

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Consolidated Financial Statements

December 31, 2006 and 2005

(With Independent Auditors' Report Thereon)

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Table of Contents

	Page
Independent Auditors' Report	1
Consolidated Statements of Financial Position	2
Consolidated Statements of Activities	3
Consolidated Statements of Cash Flows	4
Notes to Consolidated Financial Statements	5



KPMG LLP
303 East Wacker Drive
Chicago, IL 60601-5212

Independent Auditors' Report

The Board of Commissioners
The Joint Commission on Accreditation of
Healthcare Organizations:

We have audited the accompanying consolidated statements of financial position of The Joint Commission on Accreditation of Healthcare Organizations and Affiliates (The Joint Commission) as of December 31, 2006 and 2005, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of The Joint Commission's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Joint Commission on Accreditation of Healthcare Organizations and Affiliates as of December 31, 2006 and 2005, and the changes in their net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

As described in note 5 to the financial statements, effective December 31, 2006, The Joint Commission adopted Statement of Financial Accounting Standard No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*.

KPMG LLP

April 30, 2007

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Consolidated Statements of Financial Position

December 31, 2006 and 2005

Assets	2006	2005
Current assets:		
Cash and cash equivalents	\$ 10,111,132	10,890,103
Short-term investments (note 4)	747,946	10,766,759
Accounts receivable – net of allowance for doubtful accounts of \$559,000 and \$808,000 in 2006 and 2005, respectively	16,952,531	12,673,525
Publications inventory – net	880,923	815,804
Prepaid expenses	1,800,938	1,351,144
Total current assets	<u>30,493,470</u>	<u>36,497,335</u>
Investments (note 4)	102,388,020	83,800,442
Property and equipment:		
Land	4,204,400	4,204,400
Building	27,098,676	26,692,823
Office systems, furniture, and equipment	30,805,104	26,622,190
Total property and equipment	<u>62,108,180</u>	<u>57,519,413</u>
Less accumulated depreciation and amortization	<u>(29,681,884)</u>	<u>(26,235,378)</u>
Total property and equipment – net	32,426,296	31,284,035
Overfunded pension benefits (note 5)	542,528	—
Unamortized debt issuance costs	562,563	655,568
Total assets	<u>\$ 166,412,877</u>	<u>152,237,380</u>
Liabilities and Net Assets		
Current liabilities:		
Current maturity of note payable (note 2)	\$ 1,360,000	1,250,000
Accounts payable	5,887,381	7,039,510
Accrued expenses:		
Compensation and benefits	6,321,235	6,514,434
Other expenses	865,392	848,015
Deferred revenue:		
Accreditation fees and deposits	1,683,046	107,130
Publications, educational programs and other advances	3,550,161	3,964,939
Current portion of accrued postretirement benefits (note 5)	1,671,116	—
Total current liabilities	<u>21,338,331</u>	<u>19,724,028</u>
Noncurrent liabilities:		
Note payable – less current maturity (note 2)	25,195,000	26,555,000
Accrued pension and postretirement benefits (note 5)	7,587,928	8,832,497
Fair value of hedge – interest rate swap (note 2)	1,521,204	1,902,978
Other noncurrent liabilities	613,175	703,455
Total noncurrent liabilities	<u>34,917,307</u>	<u>37,993,930</u>
Total liabilities	56,255,638	57,717,958
Commitments and contingencies (notes 2, 3, and 7)		
Unrestricted net assets	<u>110,157,239</u>	<u>94,519,422</u>
Total liabilities and net assets	<u>\$ 166,412,877</u>	<u>152,237,380</u>

See accompanying notes to consolidated financial statements.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Consolidated Statements of Activities

