Event of Default as defined in and under the Master Indenture.

Remedies on Default.

If a Loan Default Event will occur, then, and in each and every such case during the continuance of such Loan Default Event, the Bond Trustee on behalf of the Authority, subject to the limitations in the Bond Indenture as to the enforcement of remedies, may take such action as it deems necessary or appropriate to collect amounts due

under the Loan Agreement, to enforce performance and observance of any obligation or agreement of the Corporation under the Loan Agreement.

DEED OF TRUST

General

Pursuant to the Deed of Trust, the Corporation grants, transfers and absolutely, unconditionally, and irrevocably assigns to the trustee thereunder (the "Deed Trustee") for the benefit of the Master Trustee, in trust, with power of sale and right of entry and possession, certain of its real property ("Land"), all right, title and interest that the Corporation may hereafter acquire in the Land, together with all of the following, whether presently owned or hereafter acquired:

(a) All buildings, structures, improvements, fixtures, equipment and appurtenances now and hereafter owned, constructed, located, erected, installed or affixed by or on behalf of the Corporation upon or appurtenant to the Land and all replacements and substitutions therefor ("Facilities");

(b) All appurtenances, improvements, easements, pipes, transmission lines or wires and other rights used in connection with the Land or as a means of access thereto, whether now or hereafter owned or constructed or placed upon or in the Land or Facilities ("Appurtenances");

(c) All machinery, equipment, goods and other tangible personal property of the Corporation, whether moveable or not, if the same is (a) now owned or hereafter acquired by the Corporation and (b) now or hereafter located at or used in connection with the Facilities or Appurtenances and all improvements, restorations, replacements, repairs, additions, accessions or substitutions thereto or therefor, including, without limitation, all building materials and supplies, machinery, equipment, material, furnishings and appliances for generation or distribution of air, water, heat, electricity, light, fuel or refrigeration, for purposes of ventilation, sanitation or drainage, for exclusion of vermin or insects, for removal or disposal of dust, refuse or garbage; all elevators, awnings, window coverings, floor covering, cabinets; all fixed equipment now or hereafter installed in the Land or Facilities which are essential elements of the Facilities and are necessary for their operation and use; the products and proceeds from any and all such property; all the estate, interest, right, title, property or other claim or demand of every nature whatsoever, in and to such property, including specifically, but without limitation, all deposits made with or other security given to utility companies by the Corporation with respect to such property and claims or demands relating to insurance or condemnation awards which the Trustor now has or may hereafter acquire ("Equipment");

(d) All leases and subleases of portions of the Land or space in the Facilities ("Leases") and all management agreements, development agreements, construction contracts and architectural agreements ("Project Agreements") with respect to the Land, Facilities, Appurtenances and Equipment;

(e) All rentals or other payments which may now or hereafter accrue or otherwise become payable under the Leases to or for the benefit of the Corporation together with all other income, rents, revenues, issues, profits, reserves, and royalties produced by the Land, Facilities, Appurtenances and Equipment, including but not limited to security deposits (collectively the "Rents");

(f) All earnings, products, damages, indemnifications, insurance proceeds and any other proceeds from any and all of such Land, Facilities, Appurtenances, Equipment, Project Agreements, Leases and Rents including specifically, but without limitation, all deposits made with or other security given to utility companies and claims or demands relating to insurance or condemnation awards which the Corporation now has or may hereafter acquire, including advance payments of insurance premiums made by the Corporation with respect thereto ("Proceeds");

(g) All accounts, accounts receivable and other rights to payment of money or other value now owned or hereafter acquired by the Corporation, whether due or to become due and whether or not earned by performance ("Accounts"), including without limitation the following:

(i) Any and all Accounts arising from any source, including without limitation operations of the Corporation or its agents at the Facilities, and at any other facility or office; and

(ii) Any and all Accounts accruing from the operation of the Corporation's health care facilities, and any other programs run by and operations of the Corporation or its agents. For such purposes, "Accounts" covered hereby include without limitation accounts, chattel paper, deposit accounts and instruments as defined by the California Uniform Commercial Code, and any amounts receivable from third-party payors (including insurance companies, Medicare and Medicaid unless otherwise prohibited by law) in connection with the foregoing;

