TRIAD HOSPITALS INC
Form 10-K/A
December 12, 2003
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

AMENDMENT NO. 1

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2002

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 0-29816

Triad Hospitals, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	75-2816101 (I.R.S. Employer Identification No.)
5800 Tennyson Parkway	
Plano, Texas (Address of principal executive offices)	75024 (Zip Code)

(214) 473-7000

(Registrant s telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act: None

Securities Registered Pursuant to Section 12(g) of the Act:

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
Common Stock, $.01 Par Value	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. YES x NO ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. YES ¨ NO x

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of the latest practical date.

As of March 14, 2003, the number of shares of common stock of Triad Hospitals, Inc. outstanding was 74,959,628. As of March 14, 2003 the aggregate market value of the common stock held by non-affiliates was approximately $1,714,127,260. For purposes of the foregoing calculation, the Registrant s directors, executive officers, and the Triad Hospitals, Inc. Retirement Savings Plan have been deemed to be affiliates.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). YES x NO ¨

At June 30, 2002, the aggregate market value of the common stock held by non-affiliates was approximately $2,975,079,285. For purposes of the foregoing calculation, the Registrant s directors, executive officers, and the Triad Hospitals, Inc. Retirement Savings Plan have been deemed to be affiliates.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for the 2003 Annual Meeting of Stockholders of Triad Hospitals, Inc. are incorporated by reference into Part III hereof.

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Explanatory Note

This Form 10-K/A constitutes amendment no. 1 to the Triad Hospitals, Inc. annual report on Form 10-K for the fiscal year ended December 31, 2002. This amendment no. 1 is being filed solely to correct a typographical error contained in Note 7 of the Consolidated Financial Statements set forth in the annual report on Form 10-K. The references to unaudited in Note 7 - Long Term Debt with respect to the audited condensed consolidating financial statements of Triad Hospitals, Inc. (parent only), its combined guarantor subsidiaries and its combined non-guarantor subsidiaries were inadvertently included in the annual report on Form 10-K and such references to unaudited have been omitted in Note 7 of the Consolidated Financial Statements filed with this amendment no. 1 on Form 10-K/A. All other information in the annual report on Form 10-K remains unchanged from the original filing.

Item 8. Financial Statements and Supplementary Data

Information with respect to this Item 8 is contained in Triad s consolidated financial statements as indicated in the Index on page F-1 of this amendment No. 1 to the annual report on Form 10-K/A.

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) Documents filed as part of the report:

1. Financial Statements The accompanying index to financial statements on page F-1 of this amendment no. 1 to the annual report on Form 10-K/A is provided in response to this item.

2. List of Financial Statement Schedules All schedules are omitted because the required information is not present, not present in material amounts or presented within the financial statements.

3. List of Exhibits

(a) Exhibits

Exhibit No.	Description
2.1	Distribution Agreement dated May 11, 1999 by and among Columbia/HCA, Triad Hospitals, Inc. and LifePoint Hospitals, Inc., incorporated by reference from Exhibit 2.1 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
2.2	Agreement and Plan of Merger, dated as of October 18, 2000, by and between Quorum Health Group, Inc. and Triad Hospitals, Inc. (the Merger Agreement), incorporated by reference from Triad Hospitals Current Report on Form 8-K dated October 18, 2000.
3.1	

Certificate of Incorporation of Triad, as amended as of April 27, 2001, incorporated by reference from Exhibit 3.1 to Triad Hospitals Post Effective Amendment No. 1 on Form S-8 to the Registration Statement Form S-4.

3.2 Bylaws of Triad Hospitals as amended February 18, 2000 incorporated by reference from Triad Hospitals Annual Report on Form 10-K for the year ended December 31, 2000.

3.3 Certificate of Incorporation of Triad Holdings, incorporated by reference from Triad Hospitals Annual Report on Form 10-K for the year ended December 31, 1999.

3.4 Bylaws of Triad Holdings, incorporated by reference from Triad Hospitals Annual Report on Form 10-K for the year ended December 31, 1999.

4.1 Indenture (including form of 11 % Senior Subordinated Notes due 2009) dated as of May 11, 1999, between Healthtrust and Citibank, N.A. as Trustee, incorporated by reference from Exhibit 4.2(a) to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.

4.2 Registration Rights Agreement dated as of May 11, 1999 between Healthtrust and the Initial Purchasers named therein, incorporated by reference from Exhibit 4.4(a) to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.

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4.3	Triad Assumption Agreement dated May 11, 1999 between Healthtrust and Triad Hospitals, incorporated by reference from Exhibit 4.4(b) to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
4.4	Holdings Assumption Agreement dated May 11, 1999 between Triad Hospitals, Inc. and Triad Holdings, incorporated by reference from Exhibit 4.4(c) to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
4.5	Guarantor Assumption Agreements dated May 11, 1999 between Triad Holdings and the Guarantors signatory thereto, incorporated by reference from Exhibit 4.4(d) to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
4.6	Indenture (including form of 8 3/4% Senior Notes due 2009) dated as of April 27, 2001, among Triad, the guarantors named therein and Citibank, N.A. as Trustee, incorporated herein by reference from Exhibit 4.1 to Triad s Quarterly Report on Form 10-Q, for the quarter ended March 31, 2001.
4.7	Registration Rights Agreement dated as of April 27, 2001 among Triad, the guarantors named therein and the Initial Purchasers named therein, incorporated herein by reference from Exhibit 4.2 to Triad s Quarterly Report on Form 10-Q for the quarter ended March 31, 2001.
10.1	Tax Sharing and Indemnification Agreement, dated May 11, 1999, by and among Columbia/HCA, LifePoint Hospitals and Triad Hospitals, incorporated by reference from Exhibit 10.1 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.2	Benefits and Employment Matters Agreement, dated May 11, 1999 by and among Columbia/HCA, LifePoint Hospitals and Triad Hospitals, incorporated by reference from Exhibit 10.2 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.3	Insurance Allocation and Administration Agreement, dated May 11, 1999, by and among Columbia/HCA, LifePoint Hospitals and Triad Hospitals, incorporated by reference from Exhibit 10.3 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.4	Computer and Data Processing Services Agreement dated May 11, 1999 by and between Columbia Information Systems, Inc. and Triad Hospitals, incorporated by reference from Exhibit 10.5 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.5	Agreement to Share Telecommunications Services dated May 11, 1999 by and between Columbia Information Systems, Inc. and Triad Hospitals, incorporated by reference from Exhibit 10.6 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.6	Triad Hospitals, Inc. 1999 Long-Term Incentive Plan, as amended on May 29, 2001, incorporated by reference from Exhibit 10.4 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended June 30, 2001.
10.7	Triad Hospitals, Inc. Executive Stock Purchase Plan, incorporated by reference from Exhibit 10.11 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.8	Triad Hospitals, Inc. Management Stock Purchase Plan, incorporated by reference from Exhibit 10.12 to Triad Hospitals Quarterly Report on Form 10-Q, for the quarter ended March 31, 1999.
10.9	Triad Hospitals, Inc. Outside Directors Stock and Incentive Compensation Plan, as amended, incorporated by reference from Exhibit B to Triad Hospitals definitive Proxy Statement on Schedule 14A of Triad s annual meeting held on May 29, 2001.
10.10	Credit Agreement dated as of April 27, 2001 among Triad, the Lenders party thereto, Merrill Lynch & Co. and Banc of America Securities LLC as co-lead arrangers, Merrill Lynch & Co. as syndication agent and Bank of America, N.A. as administrative agent, incorporated herein by reference from Exhibit 10.1 on Form 10-Q for the quarter ended March 31, 2001.
10.11	Amendment No. 1 dated as of July 10, 2001 to the Credit Agreement dated as of April 27, 2001 among Triad, the Lenders party thereto, Merrill Lynch & Co. as syndication agent and Bank of America, N.A. as administrative agent, incorporated herein by reference from Exhibit 10.2 on Form 10-Q for the quarter ended June 30, 2001.

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10.12	Amendment No. 2 dated as of August 8, 2001 to the Credit Agreement dated as of April 27, 2001 among Triad, the Lenders party thereto, Merrill Lynch & Co. as syndication agent and Bank of America, N.A. as administrative agent, incorporated herein by reference from Exhibit 10.3 on Form 10-Q for the quarter ended June 30, 2001.
10.13	Amendment No. 3 dated as of February 7, 2002 to the Credit Agreement dated as of April 27, 2001 among Triad, the Lenders party thereto, Merrill Lynch & Co. as syndication agent and Bank of America, N.A., incorporated herein by reference from Exhibit 10.21 on Form 10-K for the year ended December 31, 2001.
10.14	Quorum Health Group, Inc. 1997 Stock Option Plan, incorporated herein by reference from Exhibit B to Quorum s definitive Proxy Statement on Schedule 14A for Quorum s annual meeting held on November 10, 1997.
10.15	Amendment No. 4 dated as of June 28, 2002 to the Credit Agreement dated as of April 27, 2001 among Triad, the Lenders party thereto, Merrill Lynch & Co. as syndication agent and Bank of America, N.A. as administrative agent, incorporated herein by reference from Exhibit 10.1 on Form 10-Q for the quarter ended June 30, 2002.
12.1	Statement of Computation of Ratio of Earnings to Fixed Charges.*
21.1	List of the Subsidiaries of Triad Hospitals.*
23.1	Consent of Ernst & Young LLP.**
31.1	Certification of James D. Shelton, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. **
31.2	Certification of Burke W. Whitman, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. **
32.1	Certification of James D. Shelton, Chief Executive Officer, pursuant to 18 U.S.C. Section 1350. ***
32.2	Certification of Burke W. Whitman, Chief Financial Officer, pursuant to 18 U.S.C. Section 1350. ***
99.1	Certification of James D. Shelton, Chief Executive Officer, pursuant to 18 U.S.C. Section 1350.*
99.2	Certification of Burke W. Whitman, Chief Financial Officer, pursuant to 18 U.S.C. Section 1350.*

* Previously filed on March 27, 2003 with the Annual Report on Form 10-K of Triad Hospitals, Inc. for the fiscal year ended December 31, 2002.

** Filed herewith.

*** Furnished herewith.

(b) Reports on Form 8-K filed during the quarter ended December 31, 2002:

On October 22, 2002, Triad reported that it had issued a press release of its third quarter earnings.

On November l, 2002, Triad reported that a company not affiliated with Triad erroneously filed a current report on Form 8-K using the Electronic Data Gathering, Analysis and Retrieval access codes for Triad.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Triad Hospitals, Inc.
By: /s/ JAMES D. SHELTON

James D. Shelton
Chairman, President and Chief Executive Officer

Dated: December 12, 2003

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Report of Independent Auditors

To the Board of Directors and Stockholders

Triad Hospitals, Inc.

We have audited the accompanying consolidated balance sheets of Triad Hospitals, Inc. as of December 31, 2002 and 2001 and the related consolidated statements of operations, equity and cash flows for each of the three years in the period ended December 31, 2002. These consolidated financial statements are the responsibility of management of Triad Hospitals, Inc. (the Company). Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Triad Hospitals, Inc. at December 31, 2002 and 2001 and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2002 in conformity with accounting principles generally accepted in the United States.

As discussed in Note 1 to the financial statements, the Company changed its method of accounting for goodwill.

/s/ ERNST & YOUNG, LLP

Dallas, Texas

February 7, 2003

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TRIAD HOSPITALS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE YEARS ENDED DECEMBER 31 2002, 2001 AND 2000

(Dollars in millions, except per share amounts)

	2002	2001	2000
Revenues	$ 3,541.1	$ 2,669.5	$ 1,235.5
Salaries and benefits	1,488.4	1,128.5	511.1
Reimbursable expenses	59.0	41.6	
Supplies	546.8	411.2	185.6
Other operating expenses	647.0	501.7	259.8
Provision for doubtful accounts	272.8	239.9	103.6
Depreciation	161.4	134.4	76.1
Amortization	6.0	35.7	7.1
Interest expense, net of capitalized interest of $4.6 and $4.6 for the years ended December 31, 2002 and 2001, respectively	136.7	127.6	62.2
Interest income	(1.7)	(1.6)	(4.9)
ESOP expense	10.8	9.3	7.1
Litigation settlements	(10.4)		
Gain on sales of assets	(4.5)	(23.1)	(7.9)
Impairments of long-lived assets		23.1	8.0
	3,312.3	2,628.3	1,207.8
Income from operations before minority interests, equity in earnings (loss) and income tax provision	228.8	41.2	27.7
Minority interests in earnings of consolidated entities	(14.8)	(7.2)	(9.0)
Equity in earnings (loss) of affiliates	21.7	14.5	(1.4)
Income from operations before income tax provision	235.7	48.5	17.3
Income tax provision	(94.2)	(42.5)	(12.9)
Income from operations	141.5	6.0	4.4
Extraordinary loss on retirement of debt, net of income tax benefit of $2.0 in 2001		(3.2)	
Net income	$ 141.5	$ 2.8	$ 4.4
Income per common share:			
Basic:			
Operations	$ 1.97	$ 0.10	$ 0.14
Extraordinary loss on retirement of debt		(0.06)	
Net	$ 1.97	$ 0.04	$ 0.14
Diluted:			
Operations	$ 1.89	$ 0.10	$ 0.13

Extraordinary loss on retirement of debt		(0.05)	
Net	$ 1.89	$ 0.05	$ 0.13

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

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TRIAD HOSPITALS, INC.

CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2002 AND 2001

(Dollars in millions)

	2002	2001
ASSETS		
Current assets:		
Cash and cash equivalents	$ 68.3	$ 16.3
Restricted cash		5.7
Accounts receivable, less allowances for doubtful accounts of $174.4 and $192.4 at December 31, 2002 and 2001, respectively	507.4	446.6
Inventories	95.5	82.2
Deferred income taxes	62.3	103.1
Prepaid expenses	36.6	23.2
Other	74.3	70.2
	844.4	747.3
Property and equipment, at cost:		
Land	171.5	126.4
Buildings and improvements	1,340.6	1,173.4
Equipment	1,150.8	998.1
Construction in progress (estimated cost to complete and equip after December 31, 2002 $205.8 million)	79.6	175.8
	2,742.5	2,473.7
Accumulated depreciation	(787.3)	(656.7)
	1,955.2	1,817.0
Goodwill	1,224.0	1,215.2
Intangible assets, net of accumulated amortization	72.0	80.6
Investment in and advances to affiliates	179.7	189.4
Other	106.3	115.8
Total assets	$ 4,381.6	$ 4,165.3
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$ 132.5	$ 122.4
Accrued salaries	107.6	80.0
Current portion of long-term debt	73.1	30.9
Other current liabilities	132.0	133.0
	445.2	366.3
Long-term debt	1,618.9	1,742.9
Other liabilities	86.6	68.4
Deferred taxes	151.1	132.1
Minority interests in equity of consolidated entities	125.3	124.1

Commitments and contingencies		
Stockholders equity:		
Common stock .01 par value: 120,000,000 shares authorized, 74,937,635 and 72,202,736 shares issued and outstanding at December 31, 2002 and 2001, respectively	0.7	0.7
Additional paid-in capital	1,883.5	1,810.2
Unearned ESOP compensation and stockholder notes receivable	(20.7)	(32.9)
Accumulated other comprehensive loss	(4.0)	
Accumulated earnings (deficit)	95.0	(46.5)
Total stockholders equity	1,954.5	1,731.5
Total liabilities and stockholders equity	$ 4,381.6	$ 4,165.3

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

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TRIAD HOSPITALS, INC.

CONSOLIDATED STATEMENTS OF EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

(Dollars in millions)

	Common Stock		Additional Paid-in	Unearned ESOP Compensation and Stockholder	Accumulated Other	Accumulated	Total
	Shares	Amount	Capital	Notes Receivable	Comprehensive Loss	Earnings (Deficit)	Stockholders Equity
Balance January 1, 2000	33,943,282	$ 0.3	$ 653.4	$ (40.1)	$	$ (53.7)	$ 559.9
Issuance of common stock under employee plans	219,609		2.8				2.8
Stock options exercised	620,925	0.1	7.0				7.1
Income tax benefit from stock options exercised			(1.1)				(1.1)
ESOP compensation earned			3.7	3.4			7.1
Stock compensation expense			0.9				0.9
Spin-off transactions with HCA			(7.4)				(7.4)
Net income						4.4	4.4
Balance December 31, 2000	34,783,816	0.4	659.3	(36.7)		(49.3)	573.7
Issuance of common stock under employee plans	244,252		5.4				5.4
Stock options exercised	1,388,288		21.6				21.6
Income tax benefit from stock options exercised			11.8				11.8
Issuance of common stock for Quorum acquisition	35,786,380	0.3	1,069.2				1,069.5
Fair value of converted options			31.4				31.4
ESOP compensation earned			5.9	3.4			9.3
Stock compensation expense			5.6				5.6
Repayment of Executive Stock Purchase Plan loan				0.4			0.4
Net income						2.8	2.8
Balance December 31, 2001	72,202,736	0.7	1,810.2	(32.9)		(46.5)	1,731.5
Net income						141.5	141.5
Net change in fair value of interest rate swaps, net of income tax benefit of $2.4 million					(4.0)		(4.0)
Comprehensive income							137.5

Issuance of common stock under employees plans	371,700		9.1				9.1
Stock options exercised	2,363,199		33.3				33.3
Income tax benefit from stock options exercised			21.8				21.8
ESOP compensation earned			7.3	3.5			10.8
Stock compensation expense			0.4				0.4
Repayment of Executive Stock Purchase Plan loans			1.4	8.7			10.1
Balance at December 31, 2002	74,937,635	$ 0.7	$ 1,883.5	$ (20.7)	$ (4.0)	$ 95.0	$ 1,954.5

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

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TRIAD HOSPITALS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

(Dollars in millions)

	2002	2001	2000
Cash flows from operating activities:			
Net income	$ 141.5	$ 2.8	$ 4.4
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for doubtful accounts	272.8	239.9	103.6
Depreciation and amortization	167.4	170.1	83.2
ESOP expense	10.8	9.3	7.1
Minority interests	14.8	7.2	9.0
Equity in (earnings) loss of affiliates	(21.7)	(14.5)	1.4
Gain on sales of assets	(4.5)	(23.1)	(7.9)
Deferred income tax provision	83.7	39.6	11.8
Impairment of long-lived assets		23.1	8.0
Non-cash interest expense	9.0	10.3	1.0
Non-cash stock option expense	0.4	5.6	0.9
Extraordinary loss on retirement of debt, net of tax		3.2	
Increase (decrease) in cash from operating assets and liabilities (net of acquisitions):			
Accounts receivable	(332.7)	(193.2)	(116.9)
Inventories and other assets	(23.1)	13.3	(22.0)
Accounts payable and other current liabilities	18.2	25.0	(19.9)
Other	21.7	(0.3)	7.9
Net cash provided by operating activities	358.3	318.3	71.6
Cash flows from investing activities:			
Purchases of property and equipment	(296.6)	(200.6)	(94.4)
Distributions and advances from affiliates	31.7	17.7	22.7
Proceeds received on sale of assets	6.8	127.8	20.7
Acquisitions, net of cash acquired of $(8.3) million and $(0.4) million in the years ended December 31, 2001 and 2000, respectively	(10.1)	(1,386.6)	(118.8)
Restricted cash	5.7	(5.7)	
Other	0.7	(5.7)	(1.6)
Net cash used in investing activities	(261.8)	(1,453.1)	(171.4)
Cash flows from financing activities:			
Payments of long-term debt	(83.8)	(581.6)	(17.5)
Proceeds from long-term debt		1,752.7	51.0
Payment of debt issue costs	(1.5)	(45.8)	(1.5)
Proceeds from issuance of common stock	42.4	27.0	9.9
Proceeds from executive stock purchase plan loans	10.1		
Distributions to minority partners	(11.7)	(7.9)	(6.3)
Net cash provided by (used in) financing activities	(44.5)	1,144.4	35.6

Change in cash and cash equivalents	52.0	9.6	(64.2)
Cash and cash equivalents at beginning of period	16.3	6.7	70.9
Cash and cash equivalents at end of period	$ 68.3	$ 16.3	$ 6.7
Cash paid for:			
Interest	$ 132.2	$ 112.9	$ 60.5
Income taxes, net of refunds	$ 12.5	$ 5.0	$ 2.6

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

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES

Reporting Entity

Triad Hospitals, Inc. (Triad) is a holding company whose affiliates own 49 general, acute care hospitals and 14 ambulatory surgery centers located in the states of Alabama, Arizona, Arkansas, California, Indiana, Kansas, Louisiana, Mississippi, Missouri, Nevada, New Mexico, Ohio, Oklahoma, Oregon, South Carolina, Texas and West Virginia. Included among these facilities is one hospital operated through a 50/50 joint venture that is not consolidated for financial reporting purposes, one hospital under construction and two hospitals that are leased to third parties. Triad is also a minority investor in three joint ventures that own six general, acute care hospitals in Georgia and Nevada. On April 27, 2001, Triad completed the merger of Quorum Health Group, Inc. (Quorum) with and into Triad (see NOTE 2).

Principles of Consolidation

The consolidated financial statements include the accounts of Triad and all affiliated subsidiaries and entities controlled by Triad through Triad s direct or indirect ownership of a majority voting interest. All material intercompany transactions have been eliminated. Investments in entities which Triad does not control, but in which it has a substantial ownership interest and can exercise significant influence, are accounted for using the equity method.

Use of Estimates

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassification

Certain prior year amounts have been reclassified to conform to the current presentation.

Equity

On May 11, 1999, HCA, Inc. (HCA) completed the spin-off of Triad to its shareholders by a pro rata distribution of common stock in Triad. Equity for the year ended December 31, 2000 includes certain post spin-off related settlements with HCA.

Revenues

Triad s health care facilities have entered into agreements with third-party payers, including government programs and managed care health plans, under which the facilities are paid based upon several methodologies including established charges, the cost of providing services, predetermined rates per diagnosis, fixed per diem rates or discounts from established charges.

Revenues are recorded at estimated net amounts due from patients, third-party payers and others for health care services provided. Settlements under reimbursement agreements with third-party payers are estimated and recorded in the period the related services are rendered and are adjusted in future periods as adjustments become known or as the service years are no longer subject to audit, review or investigation. Laws and regulations governing the Medicare and Medicaid programs are extremely complex, subject to interpretation and are routinely modified for provider reimbursement. All hospitals participating in the Medicare and Medicaid programs are required to meet certain financial reporting requirements. Federal regulations require submission of annual cost reports covering

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES (continued)

medical costs and expenses associated with the services provided by each hospital to program beneficiaries. Annual cost reports required under the Medicare and Medicaid programs are subject to routine audits, which may result in adjustments to the amounts ultimately determined to be due to Triad under these reimbursement programs. These audits often require several years to reach the final determination of amounts earned under the programs. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The net adjustments to estimated settlements resulted in increases to revenues of $8.5 million, $5.5 million and $8.6 million for the years ended December 31, 2002, 2001, and 2000, respectively.

In association with ongoing federal investigations into certain of HCA s business practices (see NOTE 16), applicable governmental agencies ceased the settlement of cost reports. On March 28, 2002, HCA announced that it had reached an understanding with the Centers for Medicare and Medicaid Services (CMS) to resolve all Medicare cost reports for cost reporting periods ended on or before July 31, 2001. The understanding with CMS is subject to approval by the U.S. Department of Justice (the DOJ), which has not yet been obtained, and execution of a definitive written agreement. The understanding with CMS does not include resolution of the outstanding civil issues with the DOJ and relators with respect to cost reports and physician relations. On December 18, 2002, HCA announced that it had reached an understanding with the DOJ to settle the DOJ s outstanding civil cases with respect to cost reports and physician relations, subject to approval by senior officials at the DOJ, the approval by the DOJ of the settlement with CMS, execution of definitive settlement documents and court approval. Due to the cost reports not yet being finally settled, Triad is not receiving all of the updated information which has historically been the basis used to adjust estimated settlement amounts. At this time, Triad cannot predict when, or if, the historical cost report settlement process will be completed. Management believes that adequate provisions have been made for adjustments that may result from final determination of amounts earned under these programs. The estimated net cost report settlements as of December 31, 2002 and 2001 of approximately $9.3 million and $34.8 million, respectively, are included as a reduction to accounts receivable in the accompanying balance sheet. In connection with the spin-off from HCA (see NOTE 15), HCA agreed to indemnify Triad for any payments which it is required to make in respect of Medicare, Medicaid and Blue Cross cost reports relating to periods ending on or prior to the spin-off, and Triad agreed to indemnify HCA for and pay to HCA any payments received by it relating to such cost reports relating to periods ending on or prior to the spin-off. Triad will be responsible for the filing of these cost reports and any terminating cost reports. Triad has recorded a net receivable from HCA relating to the indemnification of $23.7 million and $24.2 million as of December 31, 2002 and 2001, respectively.

Triad provides care without charge to patients who are financially unable to pay for the health care services they receive. Because Triad does not pursue collection of amounts determined to qualify as charity care, they are not reported in revenues.

Cash and Cash Equivalents

Cash equivalents consist of all investments with an original maturity of three months or less.

Restricted Cash

Restricted cash consisted of cash funded to an escrow account for the purpose of satisfying deductibles under Triad s general and professional liability risk policy.

Accounts Receivable

Accounts receivable are recorded at the estimated net realizable amounts from federal and state agencies (under the Medicare, Medicaid and TRICARE programs), managed care health plans, commercial insurance companies, employers and patients. During the years ended December 31, 2002, 2001 and 2000, approximately

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES (continued)

32.0%, 32.2% and 29.6%, respectively, of Triad s revenues related to patients participating in the Medicare program. Triad recognizes that revenues and receivables from government agencies are significant to its operations, but it does not believe that there are significant credit risks associated with these government agencies. During the years ended December 31, 2002, 2001 and 2000 approximately 39.3%, 35.9% and 31.0%, respectively, of Triad s revenues related to patients in various managed care plans. Approximately half of Triad s facilities are located in the states of Alabama, Indiana, and Texas. Triad does not believe that there are any other significant concentrations of revenues from any particular payer or geographic area that would subject it to any significant credit risks in the collection of its accounts receivable.

Triad maintains allowances for doubtful accounts for estimated losses resulting from payers inability to make payments on accounts. Triad estimates these allowances based on historical net write offs of uncollectible accounts. Triad s policy is to write off accounts after all collection efforts have failed, typically no longer than one year after date of discharge. If payers ability to pay deteriorates, additional allowances may be required.

Inventories

Inventories of supplies are stated at the lower of cost (first-in, first-out) or market.