Years ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Revenue:		
Annual accreditation subscription fees (note 1)	\$ 46,299,198	—
On-site survey fees (note 1)	47,778,194	93,898,162
Publications and multimedia	15,954,281	14,168,833
Educational programs	7,145,792	7,008,695
Consultative technical assistance	8,864,373	8,893,410
Continuous service readiness	4,150,074	3,945,682
Performance measurement activities	3,053,546	2,920,014
Other	6,419,234	6,690,977
	<u>139,664,692</u>	<u>137,525,773</u>
Expenses:		
Salaries and benefits	86,595,267	81,285,945
Travel costs	18,059,389	16,249,783
Publishing and printing	4,157,663	4,283,257
Occupancy	3,467,369	3,825,446
Fees and services	8,811,833	7,711,426
Depreciation and amortization	4,179,406	4,038,698
General and administrative (note 8)	10,525,041	12,377,702
	<u>135,795,968</u>	<u>129,772,257</u>
Excess of revenue over expenses before investment income	3,868,724	7,753,516
Investment income (note 4)	5,517,536	3,411,534
	<u>9,386,260</u>	<u>11,165,050</u>
Other changes in unrestricted net assets:		
Net unrealized investment gains (note 4)	6,211,820	1,458,243
Change in fair value of hedge – interest rate swap (note 2)	381,774	605,586
Minimum pension liability adjustment (note 5)	5,525,693	(892,605)
Cumulative effect of change in accounting principle	(5,867,730)	—
	<u>15,637,817</u>	<u>12,336,274</u>
Net assets – beginning of year	94,519,422	82,183,148
Net assets – end of year	<u>\$ 110,157,239</u>	<u>94,519,422</u>

See accompanying notes to consolidated financial statements.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Consolidated Statements of Cash Flows

Years ended December 31, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Change in net assets	\$ 15,637,817	12,336,274
Adjustment to reconcile change in net assets to net cash flows provided by operating activities:		
Realized investment gains	(3,092,310)	(1,567,130)
Unrealized investment gains	(6,211,820)	(1,458,243)
Change in fair value of hedge – interest rate swap	(381,774)	(605,586)
Minimum pension liability adjustment	(5,525,693)	892,605
Cumulative effect of change in accounting principle	5,867,730	—
Loss on funding agreements with joint ventures	—	252,500
Depreciation and amortization	4,179,406	4,038,698
Changes in assets and liabilities:		
Accounts receivable	(4,279,006)	(1,457,071)
Accounts payable and accrued expenses	(1,327,951)	3,402,869
Deferred revenue	1,161,138	240,924
Accrued pension and postretirement benefits	(458,018)	(3,588,236)
Other assets and liabilities	(605,193)	(390,662)
Net cash flows provided by operating activities	4,964,326	12,096,942
Cash flows from investing activities:		
Purchases of investments	(46,144,975)	(296,243,938)
Sales and maturities of investments	46,880,340	291,758,878
Advances to joint ventures	—	127,500
Additions to property and equipment	(5,228,662)	(6,339,375)
Net cash flows used in investing activities	(4,493,297)	(10,696,935)
Net cash flows used in financing activities:		
Principal payments of note payable	(1,250,000)	(1,155,000)
Net increase (decrease) in cash and cash equivalents	(778,971)	245,007
Cash and cash equivalents – beginning of year	10,890,103	10,645,096
Cash and cash equivalents – end of year	\$ 10,111,132	10,890,103
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	\$ 1,124,755	1,163,154

See accompanying notes to consolidated financial statements.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

(1) Nature of Organization and Summary of Significant Accounting Policies

(a) *Nature of the Organization*

The Joint Commission on Accreditation of Healthcare Organizations (the Joint Commission) is a not-for-profit organization that seeks to continuously improve the safety and quality of care provided to the public through the provision of healthcare accreditation and related services that support performance improvement in healthcare organizations. Together, annual accreditation subscription fees and on-site survey fees account for the largest portion of the Joint Commission's total revenue.