(h) All right, title and interest of the Corporation in all the Corporation's inventory, raw materials, work in process, finished goods and goods held for sale or furnished under contracts of service, and all returned and repossessed goods, and all goods covered by documents of title, including warehouse receipts, bills of lading and all other documents of every type covering all or any part of the Property (as defined below), now owned or hereafter acquired, whether held by the Corporation or any third party, which is located on, appurtenant to, relating to, or used by or useful in connection with the Property ("Inventory");

(i) All right, title and interest of the Corporation in and to all plans, specifications contracts (including without limitation the architect's contract and the construction contract for the Facilities to be built on the Land), permits, approvals, licenses, rights to develop (including without limitation any and all subdivision approvals, whether preliminary or definitive), site plan approvals, equipment leases, service contracts and agreements, of whatever nature or type, which now or may in the future pertain to, relate to, affect or be used in connection with, the Property, including without limitation any of the foregoing necessary or convenient to the operation, maintenance and management of the Property (hereinafter collectively referred to as the "Approvals"); and

(j) All general intangibles of the Corporation ("Intangibles").

The Deed of Trust secures: (a) payment of the principal, redemption price and purchase price of and premium (if any) and interest on all Obligations now or hereafter issued and Outstanding under the Master Indenture (the "Obligations"), according to their tenor and effect, and payment and performance by the Members of the Obligated Group of all covenants and other obligations expressed or implied in the Obligations; (b) payment and performance of all of the obligations of the Obligated Group under or with respect to the Master Indenture (as subsequently amended or supplemented); (c) payment and performance of the obligations and agreements of the Corporation contained in the Environmental Compliance and Indemnification Agreement; and (d) payment and performance of each and every obligation, covenant and agreement arising under or contained in this Deed of Trust.

Events of Default

Any one or more of the following events constitute an event of default under the Deed of Trust (an "Event of Default"):

(a) failure to pay when due and payable any installment of interest or principal under any Obligation, or in the payment of any other sum which is payable under the Master Indenture or the Deed of Trust, as and when the same shall become due and payable as further described in the Obligation, the Master Indenture or the Deed of Trust; or

(b) the occurrence of an "Event of Default" as defined in the Master Indenture; or

(c) if the Corporation violates a covenant in the Deed of Trust; or

(d) if the Corporation defaults in the due observance or performance of or compliance with any of the provisions, warranties, covenants, promises, agreements, terms or conditions to be observed, performed, or complied with by the Corporation, as contained in the Deed of Trust, other than those referred to in paragraphs (a), (b) and (c) above, and such default continues uncured for a period of fifteen (15) days after written notice thereof to the Corporation from the Master Trustee except that in the case of a default under this paragraph (d) which cannot with

due diligence be cured within such period of fifteen (15) days, the time within which Corporation may cure the same shall be extended for such period as may be reasonably necessary in the Master Trustee's discretion to cure the same with due diligence (but in no event more than 90 days), provided the Corporation commences within such fifteen (15) days, proceeds diligently to cure the same and delivers a report to the Deed Trustee at least once every thirty (30) days setting forth the status of its attempt to cure such Event of Default.

Among other remedies, should an Event of Default have occurred and be continuing, the Deed Trustee, upon written request by the Master Trustee, shall provide and record such notices of default and of the election to cause the Property or any part of it to be sold as are required by law.

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APPENDIX D

FORM OF OPINION OF BOND COUNSEL

October ___, 2007

ABAG Finance Authority for Nonprofit Corporations
Oakland, California

\$60,100,000
ABAG Finance Authority for Nonprofit Corporations
Refunding Revenue Bonds
(Children's Hospital & Research Center at Oakland)
Series 2007A

Ladies and Gentlemen:

We have acted as bond counsel to the ABAG Finance Authority for Nonprofit Corporations (the "Authority") and in such capacity have examined a record of proceedings relating to the issuance of the Authority's \$60,100,000 Refunding Revenue Bonds (Children's Hospital & Research Center at Oakland), Series 2007A (the "Bonds"), dated their date of original execution and delivery (the "Date of the Bonds"). The Bonds are issued under and pursuant to the Joint Exercise of Powers Act, constituting Articles 1 through 4 (commencing with Section 6500) of Chapter 5 of Division 7 of Title 1 of the Government Code of the State of California, as now in effect, and a Bond Indenture, dated as of October 1, 2007 (the "Bond Indenture"), between the Authority and The Bank of New York Trust Company, N.A., as bond trustee (the "Bond Trustee"), for the purpose of providing funds, together with other available funds, to (i) refund in advance of maturity and defease certain outstanding securities, (ii) fund a bond reserve fund, and (iii) pay certain costs and expenses related to the issuance of the Bonds. Capitalized terms not defined herein shall have the meanings assigned to them in the Bond Indenture.

The Bonds bear interest from the Date of the Bonds and are subject to redemption prior to their respective stated maturities in the manner and upon the terms and conditions set forth therein and in the Bond Indenture. The Bonds will be issued as fully registered Bonds in denominations of \$5,000 or any integral multiple thereof and are interchangeable as provided in the Bond Indenture.

The Bonds are secured by, among other things, payments to be made by Children's Hospital & Research Center at Oakland (the "Corporation") under a Loan Agreement (the "Loan Agreement"), dated as of October 1, 2007, between the Authority and the Corporation and delivered to the Authority as evidence of the Corporation's obligation to repay the loan of the proceeds of the Bonds. The Bonds also are secured by Children's Hospital and Research Center at Oakland Obligation No. 1 ("Obligation No. 1"), dated the Date of the Bonds, issued by the Corporation pursuant to the terms of a First Supplemental Master Indenture, dated as of October 1, 2007, between the Corporation, as Obligated Group Representative, and the Master Trustee (referred to below), and a Master Trust Indenture, dated as of October 1, 2007 (the "Master Trust Indenture"), among the Corporation, Children's Hospital & Research Center Foundation (the "Foundation" and, together with the Corporation, the "Obligated Group") and The Bank of New York Trust Company, N.A., as master trustee (the "Master Trustee"). The Authority will assign to the Bond Trustee, for the benefit of bondholders, its right, title and interest in the Loan Agreement (to the extent and as more particularly described in the Bond Indenture) and Obligation No. 1.

The principal or Redemption Price of the Bonds is payable in lawful money of the United States of America at the Principal Corporate Trust Office of the Bond Trustee. The interest on the Bonds is payable through the book-entry system maintained by The Depository Trust Company, New York, New York, or, if the book-entry

system is no longer in effect, in lawful money of the United States of America by check or draft mailed to each Holder at the address shown on the registration books maintained by the Bond Trustee or, at the option of the Holder of at least \$1,000,000 in aggregate principal amount of Bonds, by wire transfer to such address as may have been filed with the Bond Trustee for such purpose.

The Bonds mature December 1 in the years and in the principal amounts, and the Bonds bear interest from the Date of the Bonds, at the following rates per annum:

Maturity Date (December 1)	Principal Amount	Interest Rate
2010	\$ 1,085,000	4.000%
2011	1,130,000	4.000
2012	1,175,000	4.250
2013	1,220,000	4.500
2014	1,275,000	4.500
2015	1,335,000	4.500
2016	1,395,000	4.250
2017	1,455,000	4.750
2018	1,525,000	4.500
2019	1,590,000	4.500
2022	5,235,000	4.750
2027	10,615,000	5.250
2037	31,065,000	5.000

The Loan Agreement and the Bond Indenture and the rights and obligations of the Authority, the Corporation, the Bond Trustee and the registered owners of the Bonds may be amended or modified in the manner and subject to the conditions and terms set forth in the Loan Agreement and the Bond Indenture.

As to questions of fact material to our opinion, we have relied upon the certified proceedings and other certifications of public officials and officials of the Corporation and the other Members of the Obligated Group furnished to us without undertaking to verify the same by independent investigation.