Property, Equipment , and Other Amortizable Intangible Assets

Property and equipment are stated at the lower of cost or market. Routine maintenance and repairs are charged to expense as incurred. Expenditures that increase capacities or extend useful lives are capitalized.

Depreciation expense, computed using the straight-line method, was $161.4 million, $134.4 million and $76.1 million for the years ended December 31, 2002, 2001, and 2000, respectively. Buildings and improvements are depreciated over estimated useful lives ranging from 10 to 40 years. Equipment is depreciated over estimated useful lives ranging from 3 to 10 years.

Other amortizable intangible assets are comprised of acquired management contracts which are amortized using the straight-line method over a period of 15 years and non-compete agreements that are being amortized based on the terms of the respective contracts.

When events, circumstances and operating results indicate that the carrying value of certain property, equipment, and other amortizable intangible assets might be impaired, Triad prepares projections of the undiscounted future cash flows expected to result from the use of the assets and their eventual disposition. If the projections indicate that the recorded amounts are not expected to be recoverable, such amounts are reduced to estimated fair value. Indicators of potential impairment are typically beyond the control of management. If market conditions become less favorable than those projected by management, impairments may be required.

On January 1, 2002 Triad adopted Statement of Financial Accounting Standards No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 supercedes Statement of Financial Accounting Standards No. 121 Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed of (SFAS 121) and the accounting and reporting provisions of Accounting Principles Board Opinion No. 30 Reporting the Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions (APB 30) for the disposal of a segment of a business. SFAS 144 establishes a single accounting model, based on the framework established in SFAS 121, for long-lived assets to be disposed of by sale and resolves implementation issues related to SFAS 121 by removing goodwill from its scope. The adoption of SFAS 144 would impact the results of operations and the

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES (continued)

financial position of Triad if a component of Triad s business is designated as held for sale after adoption of SFAS 144. Components designated as held for sale would be reported separately as discontinued operations with prior periods restated. Currently, Triad has not designated any components as held for sale under SFAS 144, but could do so in the future.

Goodwill and Other Non-Amortizable Assets

Triad adopted Statement of Financial Accounting Standards No. 142 Goodwill and Other Intangible Assets (SFAS 142) on January 1, 2002. Under SFAS 142, goodwill and intangible assets with indefinite lives are no longer amortized but reviewed for impairment annually, or more frequently if certain indicators arise. Goodwill is reviewed at the reporting unit level, which is defined in SFAS 142 as an operating segment or one level below an operating segment. Triad has determined that the reporting unit for its owned operations segment will be at the division level, which is one level below the segment. SFAS 142 required the completion of the initial step of a transitional impairment test within six months of adoption. Any impairment loss resulting from the transitional impairment would have been recorded as a cumulative effect of a change in accounting principle.

Goodwill is the excess of the purchase price in an acquisition over the fair value of identifiable assets acquired. Prior to the adoption of SFAS 142, goodwill was amortized using the straight-line method, generally over periods ranging from 30-40 years for hospital acquisitions and periods ranging from 5-20 years for physician practice and clinic acquisitions. After the adoption of SFAS 142, Triad reviews goodwill for impairment annually during the fourth quarter. Triad determines the fair value of the reporting units using discounted future cash flows. If the fair value of the reporting unit is less than the carrying value, an indication of impairment exists. The amount of the impairment would be determined by estimating the fair values of the tangible assets and liabilities, with the remaining fair value assigned to goodwill. The amount of impairment would be the difference between the carrying amount of the goodwill and the fair value of goodwill. No impairment charges were recorded during the year ended December 31, 2002 from the adoption of SFAS 142 or subsequent annual impairment testing.

Income Taxes

Triad accounts for income taxes under the provisions of Statement of Financial Accounting Standards No. 109 Accounting for Income Taxes (SFAS 109). Under SFAS 109, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse.

Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized. Income tax provision consists of Triad s current provision for federal and state income taxes and the change in Triad s deferred income tax assets and liabilities. While

Triad has considered several items including ongoing prudent and feasible tax planning strategies in assessing the need for valuation allowances, in the event Triad were to determine that the realization of its deferred tax asset in the future is different than its net recorded amount, an adjustment to income would be necessary.

General and Professional Liability Risks

Triad maintains professional malpractice liability insurance and general liability insurance in amounts which it believes to be sufficient for its operations, although it is possible that some claims may exceed the scope of the coverage in effect. Substantially all losses in periods prior to the spin-off are insured through a wholly-owned insurance subsidiary of HCA and excess loss policies maintained by HCA. HCA has agreed to indemnify Triad in respect of claims covered by such insurance policies arising prior to the spin-off. After the spin-off, Triad obtained

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES (continued)

insurance coverage on a claims incurred basis from HCA s wholly owned insurance subsidiary with excess coverage obtained from other carriers which is subject to certain deductibles which Triad considers to be reasonable. For the facilities acquired in the Quorum transaction, Triad obtained tail coverage, subject to certain deductibles, to cover claims incurred prior to July 31, 2001. These facilities were converted to Triad s existing coverage on August 1, 2001. The cost of general and professional liability coverage is based on insurance premiums paid and actuarially determined estimates for deductibles. The cost for the years ended December 31, 2002, 2001, and 2000 was approximately $74.1 million, $43.6 million and $22.2 million, respectively. Estimated liabilities for general and professional liability risks are actuarially determined and discounted using an interest rate of 6%. The estimated liability was $71.1 million and $36.0 million at December 31, 2002 and 2001, respectively.

For periods after the spin-off, Triad instituted its own self-insured programs for workers compensation and health insurance. Prior to the spin-off, Triad participated in self-insured programs for workers compensation and health insurance administered by HCA. HCA retained sole responsibility for all workers compensation and health claims incurred prior to the spin-off. The cost for these programs is based upon claims paid, plus an actuarially determined amount for claims incurred but not reported. Estimated liabilities for workers compensation were $13.6 million and $9.6 million at December 31, 2002 and 2001, respectively. Estimated liabilities for health claim liability risk were $14.9 million and $13.5 million at December 31, 2002 and 2001, respectively.

There are many factors that are used in determining the estimates, including amount and timing of historical payments, severity of individual cases and anticipated volume of services provided. Ultimate actual payments for workers compensation and general and professional liability risks may not become known for several years after incurrence. Any factors changing the underlying data used in determining these estimates could result in adjustments to the liability.

Reimbursable Expenses

Triad s wholly-owned subsidiary, Quorum Health Resources, LLC (QHR) recognizes revenue based on a contractually determined rate, plus direct costs associated with the contract. The direct costs relate primarily to salaries and benefits of QHR employees who serve as executives at hospitals managed by QHR. The salaries and benefits of these employees are legal obligations of and are paid by QHR, and are reimbursed by the managed hospitals. The direct costs are recorded as revenues and reimbursable expenses in the consolidated statements of operations.

Fair Value of Financial Instruments

Statement of Financial Accounting Standards 107 Disclosure About Fair Value of Financial Instruments, requires certain disclosures regarding the fair value of financial instruments. Cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities are reflected in

the consolidated financial statements at fair value because of the short-term maturity of these instruments. The fair value of long-term debt was determined by using quoted market prices, when available, or discounted cash flows to calculate these fair values.

Derivative Financial Instruments

Triad accounts for its derivatives under Statement of Financial Accounting Standards No. 133 Accounting for Derivative Instruments and Hedging Activities (SFAS 133). SFAS 133 requires that all derivative financial instruments that qualify for hedge accounting be recognized in the financial statements and measured at fair value regardless of the purpose or intent for holding them. Changes in fair value of derivative financial instruments are either recognized periodically in income or shareholders equity (as a component of comprehensive income), depending on whether the derivative is being used to hedge changes in fair value or cash flows. Triad s policy is to not hold or issue derivatives for trading purposes and to avoid derivatives with leverage features.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES (continued)

Stock-Based Compensation

The Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 148 Accounting for Stock-Based Compensation Transition and Disclosures (SFAS 148) in December 2002. SFAS 148 amends the disclosure provisions and transition alternatives of Statement of Financial Accounting Standards No. 123 Accounting for Stock-Based Compensation and is effective for fiscal years ending after December 15, 2002. Triad has adopted the disclosure provisions of SFAS 148 effective December 31, 2002. Triad does not anticipate a material impact on the results of operations or financial position from the adoption of SFAS 148.

As of December 31, 2002 Triad has two stock-based compensation plans, which are described more fully in Note 11. Triad accounts for these plans under the recognition and measurement principles of APB Opinion No. 25 Accounting for Stock Issued to Employees (APB 25) and related interpretations. APB 25 uses the intrinsic value method to account for options granted to employees. Stock-based compensation is generally not recognized since the option price is typically equal to the market value of the underlying common stock on the date of grant. On April 28, 2000, Triad granted 900,056 stock options with an exercise price of $17.07, which was the market price of the common stock on the effective date of grant, contingent on shareholder approval of an amendment to the 1999 Long-Term Incentive Plan increasing the number of shares available. Shareholder approval was granted on May 23, 2000. Compensation expense was recognized based on the difference between the market price of the common stock on the date the shareholder approval and the market price of the common stock on the date of grant amortized over the vesting period. Triad also has a Management Stock Purchase Plan (MSPP), which provides certain members of management an opportunity to purchase restricted shares of common stock at a discount through payroll deductions over six month intervals. These restrictions lapse three years after the date of purchase. Stock-based compensation of $0.2 million, $3.6 million and $0.8 million was recognized in the years ended December 31, 2002, 2001 and 2000, respectively, using the intrinsic value of the options. Triad has granted stock options to non-employees. Stock-based compensation of $0.2 million, $2.0 million and $0.1 million was recognized for the years ended December 31, 2002, 2001 and 2000, respectively, using the fair value of the options on the date of grant. As a result of the merger with Quorum, the non-cash stock option expense was accelerated during the year ended December 31, 2001 (see NOTE 11). The following table illustrates the effect on net income and earnings per share if Triad had applied the fair value recognition provisions of FASB Statement No. 123 Accounting for Stock-Based Compensation to all stock-based compensation (dollars in millions except per share amounts).

	For the years ended December 31,		
	2002	2001	2000
Net income as reported	$ 141.5	$ 2.8	$ 4.4
Add: Stock option expense recorded, net of income tax	0.1	2.1	0.5
Less: Fair value stock option expense, net of income tax	(17.4)	(20.2)	(5.0)
Pro forma net income (loss)	$ 124.2	$ (15.3)	$ (0.1)

Basic income per share, as reported	$ 1.97	$ 0.04	$ 0.14
Add: Stock option expense recorded, net of income tax		0.04	0.02
Less: Fair value stock option expense, net of income tax	(0.24)	(0.35)	(0.16)
Pro forma basic income (loss) per share	$ 1.73	$ (0.27)	$
Diluted income per share, as reported	$ 1.89	$ 0.05	$ 0.13
Add: Stock option expense recorded, net of income tax		0.04	0.01
Less: Fair value stock option expense, net of income tax	(0.20)	(0.34)	(0.15)
Pro forma diluted income (loss) per share	$ 1.69	$ (0.25)	$ (0.01)

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ACCOUNTING POLICIES (continued)

The fair values of stock options granted used to compute pro forma net income (loss) disclosures were estimated on the date of grant using the Black-Scholes option pricing model based on the following weighted average assumptions for the years ended December 31:

	2002	2001	2000
Risk free interest rate	4.09%	4.86%	6.50%
Expected life	5 years	5 years	5 years
Expected volatility	54.9%	58.9%	43.5%
Expected dividend yield			

Recent Accounting Pronouncements

In April 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 145 Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections (SFAS 145), which is required to be applied in fiscal years beginning after May 15, 2002, with early application encouraged. SFAS 145 rescinds Statement of Financial Accounting Standards No. 4 Reporting Gains and Losses From Extinguishment of Debt . SFAS 145 requires any gains or losses on extinguishment of debt that were classified as an extraordinary item in prior periods that do not meet the criteria in APB 30 for classification as an extraordinary item shall be reclassified into income from operations. Triad adopted the provisions of SFAS 145 on January 1, 2003. The impact of adoption of SFAS 145 will reduce income from operations by $3.2 million for the year ended December 31, 2001 through the reclassification of the extraordinary loss on retirement of debt (see NOTE 7).

In July 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 146 Accounting for Costs Associated with Exit or Disposal Activities (SFAS 146), which is effective for exit or disposal activities initiated after December 31, 2002 with early application encouraged. SFAS 146 addresses the accounting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3 Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring) . Triad does not anticipate a material impact on the results of operations or financial position from the adoption of SFAS 146.

The Financial Accounting Standards Board in November 2002, issued Financial Accounting Standards Board Interpretation No. 45 Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others (FIN 45). FIN 45 states that the fair value of certain guarantee obligations be recorded at the inception of the guarantee and clarifies disclosures required for guarantee obligations. The initial recognition provisions of FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure provisions are effective for financial statements of interim or annual periods ending after December 31, 2002. Triad does not anticipate that FIN 45 will have a material impact on its results of operations or financial position.