(b) *Principles of Consolidation*

The consolidated financial statements include the accounts of The Joint Commission and its wholly controlled affiliate, Joint Commission Resources, Inc. (JCR). JCR is a not-for-profit organization that was established for the purpose of independently assisting healthcare organizations in improving the quality of their services. JCR accomplishes this objective through the provision of publications and periodicals, educational programs, consultative technical assistance, contracted evaluation services, subscription readiness services, and international accreditation. An additional controlled affiliate, JCAHO Surveyor and QHR Consultant Corporation, administers an employment program for the Joint Commission and is also included in the accompanying consolidated financial statements. All intercompany transactions and balances have been eliminated in the consolidated financial statements.

(c) *Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities; disclosure of contingent assets and liabilities at the date of the financial statements; and the reported amounts of revenue and expenses during the reporting period. Actual results may differ from those estimates.

(d) *Cash and Cash Equivalents*

For purposes of reporting, all cash and investments with a maturity at the date of purchase of three months or less are considered cash and cash equivalents.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

(e) Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value based on quoted market prices in the consolidated statements of financial position. Investments in common and collective trust funds that invest in publicly traded securities are carried at fair value as determined by the fund manager based on the Joint Commission's proportionate interest in the fund at December 31. Interest and dividend income and realized gains and losses on sales of investments are reported as investment income or loss, while unrealized gains (losses) are reported separately in the accompanying consolidated statements of activities as a component of other changes in unrestricted net assets. Short-term investments have maturities of less than one year. Long-term investments have maturities of more than one year.

(f) Publications Inventory

Publications offered for sale or used in educational programs are stated at the lower of cost (first-in, first-out) or market, net of an allowance for excess and obsolete inventory, in the amounts of approximately \$428,000 and \$387,000 at December 31, 2006 and 2005, respectively.

(g) Property and Equipment

Property and equipment are stated at cost and are depreciated over their estimated useful lives using the straight-line method, as follows:

Building	40 years
Office systems, furniture, and equipment	3-15 years
Leasehold improvements	life of lease

Betterments, improvements, and repairs that extend the useful life of an asset and exceed \$1,000 are capitalized. Routine repairs and maintenance are expensed as incurred.

The Joint Commission accounts for long-lived assets in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. This statement requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

(h) System Development Costs

The Joint Commission capitalizes certain costs of business systems developed or obtained for internal use, consistent with the provisions of Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*. Such system development costs, which include external direct costs of materials and services and payroll costs for employees directly associated with system development projects, are amortized over a three- or five-year period using the straight-line method.

(i) Debt Issuance Costs

Financing and other costs incurred in connection with the issuance of long-term debt are amortized over the life of the debt using the effective interest method.

(j) Derivative Instruments and Hedging Activities

Effective January 1, 2001, the Joint Commission adopted SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. The derivative financial instrument used by the Joint Commission is an interest rate swap, in which a counterparty agrees to make variable payments based on a market interest rate (index rate). The fair value of the swap is included in noncurrent liabilities in the accompanying consolidated statements of financial position. The Joint Commission entered into the interest rate swap to hedge its exposure to fluctuations of the variable rate interest payments that relate to the Joint Commission's outstanding variable rate debt. Management reports the change in the fair value of the swap as a change in unrestricted net assets in the accompanying consolidated statements of activities.

(k) Revenue

Prior to January 1, 2006, domestic accreditation revenues were reported in the consolidated statements of activities as on-site survey fees. These survey fees were primarily derived from triennial on-site accreditation surveys that had been performed in the reporting period. As of January 1, 2006, organizations agree to pay an annual subscription fee for their participation in the ongoing services provided by The Joint Commission. In addition, organizations agree to pay an add-on fee in those years in which on-site surveys are conducted. Revenue from annual accreditation subscription fees is recognized ratably over the period to which the subscription fees relate. On-site survey fees are recognized in the period when the on-site surveys are conducted.