Based upon such examinations, we are of the opinion that:

1. The Bonds have been duly authorized, executed and issued.
2. The Bond Indenture has been duly authorized and executed by the Authority and is valid and binding in accordance with its terms. The Bond Indenture creates a valid pledge, to secure the payment of the principal of and premium, if any, and interest on the Bonds in accordance with their terms and the provisions of the Bond Indenture, of all of the Revenues and any other amounts (including the proceeds of the sale of Bonds) held in any fund or account established pursuant to the Bond Indenture, excepting only any amounts held in the Rebate Fund, subject to the provisions of the Bond Indenture permitting the application thereof for the purposes and on the terms and conditions set forth in the Bond Indenture. The Bond Indenture also creates a valid assignment to the Bond Trustee, for the benefit of the Holders from time to time of the Bonds, of all of the right, title and interest of the Authority in the Loan Agreement (to the extent and as more particularly described in the Bond Indenture) and Obligation No. 1.
3. The Bonds are valid and binding limited obligations of the Authority payable solely from the Revenues and other assets pledged and assigned therefor under the Bond Indenture and are not a lien or charge upon the funds or property of the Authority except to the extent of the aforementioned pledge and assignment. The Bonds shall never constitute the debt or indebtedness of the Authority within the meaning of any provision or limitation of the Constitution of the State of California, and shall not constitute nor give rise to a pecuniary liability of the Authority or a charge against its general credit or taxing powers.

4. The Loan Agreement has been duly authorized and executed by the Authority and the Corporation and is valid and binding in accordance with its terms.
5. Under existing statutes, regulations, rulings and judicial decisions, assuming compliance by the Authority and the Corporation with certain covenants of the Bond Indenture, the Loan Agreement, the Tax Certificate and other documents pertaining to the Bonds and certain requirements of the Internal Revenue Code of 1986, as amended (the "Code"), regarding the organization and operation of the Members of the Obligated Group, the use, expenditure and investment of proceeds of the Bonds and the timely payment of certain investment earnings to the United States, interest on the Bonds is not includable in the gross income of the owners of the Bonds for federal income tax purposes. In rendering the foregoing opinion, we have relied upon the opinion of Hanson, Bridgett, Marcus, Vlahos & Rudy, LLP, San Francisco, California, regarding the qualification of the Members of the Obligated Group as organizations described in Section 501(c)(3) of the Code. We can give no opinion or assurance about the future activities of the Members of the Obligated Group or about the effect of future changes in the Code, applicable regulations, the interpretation thereof or the resulting changes in enforcement thereof by the Internal Revenue Service. Failure to comply with the covenants and requirements described above or failure of one or more Members of the Obligated Group to be organized and operated in accordance with the Internal Revenue Service's requirements for the maintenance of their status as organizations described in Section 501(c)(3) of the Code may cause interest on the Bonds to be includable in gross income for federal income tax purposes retroactively to the date of issuance of the Bonds.
6. Interest on the Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability. We express no opinion regarding other federal income tax consequences caused by the ownership of or the receipt of interest on the Bonds.
7. Under existing law, interest on the Bonds is exempt from State of California personal income taxes.

Certain requirements and procedures contained or referred to in the Bond Indenture or other relevant documents relating to the Bonds may be changed, and certain actions may be taken, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of tax-exempt obligations. We express no opinion as to the exclusion of interest on the Bonds from gross income of the owners of the Bonds for federal income tax purposes on and after the date on which any such change occurs or action is taken upon the advice or approval of counsel other than this firm.

With respect to the opinions expressed herein, the enforceability of the rights and obligations under the Bonds, the Loan Agreement and the Bond Indenture and the liens and security interest described above are subject to bankruptcy, insolvency and other laws affecting creditors' rights generally and to the application of such principles of equity as the court having jurisdiction may impose, regardless of whether such enforceability is considered in a proceeding in equity or at law. We express no opinion with respect to any indemnification, contribution, choice of law, choice of forum or waiver provisions contained in the foregoing documents. Further, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement, dated October 4, 2007, issued in connection with the marketing of the Bonds and express no opinion with respect thereto.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and relate to matters described herein only as the date hereof. Such opinions may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after the date hereof. We have not undertaken to determine, or to inform any person, whether such actions are taken or such events occur, and we have no obligation to update this opinion in light of any such actions or events.

In rendering this opinion, we also have relied upon the opinion of Hanson, Bridgett, Marcus, Vlahos & Rudy, LLP, San Francisco, California, with respect to the authorization, execution and delivery by the Corporation of the Loan Agreement.