NOTE 2 ACQUISITIONS

On April 27, 2001, Triad completed the previously announced merger of Quorum with and into Triad with Triad being the surviving corporation. Triad is the acquiror for accounting purposes based on several considerations, including, in particular, that the former Quorum shareholders are not able to replace a majority of Triad s board of directors until at least the 2003 annual meeting of shareholders. The merger was accounted for under the purchase method of accounting and the results of operations for Quorum are included in Triad s results of operations beginning May 1, 2001. The purchase price of $2,434.3 million was allocated to assets acquired and liabilities assumed based on estimated fair values. Triad has obtained independent appraisals of acquired property

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 ACQUISITIONS (continued)

and equipment and identifiable intangible assets and their remaining useful lives. Triad has also reviewed and determined the fair value of other assets and liabilities assumed. The allocation was completed on April 27, 2002. The estimated fair values of the assets acquired and liabilities assumed relating to the acquisition are summarized below (in millions):

Working capital	$ 242.8
Property and equipment	941.8
Other assets	301.7
Net investment in held for sale assets	65.8
Long-term debt	(10.2)
Other non-current liabilities	(84.0)
Minority interests	(73.1)
Goodwill	1,049.5
	$ 2,434.3

On May 2, 2001, Triad sold two acute care hospitals in Minot, North Dakota acquired in the merger with Quorum for $38.0 million plus $8.2 million for working capital. Additionally, one hospital acquired in the merger with Quorum was designated as held for sale prior to the completion of the merger. The purchase price allocated to these assets was equal to the sales prices of the hospitals plus the cash flows for the holding period and the interest expense on the incremental debt incurred for the purchase of the hospitals. On August 7, 2001, Triad sold to an affiliate of a former member of Triad s board of directors its hospital in Baton Rouge, Louisiana for $19.0 million plus assumption of liabilities of $2.3 million. The results of operations of this entity are not included in Triad s results of operations. The pre-tax loss from continuing operations for this hospital and the associated interest expense excluded was $0.4 million and $0.4 million, respectively, during the year ended December 31, 2001.

In 2001, subsequent to the merger, Triad recorded charges of approximately $31.8 million associated with coordinating Quorum s accounting policies, practices and estimation processes with those of Triad. These charges included an $8.3 million pre-tax reduction to revenue, $18.5 million pre-tax increase in provision for doubtful accounts and $5.0 million additional income tax provision.

The following unaudited pro forma data summarizes the results of operations of the periods indicated as if the acquisition discussed previously had been completed as of the beginning of the periods presented. The pro forma results of operations gives effect to actual operating results prior to the acquisition, adjusted to include the pro forma effect of the acquisition. The pro forma results do not purport to be indicative of the results that would have actually been obtained if the acquisition occurred as of the beginning of the periods presented or that may be obtained in the future (in millions, except per share data).

	For the years ended December 31,	
	2001	2000
Revenues	$ 3,301.2	$ 3,103.4
Net income (loss)	$ 1.5	$ (28.1)
Net income (loss) per share:		
Basic	$ 0.02	$ (0.42)
Diluted	$ 0.02	$ (0.42)

On July 1, 2002, Triad completed the acquisition of all the assets comprising, and a 60% interest in the operations of, a hospital in Johnson, Arkansas for $10.1 million in cash.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 GOODWILL AND INTANGIBLE ASSETS

The goodwill allocated to Triad s reportable segments at December 31, 2002 and 2001 is as follows (in millions):

	2002	2001
Owned operations	$ 1,143.0	$ 1,134.4
Management services	61.1	60.9
Corporate and other	19.9	19.9
Total	$ 1,224.0	$ 1,215.2

The change in the carrying amount of goodwill subsequent to December 31, 2001 was due primarily to the completion of the Quorum purchase price allocation (see NOTE 2).

Intangible assets subject to amortization relate primarily to management contracts acquired in the management services segment. Amortization expense of intangible assets that still require amortization under SFAS 142 was $6.0 million, $4.2 million and $0.4 million for the years ended December 31, 2002, 2001, and 2000, respectively. Amortization expense relating to these intangible assets will be approximately $5.8 million per year for the next five years.

The gross carrying amount and accumulated amortization of amortized intangible assets at December 31, 2002 and 2001 are as follows (in millions):

	2002		2001	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Management contracts	$ 79.0	$ (8.8)	$ 79.0	$ (3.5)
Other	3.5	(1.7)	6.1	(1.0)
Total	$ 82.5	$ (10.5)	$ 85.1	$ (4.5)

As required by SFAS 142, results of operations for the years ended December 31, 2001 and 2000, respectively, have not been restated for the change in goodwill amortization. The following table sets forth the effect on net income and earnings per share excluding goodwill amortization which was recognized in the years ended December 31, 2001 and 2000, respectively (dollars in millions, except per share amounts).

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 GOODWILL AND INTANGIBLE ASSETS (continued)

	For the Years Ended December 31,		
	2002	**2001**	**2000**
Income from operations, as reported	$ 141.5	$ 6.0	$ 4.4
Add back goodwill amortization, net of income tax		29.7	6.3
Adjusted income from operations	141.5	35.7	10.7
Extraordinary loss on retirement of debt		(3.2)	
Adjusted net income	$ 141.5	$ 32.5	$ 10.7
Income per share			
Basic			
Income from operations, as reported	$ 1.97	$ 0.10	$ 0.14
Goodwill amortization, net of income tax		0.51	0.20
Adjusted income from operations	1.97	0.61	0.34
Extraordinary loss on retirement of debt		(0.06)	
Adjusted net income	$ 1.97	$ 0.55	$ 0.34
Diluted			
Income from operations, as reported	$ 1.89	$ 0.10	$ 0.13
Goodwill amortization, net of income tax		0.49	0.18
Adjusted income from operations	1.89	0.59	0.31
Extraordinary loss on retirement of debt		(0.05)	
Adjusted net income	$ 1.89	$ 0.54	$ 0.31

NOTE 4 SALES AND CLOSURES

On November 1, 2001, Triad sold an acute care hospital in Phoenix, Arizona for $55.3 million, including working capital. A gain of $22.0 million was recorded in the year ended December 31, 2001. This facility had revenues of $58.3 million and $64.8 million for the years ended December 31, 2001 and 2000, respectively. This facility had pre-tax income (losses) of $0.3 million and $(1.2) million for the years ended

December 31, 2001 and 2000, respectively.

Triad closed its acute care hospital in San Diego, California on November 30, 2000. On June 29, 2001, Triad sold the remaining assets of this facility for a net sales price of $6.6 million and recognized a minimal gain on the sale. For the year ended December 31, 2000, this facility had revenues of $22.1 million and losses before impairment charges and income taxes of $8.9 million.

As discussed in NOTE 2, Triad sold two acute care hospitals in Minot, North Dakota and one acute care hospital in Baton Rouge, Louisiana.

On December 14, 2000, Triad sold its hospital in Sherman, Texas, which was designated as held for sale in 1999, for $16.0 million. A gain on the sale of $2.0 million was recorded during the year ended December 31, 2000. For the year ended December 31, 2000 this facility had revenues of $27.6 million and income before impairment charges and income taxes of $1.4 million.

On March 31, 2000, Triad sold its limited partnership interest in a rehabilitation hospital located in Tucson, Arizona for $4.0 million. A gain of $4.2 million was recognized on the sale.

On February 11, 2000, Triad closed its acute care hospital in Roseburg, Oregon, which was designated as held for sale. As of December 31, 2001, the carrying value of this facility was $2.8 million. For the year ended

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 SALES AND CLOSURES (continued)

December 31, 2000 this facility had revenues of $1.9 million and losses before impairment charges and income taxes of $4.7 million. The remaining assets of this facility were sold in September 2002 for $2.4 million. A minimal loss on the sale was recorded in 2002.

NOTE 5 INCOME TAXES

The income tax provision for the years ended December 31, 2002, 2001 and 2000 consists of the following (dollars in millions):

	2002	2001	2000
Current:			
Federal	$	$ (0.2)	$
State	(10.5)	(2.7)	(1.1)
Deferred:			
Federal	(81.9)	(38.3)	(9.7)
State	(1.8)	(1.3)	(2.1)
	$ (94.2)	$ (42.5)	$ (12.9)

Triad also realized a $2.0 million tax benefit from an extraordinary loss on retirement of debt in the year ended December 31, 2001. A reconciliation of the federal statutory rate to the effective income tax rate from operations follows:

	2002	2001	2000
Federal statutory rate	35.0%	35.0%	35.0%
State income taxes, net of federal income tax benefit	3.3	2.5	4.8
Coordinating adjustments		9.3	
Non-deductible goodwill amortization		20.7	13.1
Non-deductible impairment charges		13.9	11.3
Non-deductible ESOP expense	1.2	4.7	8.1
Other items, net	0.5	1.5	2.2
Effective income tax rate	40.0%	87.6%	74.5%

A summary of the items comprising the deferred tax assets and liabilities at December 31 follows (dollars in millions):

	2002		2001	
	Assets	**Liabilities**	**Assets**	**Liabilities**
Depreciation and fixed asset basis differences	$	$ 118.8	$	$ 103.2
Accounts and other receivables	37.1		43.2	
Net operating loss carryforwards	19.3		53.7	
Compensation reserves	25.6		24.2	
Amortization and intangible asset basis differences		49.1		38.3
Other		1.9		7.6
	82.0	169.8	121.1	149.1
Valuation allowances	(1.0)		(1.0)	
	$ 81.0	$ 169.8	$ 120.1	$ 149.1

As part of the spin-off, HCA and Triad entered into a tax sharing and indemnification agreement (see NOTE 15). The tax sharing and indemnification agreement will not have an impact on the realization of deferred tax assets or the payment of deferred tax liabilities of Triad except to the extent that the temporary differences giving rise to

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 INCOME TAXES (continued)

such deferred tax assets and liabilities as of the spin-off are adjusted as a result of final tax settlements after the spin-off. In the event of such adjustments, the tax sharing and indemnification agreement will provide for certain payments between HCA and Triad as appropriate.

Deferred income taxes of $62.3 million and $103.1 million at December 31, 2002 and 2001, respectively, are included in current assets. Noncurrent deferred income tax liabilities totaled $151.1 million and $132.1 million at December 31, 2002 and 2001, respectively. Current and noncurrent deferred taxes totaled $88.8 million and $29.0 million net deferred tax liability at December 31, 2002 and 2001, respectively.

At December 31, 2002, state net operating loss carryforwards (expiring in years 2003 through 2022) available to offset future taxable income approximated $418.4 million. Utilization of net operating loss carryforwards in any one year may be limited and, in certain cases, result in a reduction of deferred tax assets. Based on available evidence, it is more likely than not that some portion of the state net operating loss carryforwards will not be realized, therefore, a valuation allowance of $1.0 million has been reflected as of December 31, 2002 and 2001.

At December 31, 2002, the federal net operating loss available to offset future taxable income approximated $21.7 million expiring in 2017 through 2021. Pursuant to the tax sharing and indemnification agreement, Triad is entitled to the tax benefit of such losses.

NOTE 6 IMPAIRMENT OF LONG-LIVED ASSETS

Through December 31, 2001, Triad followed the provisions of SFAS 121, which addressed accounting for the impairment of long-lived assets and long-lived assets to be disposed of, certain identifiable intangibles and goodwill related to those assets, and provided guidance for recognizing and measuring impairment losses. The statement required that the carrying amount of impaired assets be reduced to fair value. All impairments relate to the owned operations segment.

During the year ended December 31, 2001, Triad recorded impairment losses of $21.2 million related to one hospital facility where the recorded intangible asset values were not deemed recoverable based upon operating results, trends and projected future cash flows. The facility will continue to be used and is now recorded at estimated fair value, based upon discounted, estimated future cash flows.

During the year ended December 31, 2001, Triad recorded further impairment losses of $1.9 million on one hospital facility, which was closed in February 2000. The facility s carrying value of $4.7 million was reduced to fair value based on estimated selling value. This facility was sold during the year ended December 31, 2002 (see NOTE 4).

During the year ended December 31, 2000, Triad entered into negotiations to cancel one of its physician management contracts, which was substantially completed by December 31, 2000. Accordingly, the carrying value of the long-lived assets associated with this contract of approximately $1.0 million was reduced to fair value, based on estimated disposal value, resulting in a non-cash charge of $0.9 million. For the year ended December 31, 2000 this entity contributed revenues of $3.1 million and losses before impairment charges and income taxes of $2.8 million.

During the year ended December 31, 2000, the carrying value of the long-lived assets related to one facility that was closed on November 30, 2000 of $15.5 million, was reduced to fair value, based on the estimated selling value, for a non-cash charge of $7.1 million. This facility had revenues of $22.1 million and losses before impairment charges and income taxes of $8.9 million for the year ended December 31, 2000. This facility was sold during the year ended December 31, 2001 (see NOTE 4).

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT

Components of long-term debt at December 31 (in millions):

	Carrying Amount		Fair Value	
	2002	2001	2002	2001
Revolving Credit Line	$	$ 46.0	$	$ 46.0
Tranche A term loan	225.0	247.5	225.0	247.5
Tranche B term loan	542.5	548.5	542.5	548.5
Senior Notes	600.0	600.0	639.8	628.5
Senior Subordinated Notes	318.8	317.8	356.3	356.7
Other	5.7	14.0	6.3	14.3
	1,692.0	1,773.8	$ 1,769.9	$ 1,841.5
Less current portion	73.1	30.9		
	$ 1,618.9	$ 1,742.9		

The Tranche A term loan presently bears interest at LIBOR plus 2.25% (3.67% at December 31, 2002) with principal amounts due through 2007, the Tranche B term loan presently bears interest at LIBOR plus 3.0% (4.42% at December 31, 2002) with principal amounts due through 2008, the senior notes bear interest at 8.75% with principal amounts due in 2009 and the senior subordinated notes, which are net of $6.2 million of unamortized discount, bear interest at 11.0% with principal amounts due in 2009. The senior subordinated notes are callable, at Triad s option, in May 2004 and the senior notes are callable, at Triad s option, in May 2005. At December 31, 2002 Triad had a $250.0 million line of credit which bears interest at LIBOR plus 2.25%. No amounts were outstanding under the revolving credit line at December 31, 2002. The revolving credit line reduces to $225 million in 2004, $200 million in 2005 and matures in 2007. Triad had $36.3 million of letters of credit outstanding at December 31, 2002, which reduce the amount available under the revolving credit line. The LIBOR spread on the revolving credit line, including letters of credit outstanding under the revolving credit line, and Triad s Tranche A term loan is subject to reduction depending upon the total leverage of Triad. Triad has entered into two interest rate swaps which effectively convert $200.0 million of floating rate debt to fixed rates (see NOTE 9).