Revenue from consultative technical assistance, educational programs, and continuous service readiness is recognized when the related services are provided. Revenue from the sale of publications and multimedia is recognized when the related goods have been delivered and risk of loss has passed to the customer, persuasive evidence of an arrangement exists, the sales price is determinable, and collection of the related receivable is reasonably assured. Advance collections and deposits are recorded as deferred revenue in the accompanying consolidated statements of financial position.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

(l) Income Taxes

The Internal Revenue Service has determined that the Joint Commission and its consolidated affiliates are exempt from federal income taxation under Section 501(c)(3) of the Internal Revenue Code. The Joint Commission and its consolidated affiliates are subject to income taxes only on income determined to be unrelated business taxable income.

(m) Foreign Currency

Transaction gains and losses resulting from settlement in foreign currency are recorded in the period in which the transaction occurs and are recorded as investment income (loss) in the accompanying statements of activities. During 2006 gains totaling \$66,516 and in 2005 losses totaling \$(65,654), were recorded.

(n) New Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Post-retirement Plans* (SFAS 158). SFAS 158 requires an employer to recognize the over funded or under funded status of defined benefit pension and other postretirement plans as an asset or liability in its statement of financial position at year-end, and to recognize changes in the funded status directly to unrestricted net assets in the year in which the changes occur. The Joint Commission was required to adopt SFAS 158 by December 31, 2007, however The Joint Commission elected early adoption as of December 31, 2006 as permitted by SFAS 158.

In September 2006, the Financial Accounting Standards Board issued SFAS No. 157, *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements and is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Joint Commission does not expect the adoption of SFAS 157 will have a significant effect on the consolidated financial statements.

(o) Reclassifications

Certain reclassifications have been made to the 2005 consolidated financial statements to conform to the 2006 presentation.

(2) Note Payable and Interest Rate Swap

In October 1988, the Joint Commission entered into a Financing Agreement (the Agreement) with the City of Elmhurst, Illinois (the City) to finance the acquisition of land and the construction and furnishing of a new office building, as well as costs the Joint Commission might incur in exiting existing long-term lease agreements and in moving its operations to the new facility. Pursuant to the Agreement, the City issued \$37,000,000 of its tax-exempt Adjustable Demand Revenue Bonds and used the proceeds to purchase the Joint Commission's Adjustable Demand Note (the Note). The Joint Commission has occupied the office building since April 1990.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

Under the terms of the Note, the Joint Commission is required to pay principal and interest in amounts sufficient to cover principal and interest on the bonds issued by the City. As security for the Note and to ensure the City's ability to meet the terms of its related bonds, the Joint Commission provided the City a direct pay letter of credit of \$27,070,094. In so doing, the Joint Commission agreed to pay the bank issuance fees as well as an annual fee on the unused portion of the letter of credit. The rate in effect on the annual fee was 0.50% through January 19, 2005, 0.45% from January 20, 2005 to June 30, 2006, and 0.25% from July 1, 2006 to December 31, 2006. The current letter of credit, which expires in early 2008, contains provisions for further adjustments in the annual fee rate if certain conditions are met.

The Joint Commission and JCR are jointly and severally liable for amounts due to the issuing letter of credit bank. As security for the letter of credit, the Joint Commission has granted the issuing bank a first mortgage and security interest in virtually all of the Joint Commission's assets. Further, under the terms of the letter of credit agreement, the Joint Commission and JCR have agreed to meet various covenants on a consolidated basis, including maintenance of certain financial ratios and a minimum level of cash and investments.