Respectfully submitted,

Sidley Austin LLP

APPENDIX E
FORM OF CONTINUING DISCLOSURE AGREEMENT

This Continuing Disclosure Agreement (the “Disclosure Agreement”) is executed and delivered by Children’s Hospital & Research Center at Oakland (the “Corporation”), as Obligated Group Representative, in connection with the issuance of \$60,100,000 ABAG Finance Authority for Nonprofit Corporations Refunding Revenue Bonds (Children’s Hospital & Research Center at Oakland), Series 2007A (the “Bonds”). The Bonds are being executed and delivered pursuant to a Bond Indenture, dated as of October 1, 2007 (the “Bond Indenture”), between ABAG Finance Authority for Nonprofit Corporations (the “Authority”) and The Bank of New York Trust Company, N.A., as trustee. The proceeds of the Bonds are being loaned to the Corporation pursuant to a Loan Agreement, dated as of October 1, 2007 (the “Loan Agreement”), between the Authority and the Corporation. The Corporation's payment obligations pursuant to the Loan Agreement are secured by an Obligation issued pursuant to the Master Trust Indenture, dated as of October 1, 2007 (as supplemented and amended from time to time, the “Master Indenture”), among the Corporation, Children’s Hospital & Research Center Foundation (the “Foundation”) and The Bank of New York Trust Company, N.A., as master trustee.

The Corporation and the Foundation are currently the only Members of the Obligated Group (as defined in the Master Indenture). On behalf of itself and the Foundation, the Corporation hereby covenants and agrees as follows:

SECTION 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered by the Corporation for the benefit of the Holders and Beneficial Owners of the Bonds and in order to assist the Participating Underwriter in complying with S.E.C. Rule 15c2-12(b)(5).

SECTION 2. Definitions. In addition to the definitions set forth in the Bond Indenture, the Loan Agreement and the Master Indenture, which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

“Annual Filing Deadline” shall mean six months after the end of the Obligated Group’s Fiscal Year, commencing with the Fiscal Year ending December 31, 2007.

“Annual Information” means, with respect to each Member of the Obligated Group, the type of financial information and operating data set forth in the text and tables under the headings “FACILITIES AND SERVICES—Utilization of Health Facilities;” “SERVICE AREA, PATIENT ORIGIN AND COMPETITION—Utilization, Market Share Analysis and Competition;” “HISTORIC FINANCIAL INFORMATION—Summarized Consolidated Statements of Operation and Changes in Unrestricted Net Assets,” “—Summarized Consolidated Balance Sheets,” “—Sources of Healthcare Revenue” and “—Other Sources of Revenues;” and “MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL PERFORMANCE—Liquidity and Capital Resources,” “—Capitalization” and “Historical and Proforma Debt Service Coverage” in Appendix A to the final Official Statement, dated September 21, 2007, for the Bonds.

“Annual Report” shall mean any Annual Report provided by the Corporation pursuant to and as described in Sections 3 and 4 of this Disclosure Agreement.

“Audited Financial Statements” means the audited financial statements of the Obligated Group and any other Members of the Obligated Group prepared in conformity with generally accepted accounting principles.

“Beneficial Owner” shall mean any person who (a) has the power, directly or indirectly, to vote or consent with respect to, or to dispose of ownership of any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries) or (b) is treated as the owner of any Bonds for federal income tax purposes.

“Bond Counsel” shall mean a firm of attorneys of national reputation experienced in the field of municipal bonds whose opinions are generally accepted by purchasers of municipal bonds, which is selected by the Corporation.

“Dissemination Agent” shall mean initially The Bank of New York Trust Company, N.A., or any successor Dissemination Agent designated in writing by the Corporation (which may be the Corporation) and which has filed with the Corporation a written acceptance of such designation.

“Fiscal Year” shall mean each fiscal year of the Obligated Group (currently ending December 31) and if and when there are additional Obligated Group Members, such Members’ respective fiscal year.

“Holders” shall mean registered owners of the Bonds.

“Listed Events” shall mean any of the events listed in Section 5(a) of this Disclosure Agreement.