Triad s term loans and revolving lines of credit are collateralized by a pledge of substantially all of its assets other than real estate associated with the Quorum facilities. The debt agreements require that Triad comply with various financial ratios and tests and have restrictions, including but not limited to, new indebtedness, asset sales and use of proceeds therefrom, capital expenditures and dividends. In June 2002, Triad completed an amendment to its bank credit facility which favorably modified restrictions on new indebtedness, use of proceeds from debt and equity transactions, capital expenditures and various other restrictions. Triad currently is in compliance with all debt agreement covenants and

restrictions. If an event of default occurs with respect to the debt agreements, then the balances of the term loans and revolving line of credit could become due and payable which could result in other debt obligations of Triad also becoming due and payable.

Triad recorded $1.5 million of deferred loan costs in connection with the credit agreement amendment during the year ended December 31, 2002. During the year ended December 31, 2001, Triad recorded approximately $45.8 million of debt issue costs in connection with the Quorum acquisition. These costs are being amortized using the effective interest method over the lives of the related debt. Accumulated amortization of the debt issue costs was $17.0 million and $8.9 million as of December 31, 2002 and 2001, respectively.

As a result of the debt financing with the Quorum acquisition, an extraordinary loss of $2.4 million was incurred during the second quarter of 2001 from the write off of $3.9 million of associated debt issue costs, net of tax benefit of $1.5 million. During the fourth quarter of 2001, an extraordinary loss of $0.8 million, net of tax benefit of $0.5 million, was incurred from the write off of $1.3 million of debt issue costs associated with the early retirement of Triad s $150 million Asset Sale term loan.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Triad uses varying methods and significant assumptions to estimate fair values of long-term debt (see NOTE 1).

A debt maturity schedule is as follows (in millions):

2003		$ 72.8
2004		92.3
2005		91.6
2006		96.7
2007		222.5
Thereafter		1,122.3
		1,698.2
Less unamortized debt discount	Senior Subordinated Notes	6.2
		$ 1,692.0

Triad s senior subordinated notes and senior notes are guaranteed by all wholly owned operating subsidiaries of Triad (the Guarantor Subsidiaries). The guarantee obligations of the Guarantor Subsidiaries are full, unconditional and joint and several. Triad s non-wholly owned operating subsidiaries do not guarantee the notes (the Non-Guarantor Subsidiaries).

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed consolidating financial statements for Triad and its subsidiaries including the financial statements of Triad Hospitals, Inc. (parent only), the combined Guarantor Subsidiaries and the combined Non-Guarantor Subsidiaries are as follows:

Condensed Consolidating Statements of Operations

For the year ended December 31, 2002

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues	$	$ 2,943.0	$ 605.9	$ (7.8)	$ 3,541.1
Salaries and benefits	0.4	1,192.0	296.0		1,488.4
Reimbursable expenses		59.0			59.0
Supplies		463.1	83.7		546.8
Other operating expenses	2.1	533.0	111.9		647.0
Provision for doubtful accounts		233.1	39.7		272.8
Depreciation		136.6	24.8		161.4
Amortization		5.6	0.4		6.0
Interest expense allocated	(147.7)	137.9	9.8		
Interest expense, net	139.4	(4.9)	0.5		135.0
ESOP expense	10.8				10.8
Management fees			7.8	(7.8)	
Litigation settlements	(4.5)		(5.9)		(10.4)
Gain on sales of assets		(4.2)	(0.3)		(4.5)
Total operating expenses	0.5	2,751.2	568.4	(7.8)	3,312.3
Income (loss) before minority interests, equity in earnings and income tax provision	(0.5)	191.8	37.5		228.8
Minority interests		(10.9)	(3.9)		(14.8)
Equity in earnings of affiliates	236.2	55.3		(269.8)	21.7
Income before income tax provision	235.7	236.2	33.6	(269.8)	235.7
Income tax provision	(94.2)				(94.2)

Net income	$ 141.5	$ 236.2	$ 33.6	$ (269.8)	$ 141.5

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Statements of Operations

For the year ended December 31, 2001

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues	$	$ 2,296.0	$ 380.8	$ (7.3)	$ 2,669.5
Salaries and benefits	5.6	937.0	185.9		1,128.5
Reimbursable expenses		41.6			41.6
Supplies		356.4	54.8		411.2
Other operating expenses	0.1	432.1	69.5		501.7
Provision for doubtful accounts		213.1	26.8		239.9
Depreciation		117.0	17.4		134.4
Amortization		32.5	3.2		35.7
Interest expense allocated			5.2	(5.2)	
Interest expense, net	127.4	(1.5)	0.1		126.0
ESOP expense	9.3				9.3
Management fees			2.1	(2.1)	
Gain on sales of assets		(23.1)			(23.1)
Impairment of long lived assets		23.1			23.1
Total operating expenses	142.4	2,128.2	365.0	(7.3)	2,628.3
Income (loss) before minority interests, equity in earnings and income tax provision	(142.4)	167.8	15.8		41.2
Minority interests		(7.6)	0.4		(7.2)
Equity in earnings of affiliates	190.9	30.7		(207.1)	14.5
Income before income tax provision	48.5	190.9	16.2	(207.1)	48.5
Income tax provision	(42.5)				(42.5)
Income from operations	6.0	190.9	16.2	(207.1)	6.0
Extraordinary item, net of tax	(3.2)				(3.2)
Net income	$ 2.8	$ 190.9	$ 16.2	$ (207.1)	$ 2.8

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TRIAD HOSPITALS, INC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Statements of Operations

For the year ended December 31, 2000

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues.	$	$ 1,176.6	$ 59.7	$ (0.8)	$ 1,235.5
Salaries and benefits	0.9	495.3	14.9		511.1
Supplies		171.9	13.7		185.6
Other operating expenses		251.3	8.5		259.8
Provision for doubtful accounts		102.2	1.4		103.6
Depreciation		73.2	2.9		76.1
Amortization		6.6	0.5		7.1
Interest expense allocated		0.1		(0.1)	
Interest expense, net	63.1	(5.8)			57.3
ESOP expense	7.1				7.1
Management fees			0.7	(0.7)	
Gain on sales of assets		(7.9)			(7.9)
Impairment of long lived assets		8.0			8.0
Total operating expenses	71.1	1,094.9	42.6	(0.8)	1,207.8
Income (loss) before minority interests, equity in earnings and income tax provision	(71.1)	81.7	17.1		27.7
Minority interests		(9.0)			(9.0)
Equity in earnings of affiliates	88.4	15.7		(105.5)	(1.4)
Income before income tax provision	17.3	88.4	17.1	(105.5)	17.3
Income tax provision	(12.9)				(12.9)
Net income	$ 4.4	$ 88.4	$ 17.1	$ (105.5)	$ 4.4

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Balance Sheets

December 31, 2002

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Assets					
Current assets					
Cash and cash equivalents	$	$ 60.5	$ 7.8	$	$ 68.3
Accounts receivable, net		420.8	86.6		507.4
Other current assets	78.0	176.1	22.6	(8.0)	268.7
Total current assets	78.0	657.4	117.0	(8.0)	844.4
Net property and equipment, at cost		1,639.5	315.7		1,955.2
Goodwill		1,175.7	48.3		1,224.0
Intangible assets		72.0			72.0
Investments in subsidiaries	1,674.3	445.1		(1,939.7)	179.7
Due from affiliates	2,004.5			(2,004.5)	
Other	56.4	76.9		(27.0)	106.3
Total assets	$ 3,813.2	$ 4,066.6	$ 481.0	$ (3,979.2)	$ 4,381.6
Liabilities and Equity					
Current liabilities	$ 85.9	$ 313.9	$ 46.8	$ (1.4)	$ 445.2
Due to affiliates		1,895.1	109.4	(2,004.5)	
Long-term debt	1,615.3	30.7	6.5	(33.6)	1,618.9
Deferred taxes and other liabilities	157.5	80.2			237.7
Minority interests in equity of consolidated entities		72.4	52.9		125.3
Equity	1,954.5	1,674.3	265.4	(1,939.7)	1,954.5
Total liabilities and equity	$ 3,813.2	$ 4,066.6	$ 481.0	$ (3,979.2)	$ 4,381.6

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Balance Sheets

December 31, 2001

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Assets					
Current assets					
Cash and cash equivalents	$	$ 14.7	$ 1.6	$	$ 16.3
Restricted cash	5.7				5.7
Accounts receivable, net		365.8	80.8		446.6
Other current assets	104.6	155.9	18.2		278.7
Total current assets	110.3	536.4	100.6		747.3
Net property and equipment, at cost		1,526.1	290.9		1,817.0
Goodwill		1,166.9	48.3		1,215.2
Intangible assets		80.6			80.6
Investments in subsidiaries	3,174.1	471.0		(3,455.7)	189.4
Due from affiliates	313.7			(313.7)	
Other	39.5	66.4	9.9		115.8
Total assets	$ 3,637.6	$ 3,847.4	$ 449.7	$ (3,769.4)	$ 4,165.3
Liabilities and Equity					
Current liabilities	$ 42.6	$ 279.2	$ 44.5	$	$ 366.3
Due to affiliates		249.7	64.0	(313.7)	
Long-term debt	1,731.4	4.8	6.7		1,742.9
Deferred taxes and other liabilities	132.1	68.4			200.5
Minority interests in equity of consolidated entities		71.2	52.9		124.1
Equity	1,731.5	3,174.1	281.6	(3,455.7)	1,731.5
Total liabilities and equity	$ 3,637.6	$ 3,847.4	$ 449.7	$ (3,769.4)	$ 4,165.3

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Statements of Cash Flows

For the year ended December 31, 2002

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net cash provided by operating activities	$ 0.1	$ 286.8	$ 71.4	$	$ 358.3
Cash flows from investing activities					
Purchases of property and equipment		(255.3)	(41.3)		(296.6)
Distributions and advances (to) from affiliates	75.8	20.7	(64.8)		31.7
Proceeds received on sales of assets		6.7	0.1		6.8
Acquisitions		(10.1)			(10.1)
Restricted cash	5.7				5.7
Other		0.7			0.7
Net cash provided by (used in) investing activities	81.5	(237.3)	(106.0)		(261.8)
Cash flows from financing activities					
Payments of long-term debt	(74.5)	(2.2)	(7.1)		(83.8)
Payment of debt issue costs	(1.5)				(1.5)
Proceeds from issuance of common stock	42.4				42.4
Proceeds from executive stock purchase plan loans	10.1				10.1
Distributions to minority partners		(9.7)	(2.0)		(11.7)
Net borrowings to (from) affiliate	(33.9)	27.0	6.9		
Net change in due to (from) affiliate	(24.2)	(18.8)	43.0		
Net cash provided by (used in) financing activities	(81.6)	(3.7)	40.8		(44.5)
Change in cash and cash equivalents		45.8	6.2		52.0
Cash and cash equivalents at beginning of period		14.7	1.6		16.3
Cash and cash equivalents at end of period	$	$ 60.5	$ 7.8	$	$ 68.3

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Statements of Cash Flows

For the year ended December 31, 2001

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net cash provided by (used in) operating activities	$ (156.0)	$ 418.1	$ 56.2	$	$ 318.3
Cash flows from investing activities					
Purchases of property and equipment		(159.7)	(40.9)		(200.6)
Distributions and advances (to) from affiliates	122.1	(72.5)	(31.9)		17.7
Proceeds received on sales of assets		127.8			127.8
Acquisitions	(1,386.6)				(1,386.6)
Restricted cash	(5.7)				(5.7)
Other		(5.7)			(5.7)
Net cash used in investing activities	(1,270.2)	(110.1)	(72.8)		(1,453.1)
Cash flows from financing activities					
Payments of long-term debt	(577.5)	(3.0)	(1.1)		(581.6)
Proceeds from long-term debt	1,752.7				1,752.7
Payment of debt issue costs	(45.8)				(45.8)
Proceeds from issuance of common stock	27.0				27.0
Distributions to minority partners		(7.7)	(0.2)		(7.9)
Net change in due to (from) affiliate	269.8	(289.0)	19.2		
Net cash provided by (used in) financing activities	1,426.2	(299.7)	17.9		1,144.4
Change in cash and cash equivalents		8.3	1.3		9.6
Cash and cash equivalents at beginning of period		6.4	0.3		6.7
Cash and cash equivalents at end of period	$	$ 14.7	$ 1.6	$	$ 16.3

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 LONG-TERM DEBT (continued)

Condensed Consolidating Statements of Cash Flows

For the year ended December 31, 2000

(Dollars in millions)

	Triad Hospitals, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net cash provided by (used in) operating activities	$ (61.0)	$ 117.2	$ 15.4	$	$ 71.6
Cash flows from investing activities					
Purchases of property and equipment		(90.2)	(4.2)		(94.4)
Distributions and advances (to) from affiliates	(2.4)	34.9	(9.8)		22.7
Proceeds received on sales of assets		20.7			20.7
Acquisitions		(118.2)	(0.6)		(118.8)
Other		(1.6)			(1.6)
Net cash used in investing activities	(2.4)	(154.4)	(14.6)		(171.4)
Cash flows from financing activities					
Payments of long-term debt	(15.8)	(1.7)			(17.5)
Proceeds from long-term debt	51.0				51.0
Payment of debt issue costs	(1.5)				(1.5)
Proceeds from issuance of common stock	9.9				9.9
Distributions to minority partners		(6.3)			(6.3)
Net change in due to (from) affiliate	19.8	(19.2)	(0.6)		
Net cash provided by (used in) financing activities	63.4	(27.2)	(0.6)		35.6
Change in cash and cash equivalents		(64.4)	0.2		(64.2)
Cash and cash equivalents at beginning of period		70.8	0.1		70.9
Cash and cash equivalents at end of period	$	$ 6.4	$ 0.3	$	$ 6.7

NOTE 8 GUARANTEES

Triad has entered into agreements whereby it has guaranteed certain loans entered into by patients who had services performed at Triad s facilities. These loans are provided by various financial institutions. Triad would be obligated to repay the financial institutions if a patient fails

to repay their loan. Triad would then pursue collections from the patient. At December 31, 2002 and 2001, the amounts subject to the guarantees were $13.6 million and $6.8 million, respectively. Triad had accrued liabilities of $3.0 million and $1.5 million at December 31, 2002 and 2001, respectively, for the estimated loan defaults that would be covered under the guarantees.