“National Repository” shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule. The National Repositories currently approved by the Securities and Exchange Commission can be found at www.sec.gov/info/municipal/nrmsir.htm.

“Participating Underwriter” shall mean any of the original Underwriter of the Bonds required to comply with the Rule in connection with offering of the Bonds.

“Quarterly Filing Deadline” shall mean two months after the first fiscal quarter, second fiscal quarter and third fiscal quarter of each Fiscal Year, commencing with the fiscal quarter ending December 31, 2007.

“Quarterly Information” shall mean unaudited year to date financial information to consist of a consolidated balance sheet and consolidated change in unrestricted assets, and a calculation of Days Cash on Hand Ratio.

“Quarterly Report” shall mean any Quarterly Report provided by the Corporation pursuant to and as described in Sections 3 and 4 of this Disclosure Agreement

“Repository” shall mean each National Repository and each State Repository.

“Rule” shall mean Rule 15c2-12 adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

“State” shall mean the State of California.

“State Repository” shall mean any public or private repository or entity designated by the State as a state repository for the purpose of the Rule and recognized as such by the Securities and Exchange Commission. As of the date of this Disclosure Agreement, there is no State Repository.

SECTION 3. Provision of Annual Reports and Quarterly Reports.

(a) Unless otherwise permitted by Section 8, the Corporation shall provide, or shall cause the Dissemination Agent to provide, not later than each Annual Filing Deadline, to each Repository an Annual Report consistent with the requirements of Section 4 of this Disclosure Agreement. The Annual Report may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in Section 4 of this Disclosure Agreement; provided that the Audited Financial Statements may be submitted separately from the balance of the Annual Report and later than each Annual Filing Deadline, if they are not available by the Annual Filing Deadline. If the Corporation’s or any other Member’s Fiscal Year changes, the Corporation or such Member, as applicable, shall give notice of such change in the same manner as for a Listed Event under Section 5(c).

(b) Unless otherwise permitted by Section 8, the Corporation shall provide, or shall cause the Dissemination Agent to provide, not later than each Quarterly Filing Deadline, to each Repository a Quarterly Report which complies with the requirements of Section 4 of this Disclosure Agreement. The Quarterly Report may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in Section 4 of this Disclosure Agreement.

(c) Not later than 30 days nor more that 60 days prior to each Annual Filing Deadline and each Quarterly Filing Deadline, the Dissemination Agent shall give notice to the Corporation that the Annual Report or Quarterly Report, as applicable, shall be required to be filed in accordance with the terms of this Disclosure Agreement. Not later than 5 Business Days prior to each Annual Filing Deadline and each Quarterly Filing Deadline, the Corporation shall provide the Annual Report or Quarterly Report, as applicable, in a format suitable for providing to the Repositories, to the Dissemination Agent (if other than the Corporation). If the Corporation is unable to provide to the Repositories an Annual Report by a Annual Filing Deadline or a Quarterly Report by a Quarterly Filing Deadline, the Corporation shall send a notice to each Repository in substantially the form attached as Exhibit A with a copy to the Dissemination Agent. The Dissemination Agent (if other than the Corporation) shall not be required to file any notice of the failure to file an Annual Report or a Quarterly Report.

(d) The Dissemination Agent (if other than the Corporation) shall file a report with the Corporation stating it has filed the Annual Report or the Quarterly Report, as applicable, in accordance with its obligations hereunder, stating the date it was provided and listing all the Repositories to which it was provided.

SECTION 4. Content of Annual Reports and Quarterly Reports.

(a) The Annual Report shall contain or include by reference the following:

1. The Audited Financial Statements for the prior Fiscal Year. If the Audited Financial Statements are not available by the Annual Filing Deadline, the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the Official Statement, and the Audited Financial Statements shall be filed in the same manner as the Annual Report when they become available; and

2. Annual Information for the preceding Fiscal Year.

(b) The Quarterly Report shall contain the Quarterly Information for the first fiscal quarter, the second fiscal quarter or the third fiscal quarter, as applicable.

Any or all of the items listed above in subsection (a) or (b) may be included by specific reference to other documents, including official statements of debt issues of the Obligated Group or related public entities, that have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The Corporation shall clearly identify each such other document so included by reference.