NOTE 9 DERIVATIVE FINANCIAL INSTRUMENTS

Triad has entered into interest rate swap agreements. In January 2002, Triad entered into an interest rate swap agreement, which effectively converts a notional amount of $100 million of floating rate borrowings to fixed rate borrowings. The term of the interest rate swap expires in January 2004. Triad will pay a rate of 3.22% and receive LIBOR, which was set at 1.76% at December 31, 2002. Subsequent to December 31, 2002, the LIBOR rate was reset at 1.38%. In June 2002, Triad entered into another interest rate swap agreement, which effectively converts an additional notional amount of $100 million of floating rate borrowings to fixed rate borrowings. The term of the interest rate swap expires in June 2005. Triad will pay a rate of 3.99% and receive LIBOR, which was set at 1.41% at December 31, 2002.

Both of the interest rate swap agreements are with the same counterparty. Triad is exposed to credit losses in the event of nonperformance by the counterparty. The counterparty is a creditworthy financial institution and it is anticipated that the counterparty will be able to fully satisfy the obligation under the contracts. The interest rate swaps are designated as cash flow hedges and Triad believes that the hedges are highly effective.

At December 31, 2002, the fair value of the interest rate swaps of $6.4 million was recorded in other liabilities in the consolidated balance sheet. The change in fair value of the interest rate swaps, net of income tax benefit of $2.4 million, was recognized through other comprehensive loss.

NOTE 10 LEASES

Triad leases real estate properties, equipment and vehicles under cancelable and non-cancelable leases. Rental expense for the years ended December 31, 2002, 2001 and 2000 was $60.8 million, $50.3 million and $31.0 million, respectively. Future minimum operating and capital lease payments are as follows at December 31, 2002 (in millions):

	Operating	Capital
2003	$ 37.1	$ 0.5
2004	35.9	0.4
2005	30.2	0.2
2006	23.6	0.2
2007	16.2	0.2
Thereafter	56.1	0.1
Total minimum payments	$ 199.1	1.6
Less amounts representing interest		0.3
Present value of minimum lease payments		$ 1.3

The following summarizes amounts related to equipment leased by Triad under capital leases at December 31 (in millions):

	2002	2001
Equipment	$ 1.6	$ 0.9
Accumulated amortization	(0.3)	(0.4)
Net book value	$ 1.3	$ 0.5

On January 1, 1999, Triad transferred two acute care hospitals and three ambulatory surgery centers to an unaffiliated third party pursuant to a long-term lease. Lease income of $18.0 million, $17.8 million and $16.9 million was recorded in the years ended December 31, 2002, 2001 and 2000, respectively. The following summarizes the assets leased at December 31, 2002 and 2001 (in millions):

	2002	2001
Land	$ 7.7	$ 7.7
Buildings	51.6	51.6
Equipment	69.1	69.1
	128.4	128.4
Accumulated depreciation	(91.7)	(86.3)
	$ 36.7	$ 42.1

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 LEASES (continued)

The following is a schedule of minimum future lease income on these leases as of December 31, 2002 (dollars in millions):

2003	$ 18.2
2004	18.5
2005	18.8
2006	19.1
2007	19.4
Thereafter	122.4
Total minimum income	$ 216.4

NOTE 11 STOCK BENEFIT PLANS

Triad s 1999 Long-Term Incentive Plan has 14,000,000 shares of Triad s common stock reserved for issuance. The 1999 Long-Term Incentive Plan authorizes the grant of stock options, stock appreciation rights and other stock based awards to officers and employees of Triad. Stock options granted are generally at an exercise price equal to the fair market value at the date of grant and are exercisable over a four year period and expire ten years from date of grant. The plan provides for immediate vesting upon a change in control.

The merger of Triad and Quorum (see NOTE 2) constituted a change of control under the terms of the Triad 1999 Long-Term Incentive Plan, the Triad MSPP, the Triad Executive Stock Purchase Plan and all other similar plans. All of the outstanding, unvested stock options became vested and exercisable at the effective time of the merger; however, certain executive officers of Triad waived the vesting of certain stock options in connection with the merger. The waivers ended June 29, 2001. In addition, restrictions lapsed on shares of Triad restricted common stock issued under the MSPP and these shares became fully vested and transferable and no longer are subject to forfeiture.

Triad has an Executive Stock Purchase Plan, for which 1,000,000 shares of Triad s common stock were reserved for issuance. The Executive Stock Purchase Plan granted to specified executives of Triad a right to purchase shares of common stock from Triad. Triad loaned each participant in the plan approximately 100% of the purchase price of Triad s common stock bearing interest at 5.15% per annum, on a full recourse basis. The principal and interest of the loans mature on the fifth anniversary following the purchase of the shares, termination of the participants employment or bankruptcy of the participant. In addition, Triad has granted to such executives stock options equal to three-quarters of a share for each share purchased. The exercise price of these stock options is equal to the purchase price of the shares and the options expire in 10 years. During the year ended December 31,1999, 970,000 shares were purchased by participants in the plan and options to purchase an additional 727,500 shares were issued in connection with such purchased shares. The total amount which had been loaned to participants to purchase shares under the plan was $9.1 million which was recorded as a reduction to equity. Triad received a $0.4 million payment from one

participant in 2001. Triad received $8.7 million in principal and $1.4 million in interest payments from all remaining participants in 2002. The interest payments were recorded as additional paid-in capital. No amounts remain outstanding on the loans.

Triad adopted various other plans for which 500,000 shares of Triad s common stock have been reserved for issuance.

As anticipated at the time of the spin-off, Triad entered into a stock option pledge agreement with a charitable corporation granting 100,000 stock options on July 11, 2000, subject to approval by the Internal Revenue Service (the IRS). The exercise price of these stock options is equal to the market price on the grant date. The stock options become immediately exercisable upon receipt of IRS approval and expire 10 years from that date. Triad waived the IRS approval provision on June 27, 2001 and the options are now exercisable. Non-cash stock option expense of $1.4 million was recorded in 2001 using the fair value of these options. Since the options were immediately exercisable, no additional non-cash stock option expense was recorded subsequent to December 31, 2001.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11 STOCK BENEFIT PLANS (continued)

As part of the merger (see NOTE 2), Triad issued stock options to Quorum option holders under Quorum s 1997 Stock Option Plan. The fair value of these options was included in the purchase price for the merger.

Information regarding stock options for 2002, 2001 and 2000 is summarized below:

	Stock Options	Option Price Per Share	Weighted Average Exercise Price
Balances, January 1, 2000	4,450,608	$ 0.07 - $18.84	$ 11.26
Granted	2,102,556	$ 16.50 - $27.69	$ 17.48
Exercised	(618,456)	$ 0.07 - $18.84	$ 11.52
Cancelled	(267,922)	$ 0.07 - $27.69	$ 13.62
Balances, December 31, 2000	5,666,786	$ 0.07 - $27.69	$ 13.43
Granted	4,948,479	$ 12.27 - $50.35	$ 25.90
Exercised	(1,388,414)	$ 0.19 - $30.47	$ 15.56
Cancelled	(320,301)	$ 0.19 - $50.35	$ 27.90
Balances, December 31, 2001	8,906,550	$ 0.07 - $50.35	$ 19.49
Granted	3,012,250	$ 32.15 - $42.00	$ 32.70
Exercised	(2,363,199)	$ 0.19 - $35.70	$ 14.11
Cancelled	(282,944)	$ 3.65 - $50.35	$ 30.56
Balances, December 31, 2002	9,272,657	$ 0.07 - $42.00	$ 24.81

The weighted-average fair value of stock options granted to Triad employees during the years ended December 31, 2002, 2001 and 2000, was $16.88, $16.37 and $9.67 per option, respectively. At December 31, 2002, 2001 and 2000, there were 4,204,637, 5,852,800 and 1,337,085 options exercisable, respectively. There were 2,307,304, 4,682,181 and 466,506 stock options available for grant at December 31, 2002, 2001 and 2000, respectively.

The following table summarizes information regarding the options outstanding at December 31, 2002:

	Options Outstanding			Options Exercisable	
	Number Outstanding at 12/31/02	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable at 12/31/02	Weighted Average Exercise Price
Range of Exercise Prices					
$16.69 to $16.71	152,551	3 years	$ 16.71	152,551	$ 16.71
$15.42 to $29.08	150,557	4 years	$ 17.06	150,557	$ 17.06
$22.63 to $31.50	10,565	5 years	$ 26.98	10,565	$ 26.98
$16.34 to $27.84	85,093	6 years	$ 17.12	85,093	$ 17.12
$0.07 to $18.84	1,822,216	7 years	$ 11.38	1,822,216	$ 11.38
$16.50 to $27.69	1,259,487	8 years	$ 17.62	1,259,487	$ 17.62
$24.63 to $35.70	2,886,438	9 years	$ 29.54	724,168	$ 28.99
$32.15 to $42.00	2,905,750	10 years	$ 32.70		$
	9,272,657		$ 24.81	4,204,637	$ 16.83

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11 STOCK BENEFIT PLANS (continued)

Subsequent to December 31, 2002, Triad granted 1,229,300 stock options with an exercise price equal to the market price on the date of grant. The options are exercisable over a four-year period and expire ten years from the date of grant.

Triad has an Employee Stock Purchase Plan (ESPP) which provides an opportunity to purchase shares of its common stock at a discount (through payroll deductions over six month intervals) to substantially all employees. Shares of common stock issued to employees through the ESPP were 344,090, 209,553 and 147,023 during the years ended December 31, 2002, 2001 and 2000, respectively.

Shares issued through the MSPP were 27,610 at a weighted average price of $25.49 per share, 34,699 at a weighted average price of $21.51 per share and 72,586 at a weighted average price of $10.86 per share during the years ended December 31, 2002, 2001 and 2000, respectively. Subsequent to December 31, 2002, 16,238 shares at $27.08 per share were issued through the MSPP.

NOTE 12 RETIREMENT PLANS

Triad has established an Employee Stock Ownership Plan (ESOP) for substantially all of its employees. The ESOP purchased from Triad, at fair market value, 3,000,000 shares of Triad s common stock. The purchase was primarily financed by the ESOP issuing a promissory note to Triad, which will be repaid annually in equal installments over a 10-year period beginning December 31, 1999. Triad makes contributions to the ESOP which the ESOP uses to repay the loan. Triad s stock acquired by the ESOP is held in a suspense account and will be allocated to participants at market value from the suspense account as the loan is repaid.

The loan to the ESOP is recorded in unearned ESOP compensation and stockholders notes receivable in the consolidated balance sheets. Reductions are made to unearned ESOP compensation as shares are committed to be released to participants at cost. Recognition of ESOP expense is based on the average market price of shares committed to be released to participants. Shares are deemed to be committed to be released ratably during each period as the employees perform services. The difference between average market price and cost of the shares is shown as a change in additional paid-in capital. As the shares are committed to be released, the shares become outstanding for earnings per share calculations. Triad recognized ESOP expense of $10.8 million, $9.3 million and $7.1 million during the years ended December 31, 2002, 2001 and 2000, respectively, and the unearned ESOP compensation was $20.7 million and $24.2 million at December 31, 2002 and 2001, respectively.