SECTION 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the Corporation shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

1. principal and interest payment delinquencies;
2. non-payment related defaults;
3. modifications to rights of Holders;
4. optional, contingent or unscheduled bond calls;
5. defeasances;
6. rating changes;
7. adverse tax opinions or events affecting the tax-exempt status of the Bonds;
8. unscheduled draws on the debt service reserves reflecting financial difficulties;
9. unscheduled draws on any credit enhancement reflecting financial difficulties;
10. substitution of the credit or liquidity providers or their failure to perform; or
11. release, substitution or sale of property securing repayment of the Bonds.

(b) Whenever the Corporation obtains knowledge of the occurrence of a Listed Event, the Corporation shall as soon as possible determine if such event would be material under applicable federal securities laws.

(c) If the Corporation determines that knowledge of the occurrence of a Listed Event would be material under applicable federal securities laws, the Corporation shall promptly file a notice of such occurrence with the Repositories or provide notice of such reportable event to the Dissemination Agent in format suitable for filing with the Repositories. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(4) and (5) above need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to Holders of affected Bonds pursuant to the Bond Indenture. The Dissemination Agent (if other than the Corporation) shall have no duty to independently prepare or file any report of Listed Events. The Dissemination Agent may conclusively rely on the Corporation's determination of materiality pursuant to Section 5(b).

SECTION 6. Termination of Reporting Obligation. The Corporation's obligations under this Disclosure Agreement shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the Corporation shall give notice of such termination in the same manner as for a Listed Event under Section 5(a).

SECTION 7. Dissemination Agent. The Corporation may, from time to time, appoint or engage a Dissemination Agent (or substitute Dissemination Agent) to assist it in carrying out its obligations under this Disclosure Agreement, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. A Dissemination Agent that is not the Corporation may resign upon 15 days written notice to the Corporation. Upon such resignation, the Corporation shall act as its own Dissemination Agent until it appoints a successor. Any Dissemination Agent appointed by the Corporation shall not be responsible in any manner for the content of any notice or report prepared by the Corporation pursuant to this Disclosure Agreement and shall not be responsible to verify the accuracy, completeness or materiality of any continuing disclosure information provided by

the Corporation. The Corporation shall compensate the Dissemination Agent for its fees and expenses hereunder as agreed by the parties. Any entity succeeding to all or substantially all of the Dissemination Agent's corporate trust business shall be the successor Dissemination Agent without the execution or filing of any paper or further act.

SECTION 8. Alternate Means of Disclosure. Notwithstanding the provisions of Sections 3, 4 and 5 requiring that the Corporation file its Annual Report, notice of any Material Event and notice of any failure to comply with this Disclosure Agreement with each of the National Repositories and any State Repository, the Corporation may instead comply with the provisions of this Disclosure Agreement by filing the required information with an entity recognized, as of the time of any filing hereunder, by the Securities and Exchange Commission as eligible to receive filings under Rule 15c2-12 (a "Central Post Office") and submit such filings to such Central Post Office. Prior to any filing with a Central Post Office, the Corporation shall determine the current Central Post Office. As of the date of this Disclosure Agreement, the Central Post Office that has been so recognized by the Securities and Exchange Commission is:

DisclosureUSA.org
P.O. Box 684667
Austin, Texas 78768-4667
Fax: (512) 476-6403
<http://www.disclosureUSA.org>

SECTION 9. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Agreement, the Corporation may amend this Disclosure Agreement, and any provision of this Disclosure Agreement may be waived, provided that the Corporation first obtains an opinion of Bond Counsel that such amendment or waiver is permitted under the Rule.

In the event of any amendment or waiver of a provision of this Disclosure Agreement, the Corporation shall describe such amendment in the next Annual Report.

SECTION 10. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the Corporation from disseminating any other information, using the means of dissemination set forth in this Disclosure Agreement or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Agreement. If the Corporation chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Agreement, the Corporation shall have no obligation under this Disclosure Agreement to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

SECTION 11. Default. In the event of a failure of the Corporation to comply with any provision of this Disclosure Agreement, the sole remedy hereunder of any Holder or Beneficial Owner of the Bonds shall be any actions as may be necessary and appropriate to compel performance, including seeking mandate or specific performance by court order, to cause the Corporation to comply with its obligations under this Disclosure Agreement. A default under this Disclosure Agreement shall not be deemed an event of default under the Master Indenture, including the Supplemental Master Indenture of Trust for Obligation No. 1, the Bonds, the Bond Indenture, the Loan Agreement or any agreement entered into by any Obligated Group Member in connection with the execution and delivery of the Bonds.

SECTION 12. Duties, Immunities and Liabilities of Dissemination Agent. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Agreement. The Dissemination Agent (if other than the Corporation) acts hereunder solely for the benefit of the Corporation; this Disclosure Agreement shall confer no duties on the Dissemination Agent to the Participating Underwriter, the Holders and the Beneficial Owners. The Corporation agrees to indemnify and save the Dissemination Agent (if other than the Corporation), its officers, directors, employees and agents, harmless against any loss, expense and liabilities which it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's gross negligence or willful misconduct. The obligations of the Corporation under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds. The Dissemination Agent (if other than the Corporation) shall have no liability for the failure to report any event or any

financial information as to which the Corporation has not provided an information report in format suitable for filing with the Repositories. The Dissemination Agent (if other than the Corporation) shall not be required to monitor or enforce the Corporation's duty to comply with its continuing disclosure requirements hereunder.

SECTION 13. Beneficiaries. This Disclosure Agreement shall inure solely to the benefit of the Corporation, the Dissemination Agent, the Participating Underwriter and Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity.

Date: As of October 1, 2007

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND, as Obligated Group Representative

By: _____
Its: Chief Financial Officer

ACCEPTED AND AGREED TO BY:
THE BANK OF NEW YORK TRUST COMPANY, N.A.,
as Dissemination Agent

By: _____
Authorized Officer

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APPENDIX F

Book-Entry Only System

The information provided in this APPENDIX F has been provided by DTC. No representation is made by the Authority, the Underwriter, the Trustee or the Corporation as to the accuracy or adequacy of such information provided by DTC or as to the absence of material adverse changes in such information subsequent to the date of this Official Statement.

The Depository Trust Company (“DTC”), New York, New York, will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully registered bond certificate will be issued for the Bonds, in the principal amount of such Bonds, and will be deposited with DTC.

DTC, the world’s largest depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Bonds under the Book-Entry System must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Series 2007 Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the Book-Entry System for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co. or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of the Bonds may wish to take certain steps to augment transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to security documents. For example, Beneficial Owners of the Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners, or in the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of the notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in the Bonds to be redeemed.

Neither DTC nor Cede & Co. (nor such other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Bond Trustee as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Bonds will be made to Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts, upon DTC's receipt of funds and corresponding detail information from the Authority or the Bond Trustee on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Bond Trustee, the Authority or the Borrower, subject to any statutory or regulatory requirements as may be in effect from time to time. Payments of principal and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) are the responsibility of the Bond Trustee, disbursement of such payments to Direct Participants is the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

A Beneficial Owner shall give notice to elect to have its Bonds purchased or tendered, through its Participant, to the Bond Trustee, and shall effect delivery of such Bonds by causing the Direct Participant to transfer the Participant's interest in the Bonds, on DTC's records, to the Bond Trustee. The requirement for physical delivery of Bonds in connection with an optional tender or a mandatory purchase will be deemed satisfied when the ownership rights in the Bonds are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered Bonds to the Bond Trustee's DTC's account.

DTC may discontinue providing its services as securities depository with respect to Bonds at any time by giving notice to the Authority and the Bond Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, bond certificates will be printed and delivered to DTC.

While the Bonds are in the Book-Entry System, reference in this Official Statement to owners of such Bonds should be read to include any person for whom a Participant acquires an interest in the Bonds, but (i) all rights of ownership, as described herein, must be exercised through DTC and the Book-Entry System and (ii) notices that are to be given to registered owners by the Bond Trustee will be given only to DTC. DTC is required to forward (or cause to be forwarded) the notices to the Participants by its usual procedures so that such Participants may forward (or cause to be forwarded) such notices to the Beneficial Owners.

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