The ESOP shares as of December 31, 2002 were as follows:

Shares released	900,000
Shares committed to be released	300,000
Unreleased shares	1,800,000
Total ESOP shares	3,000,000
Fair value of unreleased shares	$ 53.7 million

Triad has instituted a defined contribution retirement plan which covers substantially all employees. Benefits are determined primarily as a percentage of a participant s annual income, less contributions to the ESOP. These benefits are vested over specific periods of employee service. Triad has also instituted a contributory benefit plan which is available to employees who meet certain minimum requirements. The plan requires that Triad match 50% of a participant s contribution up to certain maximum levels. Triad recorded expense under these plans of $28.9 million, $6.9 million and $4.3 million for the years ended December 31, 2002, 2001 and 2000, respectively, and recorded reductions of estimates of prior year retirement plan accruals of $3.4 million, $1.5 million and $5.0 million

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12 RETIREMENT PLANS (continued)

for the years ended December 31, 2002, 2001 and 2000, respectively. Contributions to the retirement plan are funded annually. Triad s contributions to the contributory benefit plan are funded periodically during the year.

In the Quorum acquisition (see NOTE 2), Triad assumed defined contribution employee benefit plans covering substantially all employees that were employees of Quorum. Employees could contribute up to 15% of eligible compensation subject to IRS limits. The plans permitted a discretionary base contribution and a discretionary match to employee deferrals. Contributions to the plans were determined annually. Base contributions under the plans vest at the end of each plan year and matching contributions vest after five years of qualifying service. Reductions of estimates in the prior year retirement plan accruals of $1.4 million were recorded in the year ended December 31, 2002. Benefit plan expense for this plan was $10.2 million for the year ended December 31, 2001. On January 1, 2002, this plan was merged into the Triad defined contribution plan described above.

NOTE 13 LITIGATION SETTLEMENTS

Quorum was involved in a malpractice case in which Quorum s insurance company issued a reservation of rights, which means that the insurance company was providing a current defense, but was reserving a right ultimately not to pay the claim. Accordingly, the potential exposure was recorded as a liability as part of the Quorum purchase price allocation. During the third quarter of 2002, Triad settled the malpractice case and the insurance company agreed to pay the claim. Triad reflected the settlement, less remaining legal fees, of $5.9 million in the third quarter of 2002.

In June 2002, Triad received notification that HCA had agreed to reimburse Triad for a portion of the settlement on a False Claims Act case, settled by Quorum prior to Triad s acquisition. Triad received this reimbursement in the amount of $4.5 million, in July 2002.

NOTE 14 INCOME PER SHARE

Income per common share is based on the weighted average number of shares outstanding adjusted for the shares issued to the ESOP. Diluted weighted average shares outstanding is calculated by adjusting basic weighted average shares outstanding by all potentially dilutive stock options. For the year ended December 31, 2002, options outstanding of 301,063 were not included in the computation of diluted income per share because the exercise prices of the options were greater than the average market price of the common stock. Weighted average shares for the years ended December 31, 2002, 2001 and 2000 are as follows:

	For the years ended December 31,		
	2002	2001	2000
Weighted average shares exclusive of unreleased ESOP shares	71,552,847	57,508,685	31,593,403
ESOP shares committed to be released	150,000	150,000	150,000
Basic weighted average shares outstanding	71,702,847	57,658,685	31,743,403
Effect of dilutive securities employee stock options	3,293,614	3,397,009	2,390,007
Diluted weighted average shares outstanding	74,996,461	61,055,694	34,133,410

NOTE 15 AGREEMENTS WITH HCA

Triad has entered into distribution and other related agreements governing the spin-off of Triad from HCA and Triad s subsequent relationship with HCA. These agreements provide certain indemnifications for the parties, and provide for the allocation of tax and other assets, liabilities and obligations arising from periods prior to the spin-off.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15 AGREEMENTS WITH HCA (continued)

HCA and Triad entered into a distribution agreement providing for certain arrangements among HCA and Triad subsequent to the date of the spin-off. The distribution agreement generally provides that Triad will be financially responsible for liabilities arising out of or in connection with the assets and entities that constitute Triad. The distribution agreement provides, however, that HCA will indemnify Triad for any losses, which it incurs arising from the pending governmental investigations of certain of HCA s business practices. The distribution agreement further provides that HCA will indemnify Triad for any losses which it may incur arising from stockholder actions and other legal proceedings related to the governmental investigations which are currently pending against HCA, and from proceedings which may be commenced by governmental authorities or by private parties in the future that arise from acts, practices or omissions engaged in prior to the date of the spin-off and related to such proceedings. HCA has also agreed that, in the event that any hospital owned by Triad as of the date of the spin-off is permanently excluded from participation in the Medicare and Medicaid programs as a result of the proceedings described above, then HCA will make a cash payment to Triad in an amount (if positive) equal to five times the excluded hospital s 1998 income from continuing operations before depreciation and amortization, interest expense, management fees, impairment of long-lived assets, minority interests and income taxes less the net proceeds of the sale or other disposition of the excluded hospital. HCA will not indemnify Triad for losses relating to any acts, practices and omissions engaged in by Triad after the date of the spin-off, whether or not Triad is indemnified for similar acts, practices and omissions occurring prior to the date of the spin-off.

HCA has entered into a compliance agreement setting forth certain agreements to comply with applicable laws and regulations. Triad was obligated to participate with HCA in these negotiations. On November 1, 2001, Triad entered into a five-year corporate integrity agreement with the Office of the Inspector General and agreed to maintain its compliance program in accordance with the corporate integrity agreement. This obligation could result in greater scrutiny by regulatory authorities. Violations of the integrity agreement could subject Triad s hospitals to substantial monetary penalties. The cost to implement and maintain the compliance program was approximately $3.0 million and $2.0 million in 2002 and 2001, respectively. Continuing compliance with the corporate integrity agreement may impose expensive and burdensome requirements on certain operations which could have a material adverse impact on Triad. The compliance measures and reporting and auditing requirements for Triad s hospitals contained in the integrity agreement include:

Continuing the duties and activities of corporate compliance officers and committees and maintaining a written code of conduct and written policies and procedures;

Providing general training on the compliance policy in the agreement and specific training for the appropriate personnel on billing, coding and cost report issues;

Having an independent third party conduct periodic audits of inpatient DRG coding and laboratory billing;

Continuing a confidential disclosure program and compliance hotline and implementing enhanced screening to ensure ineligible employees and contractors are not hired;

Reporting material deficiencies resulting in an overpayment by a federal healthcare program and probable violations of certain laws, rules and regulations; and

Submitting annual reports to the Inspector General describing the operations of the corporate compliance program for the past year.

In connection with the spin-off, HCA also agreed to indemnify Triad for any payments which it is required to make in respect to Medicare, Medicaid and Blue Cross cost reports relating to the cost report periods ending on or prior to the date of the spin-off, and Triad agreed to indemnify HCA for and pay to HCA any payments received by Triad relating to such cost reports. Triad will be responsible for the filing of these cost reports and any terminating cost reports.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15 AGREEMENTS WITH HCA (continued)

HCA and Triad entered into a tax sharing and indemnification agreement, which allocates tax liabilities among HCA and Triad, and addresses certain other tax matters such as responsibility for filing tax returns, control of and cooperation in tax litigation and qualification of the spin-off as a tax-free transaction. Generally, HCA will be responsible for taxes that are allocable to periods prior to the spin-off, and HCA and Triad will each be responsible for its own tax liabilities (including its allocable share of taxes shown on any consolidated, combined or other tax return filed by HCA) for periods after the spin-off. The tax sharing and indemnification agreement prohibits Triad from taking actions that could jeopardize the tax treatment of either the spin-off or the internal restructuring of HCA that preceded the spin-off, and requires Triad to indemnify HCA for any taxes or other losses that result from any such actions.

Prior to the date of the spin-off, HCA maintained various insurance policies for the benefit of Triad. In connection with the spin-off, HCA and Triad entered into an agreement relating to insurance matters which provides that any claims against insurers outstanding at the spin-off will be for the benefit of the party who will own the asset which is the basis for the claim, or, in the case of liability claims, which is the owner of the facility at which the activity which is the subject of the claim occurred. HCA will pay Triad any portion of such a claim that is unpaid by an insurer to satisfy deductible, co-insurance or self-insurance amounts (unless such amounts were paid to or accounted for by the affected entity prior to the spin-off). HCA and Triad have ensured that all of the insurance policies in effect after the spin-off provided the same coverage to Triad that were available prior to the spin-off. Triad purchased continuous coverage under extensions or renewals of existing, or new, policies issued by Health Care Indemnity, Inc., a subsidiary of HCA. Any retroactive rate adjustments for periods ending on or before the spin-off, in respect of such insurance policies, will be paid or received by HCA. Triad continues to purchase a portion of its general and professional liability insurance from Health Care Indemnity, Inc. (see NOTE 1).

HCA s wholly owned subsidiary, Columbia Information Services, Inc. (CIS), entered into a computer and data processing services agreement with Triad. Pursuant to this agreement, CIS will provide computer installation, support, training, maintenance, data processing and other related services to Triad. The initial term of the agreement is seven years, which will be followed by a wind-down period of up to one year. CIS charged Triad approximately $24.7 million, $22.0 million, and $19.0 million in the years ended December 31, 2002, 2001 and 2000, respectively, for services provided under this agreement. In the event the agreement is terminated by Triad, it will be required to pay a termination fee equal to the first month s billed fees, multiplied by the remaining number of months in the agreement.

HCA and Triad entered into an agreement relating to benefit and employment matters which allocates responsibilities for employment compensation, benefits, labor, benefit plan administration and certain other employment matters on and after the date of the spin-off. The agreement generally provides that Triad assumed responsibility for its employees from and after the date of the spin-off, and that HCA retained the liabilities with respect to former employees associated with the facilities and operations of Triad who terminated employment on or prior to the date of the spin-off. Benefit plans established by Triad generally recognize past service with HCA.

HCA also entered into an agreement with Triad, pursuant to which Triad sub-leased from HCA its former principal executive offices (at the same price per square foot as was payable under the HCA lease). Triad s sub-lease terminated on January 31, 2003.

HCA also entered into a transitional service agreement with Triad pursuant to which HCA furnished various administrative services to Triad. These services include support in various aspects of payroll processing and tax reporting for employees of Triad, real estate design and construction management, legal, human resources, insurance and accounting matters on an as needed basis. Each agreement terminated on December 31, 2000.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15 AGREEMENTS WITH HCA (continued)

The agreements provide that Triad s fees to HCA for services provided are based on HCA s costs incurred in providing such services.

Triad is an investor along with HCA in a group purchasing organization which makes certain national supply and equipment contracts available to their respective facilities.

HCA entered into agreements with Triad whereby HCA will share telecommunications services with Triad under HCA s agreements with its telecommunications services provider and whereby HCA will make certain account collection services available to Triad.

NOTE 16 CONTINGENCIES

False Claims Act Litigation

As a result of its ongoing discussions with the government prior to the merger, Quorum learned of two *qui tam* complaints against it alleging violations of the False Claims Act for claims allegedly submitted to the government involving one owned and two managed hospitals. Quorum accrued the estimated liability on these items prior to the merger. One such matter remains under seal. With respect to the matter involving the two managed hospitals, the government has requested that Quorum conduct a self audit with respect to one Medicare cost report for one managed hospital and three other specific issues and that matter remains under seal. The government has stated that it intends to investigate certain other allegations. With respect to the complaint involving the owned hospital, Triad has settled this matter through the payment to the government of $427,500 (plus interest to the date of actual payment), and payment of certain attorneys fees to the relators under the complaint. Payment was made on January 15, 2002, and the case has been dismissed with prejudice.

At this time Triad cannot predict the final effect or outcome of the ongoing investigations or *qui tam* action. If violations of Federal or state laws relating to Medicare, Medicaid or other government programs are found, then Triad may be required to pay substantial fines and civil and criminal damages and also may be excluded from participation in the Medicare and Medicaid programs and other government programs. Similarly, the amount of damages sought in the *qui tam* actions or in the future may be substantial. Triad could be subject to substantial costs resulting from defending, or from an adverse outcome in, any current or future investigations, administrative proceedings or litigation. In an effort to resolve one or more of these matters, Triad may choose to negotiate a settlement. Amounts paid to settle any of these matters may be material. Agreements entered into as a part of any settlement could also materially adversely affect Triad. Any current or future investigations or actions could have a material adverse effect on Triad s results of operations or financial position.

From time to time Triad may be the subject of additional investigations or a party to additional litigation which alleges violations of law. Triad may not know about those investigations, or about *qui tam* actions filed against it unless and to the extent such are unsealed. If any of those matters were successfully asserted against Triad, there could be a material adverse effect on Triad s business, financial position, results of operations or prospects.

Stockholder Class Action Regarding the Securities Exchange Act of 1934

Quorum was a defendant in a lawsuit filed by certain of its stockholders alleging that Quorum violated Federal securities laws by materially inflating its net revenues through inclusion of amounts received from the settlement of cost reports allegedly filed in violation of applicable Medicare regulations. The parties agreed to submit the lawsuit to non-binding mediation. Quorum had accrued an estimated liability on this item prior to the merger. During the second quarter of 2002, the parties agreed to a settlement and made payment on the settlement in June 2002.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 16 CONTINGENCIES (continued)

Income Taxes

The IRS is in the process of conducting an examination of the federal income tax returns of Triad for the calendar years ended December 31, 1999 and 2000, and the federal income tax returns of Quorum for the fiscal years ended June 30, 1999 and 2000. To date the IRS has not proposed any adjustments.

The IRS has proposed adjustments with respect to partnership returns of income for certain joint ventures in which Quorum owned a majority interest for the fiscal years ended June 30, 1997 and 1998. The most significant adjustments involve the tax accounting methods adopted for computing bad debt expense, the valuation of purchased hospital property and equipment and related depreciable lives, income recognition related to cost reports and the loss calculation on a taxable liquidation of a subsidiary. Triad has filed protests on behalf of the joint ventures with the Appeals Division of the IRS contesting substantially all of the proposed adjustments. In the opinion of management, the ultimate outcome of the IRS examinations will not have a material effect on Triad s results of operations or financial position.

HCA Litigation and Investigations

HCA is the subject of Federal investigations and litigation relating to its business practices. Given the breadth of the ongoing investigations, HCA expects continued investigative activity in the future. The investigations, actions and claims relate to HCA and its subsidiaries, including subsidiaries that, prior to the spin-off from HCA, owned facilities now owned by Triad. HCA is also the subject of a formal order of investigation by the Securities and Exchange Commission (SEC). HCA understands that the SEC s investigation includes the anti-fraud, insider trading, periodic reporting and internal accounting control provisions of the Federal securities laws.

HCA is a defendant in *qui tam* actions on behalf of the United States of America alleging, in general, submission of improper claims to the government for reimbursement. The lawsuits seek three times the amount of damages caused to the United States by the submission of any Medicare or Medicaid false claims presented by the defendants to the Federal government, civil damages of not less than $5,500 nor more than $11,000 for each such Medicare or Medicaid claim, attorneys fees and costs. HCA has disclosed that of the original 30 *qui tam* actions, the DOJ remains active in and has elected to intervene in eight actions. HCA also has disclosed that it is aware of additional *qui tam* actions that remain under seal and believes that there may be other sealed *qui tam* cases of which it is unaware.

On May 5, 2000, Triad was advised that one of the *qui tam* cases referenced above, which occurred prior to the spin-off, listed three of Triad s hospitals as defendants. This *qui tam* action alleges various violations arising out of the relationship between Curative Health Services and the other defendants, including allegations of false claims relating to contracts with Curative Health Services for the management of certain wound

care centers and excessive and unreasonable management fees paid to Curative Health Services and submitted for reimbursement. Two of the three Triad hospitals named as defendants terminated their relationship with Curative Health Services prior to the spin-off and the third hospital terminated its contract thereafter.

HCA is also a defendant in a number of other suits, which allege, in general, improper and fraudulent billing, overcharging, coding and physician referrals, as well as other violations of law. Certain of the suits have been conditionally certified as class actions. Since April 1997, numerous securities class action and derivative lawsuits have been filed against HCA and a number of its current and former directors, officers and/or employees alleging breach of fiduciary duty, and failure to take reasonable steps to ensure that HCA did not engage in illegal practices thereby exposing it to significant damages.

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 16 CONTINGENCIES (continued)

In December 2000, HCA entered into an agreement with the Criminal Division of the DOJ and various U.S. Attorney s Offices and a civil and administrative settlement agreement with the Civil Division of the DOJ. These agreements resolve only the specific Federal criminal issues outstanding against HCA and certain issues involving Federal civil claims by or on behalf of the government involving DRG coding, outpatient laboratory billing and home health issues. Civil issues that are not covered and remain outstanding include claims related to cost reports and physician relations issues. These agreements do not resolve any of the *qui tam* actions or any pending state actions.

In addition, 14 of Triad s current and former hospitals received notices in early 2001 from CMS that it was re-opening for examination cost reports for Medicare and Medicaid reimbursement filed by these hospitals for periods between 1993 and 1998, which pre-dates Triad s spin-off from HCA. Furthermore, two of Triad s hospitals formerly owned by Quorum have received such notices. HCA or its predecessors owned these hospitals during the period covered by the notices. HCA is obligated to indemnify Triad for liabilities arising out of cost reports filed during these periods.

On March 28, 2002, HCA announced that it had reached an understanding with CMS to resolve all Medicare cost report appeal issues between HCA and CMS on more than 2,600 cost reports for reporting periods from 1993 through July 31, 2001. The understanding, which is subject to approval of the Department of Justice and execution of a mutually satisfactory definitive written agreement, would require HCA to pay CMS the sum of $250 million. The understanding does not include resolution of outstanding civil issues with the DOJ and relators under HCA s various *qui tam* cases with respect to cost reports and physician relations.

In December 2002, HCA reached an understanding with the Civil Division of the DOJ to recommend an agreement to settle, subject to certain conditions, the litigation brought by the Division against HCA, including the remaining outstanding issues of cost reports and physician relations, in exchange for a payment by HCA of $631 million, plus interest. HCA has stated that this understanding, which is subject to approvals by senior DOJ officials and execution of definitive documents, would effectively end the Division s investigation of HCA. HCA also agreed in principle with representatives of states that may have similar claims against HCA to pay $17.5 million to resolve these claims. HCA will also pay the legal fees of certain whistleblowers attorneys.

Triad is unable to predict the effect or outcome of any of the ongoing investigations or *qui tam* and other actions, or whether any additional investigations or litigation will be commenced. In connection with the spin-off from HCA, Triad entered into a distribution agreement with HCA (see NOTE 15). The terms of the distribution agreement provide that HCA will indemnify Triad for any losses (other than consequential damages) which it may incur as a result of the proceedings described above. HCA has also agreed to indemnify Triad for any losses (other than consequential damages) which it may incur as a result of proceedings which may be commenced by government authorities or by private parties in the future that arise from acts, practices or omissions engaged in prior to the date of the spin-off and that relate to the proceedings described above. HCA has also agreed that, in the event that any hospital owned by Triad at the time of the spin-off is permanently excluded from participation in the Medicare and Medicaid programs as a result of the proceedings described above, then HCA will make a cash payment to Triad, in an amount (if positive) equal to five times the excluded hospital s 1998 income from continuing operations before depreciation and amortization, interest expense, management fees, impairment of long-lived assets, minority interests and income taxes, as set forth on a schedule to the distribution agreement, less the net proceeds of the sale or other disposition of the excluded hospital.

HCA will not indemnify Triad under the distribution agreement for losses relating to any acts, practices and omissions engaged in by Triad after the spin-off date, whether or not Triad is indemnified for similar acts, practices and omissions occurring prior to the spin-off. HCA also will not indemnify Triad under the distribution agreement for similar *qui tam* litigation, governmental investigations and other actions to which Quorum was subject, some of

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 16 CONTINGENCIES (continued)

which are described above. If indemnified matters were asserted successfully against Triad or any of its facilities, and HCA failed to meet its indemnification obligations, then this event could have a material adverse effect on Triad s business, financial condition, results of operations or prospects.

The extent to which Triad may or may not continue to be affected by the ongoing investigations of HCA and the initiation of additional investigations, if any, cannot be predicted. These matters could have a material adverse effect on Triad s business, financial condition, results of operations or prospects.

General Liability Claims

Triad is subject to claims and suits arising in the ordinary course of business, including claims for personal injuries or wrongful restriction of, or interference with, physicians staff privileges. In certain of these actions the claimants may seek punitive damages against Triad, which are usually not covered by insurance. It is management s opinion that the ultimate resolution of these pending claims and legal proceedings will not have a material adverse effect on Triad s results of operations or financial position.

NOTE 17 SEGMENT AND GEOGRAPHIC INFORMATION

Triad through its affiliates operates hospitals and related health care entities. During the years ended December 31, 2002, 2001 and 2000, approximately 32.0%, 32.2%, and 29.6%, respectively, of Triad s revenues related to patients participating in the Medicare program.

Triad has structured its operations into two segments. The owned operations segment includes Triad s acute care hospitals and related health care entities. The management services segment provides executive management services to independent acute care hospitals.

The distribution of Triad s revenues, EBITDA (which is used by management for operating performance review, see (a)) and assets are summarized in the following tables (dollars in millions):

	For the years ended December 31,

	2002	2001	2000
Revenues:			
Owned operations	$ 3,375.2	$ 2,546.1	$ 1,218.2
Management services	139.8	95.5	
Corporate and other	26.1	27.9	17.3
	$ 3,541.1	$ 2,669.5	$ 1,235.5

	2002	2001	2000
EBITDA (a):			
Owned operations	$ 557.7	$ 374.9	$ 170.8
Management services	21.2	15.3	
Corporate and other	(30.1)	(29.1)	3.2
	$ 548.8	$ 361.1	$ 174.0

	December 31,	
	2002	2001
Assets:		
Owned operations	$ 3,927.5	$ 3,739.7
Management services	143.8	154.9
Corporate and other	310.3	270.7
	$ 4,381.6	$ 4,165.3

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 17 SEGMENT AND GEOGRAPHIC INFORMATION (continued)

EBITDA for owned operations includes equity in earnings (loss) of affiliates of $21.7 million, $14.5 million and $(1.4) million in years ended December 31, 2002, 2001 and 2000, respectively.

A reconciliation of EBITDA to income from operations before income taxes follows (in millions):

	For the years ended December 31,		
	2002	2001	2000
Total EBITDA for reportable segments	$ 548.8	$ 361.1	$ 174.0
Depreciation	161.4	134.4	76.1
Amortization	6.0	35.7	7.1
Interest expense	136.7	127.6	62.2
Interest income	(1.7)	(1.6)	(4.9)
ESOP expense	10.8	9.3	7.1
Litigation settlements	(10.4)		
Gain on sales of assets	(4.5)	(23.1)	(7.9)
Impairment of long-lived assets		23.1	8.0
Minority interests in earnings of consolidated entities	14.8	7.2	9.0
Income from operations before income taxes	$ 235.7	$ 48.5	$ 17.3

(a) EBITDA is defined as earnings before depreciation, amortization, interest expense, interest income, ESOP expense, litigation settlements, gain on sales of assets, impairment of long-lived assets, minority interests in earnings of consolidated entities, income tax provision and extraordinary loss. EBITDA is used by management to evaluate financial performance and resource allocation for each facility and for Triad as a whole. EBITDA is commonly used as an analytical indicator within the health care industry, and also serves as a measure of leverage capacity and debt service ability. EBITDA should not be considered as a measure of financial performance under generally accepted accounting principles, and the items excluded from EBITDA are significant components in understanding and assessing financial performance. EBITDA should not be considered in isolation or as an alternative to net income, cash flows generated by operating, investing or financing activities or financial statement data presented in the consolidated financial statements as an indicator of financial performance or liquidity. Because EBITDA is not a measurement determined in accordance with generally accepted accounting principles and is thus susceptible to varying calculations, EBITDA as presented may not be comparable to other similarly titled measures of other companies.

NOTE 18 OTHER CURRENT LIABILITIES AND ALLOWANCES FOR DOUBTFUL ACCOUNTS

A summary of other current liabilities as of December 31 follows (in millions):

	2002	2001
Due to HCA	$ 1.6	$ 2.1
Employee retirement plan	20.9	17.8
Taxes, other than income	17.4	19.3
Accrued interest	13.7	13.9
Self insured employee benefit programs	29.5	23.2
Current portion of professional liability risk	18.6	8.7
Deferred income	3.8	4.0
Other	26.5	44.0
	$ 132.0	$ 133.0

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TRIAD HOSPITALS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 OTHER CURRENT LIABILITIES AND ALLOWANCES FOR DOUBTFUL ACCOUNTS (continued)

A summary of activity in Triad s allowances for doubtful accounts follows (in millions):

	Balances at Beginning of Period	Additions Charged to Expense	Accounts Written off, Net of Recoveries	Acquisition	Sales	Balances at End of Period
Allowances for doubtful accounts:						
Year ended December 31, 2000	$ 156.7	$ 103.6	$ (137.4)			$ 122.9
Year ended December 31, 2001	$ 122.9	$ 239.9	$ (234.7)	$ 74.6	$ (10.3)	$ 192.4
Year ended December 31, 2002	$ 192.4	$ 272.8	$ (290.8)			$ 174.4

NOTE 19 UNAUDITED QUARTERLY FINANCIAL INFORMATION

The quarterly interim financial information shown below has been prepared by Triad s management and is unaudited. It should be read in conjunction with the audited consolidated financial statements appearing herein (dollars in millions, except per share amounts).

	2002			
	First	Second	Third	Fourth
Revenues	$ 860.9	$ 867.2	$ 894.0	$ 919.0
Net income	$ 40.4	$ 32.8	$ 32.6	$ 35.7
Basic net income per share	$ 0.58	$ 0.46	$ 0.45	$ 0.49
Diluted net income per share	$ 0.55	$ 0.44	$ 0.43	$ 0.47

	2001			
	First	Second	Third	Fourth
Revenues	$ 365.8	$ 643.2	$ 829.5	$ 831.0
Net income (loss)	$ 7.8	$ (21.3)(a)	$ 6.5	$ 9.8(b)
Basic net income (loss) per share	$ 0.24	$ (0.36)(a)	$ 0.09	$ 0.14(b)
Diluted net income (loss) per share	$ 0.22	$ (0.36)(a)	$ 0.09	$ 0.13(b)

(a) During the second quarter of 2001, Triad recorded $31.8 million of charges associated with coordinating Quorum s accounting policies, practices and estimation processes with those of Triad and a $2.4 million, net of tax benefit, extraordinary loss on retirement of debt.

(b) During the fourth quarter of 2001, Triad recorded $6.5 million pre-tax reduction to expense related to preliminary purchase price allocations, $23.1 million pre-tax charges related to impairment of certain long-lived assets, a $22.0 million pre-tax gain on sale of assets and a $0.8 million, net of tax benefit, extraordinary loss on retirement of debt.