The Note matures on July 1, 2018. Note redemption commenced on July 1, 1994, and will continue pursuant to the terms of the Agreement through maturity. In the event the agent is unable to remarket the bonds, the bonds become a demand note under the letter of credit. The Note is also subject to mandatory redemption upon expiration of the letter of credit in January 2008, unless a suitable alternative letter of credit is in place. The annual maturities of the Note are as follows:

2007	\$	1,360,000
2008		1,475,000
2009		1,600,000
2010		1,735,000
2011		1,885,000
Thereafter		<u>18,500,000</u>
Total	\$	<u><u>26,555,000</u></u>

Interest on the Note is variable and subject to weekly adjustments that parallel fluctuations in the municipal bond market. The effective interest rate on the Note was 3.47% in 2006 and 2.46% in 2005. The interest rate for nonpayment of principal or interest is the prime rate plus 2.00%. Under certain conditions described in the Agreement, the Joint Commission may convert its interest rate on the Note to a fixed interest rate or a floating rate that changes less frequently than weekly.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

The Joint Commission utilizes an interest rate swap agreement to reduce the risk associated with the weekly adjustment to the Note's interest rate. The interest rate swap agreement involves a declining notional amount that reflects two-thirds of the remaining principal balance of the Note. The following table summarizes the swap agreement terms in place and fair value during 2006 and 2005:

<u>Notional amount (in millions)</u>	<u>Expiration</u>	<u>Fixed rate</u>	<u>Fair value as of December 31,</u>	
			<u>2006</u>	<u>2005</u>
\$19.3 to \$17.7	2018	4.88%	\$ (1,521,204)	(1,902,978)

The Joint Commission made payments to a counterparty at a fixed rate of 4.88%, and in return, received payments based on 67% of a LIBOR index. Management continually monitors the credit rating of the counterparty, which is a large financial institution. Should nonperformance of the counterparty occur, interest costs would fluctuate with the weekly adjustable interest rate under the Note. The fair value of the swap is presented as a noncurrent liability in the consolidated statements of financial position.

Interest expense totaled \$1,123,217 in 2006 and \$1,103,583 in 2005, inclusive of interest rate swap settlement payments of \$176,918 and \$402,920 in 2006 and 2005, respectively. Interest expense is included in occupancy expense in the consolidated statements of operations.

The estimated fair value of debt obligations, as determined by the Joint Commission's bond remarketing agents, approximates the carrying value at December 31, 2006 and 2005.

(3) Leases

The Joint Commission primarily leases office space, laptop computers, printers, and copiers under operating lease arrangements. Lease terms generally range from 3 to 6 years and contain renewal or purchase options. During 2004, in connection with the relocation of its headquarters, JCR entered into a ten and one-half year operating lease for office space that includes a renewal option and scheduled rent increases. Rent expense is recognized over the life of the lease using the straight-line method. There are no leases that contain restrictions on the Joint Commission's ability to incur additional debt or engage in further leasing activities. JCR also leases office space in Italy, France, Dubai, and Singapore. Obligations in foreign currency are reflected in U.S. dollars as of December 31, 2006. Such obligations are subject to foreign currency exchange risk.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

Rent expense related to operating lease agreements was \$1,634,138 in 2006 and \$1,859,113 in 2005.

Obligations under operating leases having initial terms in excess of one year at current rates are as follows:

2007		\$	1,213,901
2008			891,593
2009			315,143
2010			273,385
2011			267,544
Thereafter			847,224
Total		\$	<u><u>3,808,790</u></u>

(4) Investments

The following table summarizes the types of investments and total return on investments as of and for the years ended December 31, 2006 and 2005:

		<u>2006</u>	<u>2005</u>
Type of investments:			
U.S. government and government agency securities	\$	3,842,945	23,557,940
Common and collective trust funds		39,657,898	6,621,105
Common stocks and stock funds		20,437,598	44,824,880
Corporate bonds, demand notes, and bond funds		<u>39,197,525</u>	<u>19,563,276</u>
Total investments – at fair value	\$	<u><u>103,135,966</u></u>	<u><u>94,567,201</u></u>
Return on investments:			
Interest income and dividends	\$	2,425,226	1,844,404
Realized gains on sales of investments, net		3,092,310	1,567,130
Unrealized market appreciation, net		<u>6,211,820</u>	<u>1,458,243</u>
Total return on investments	\$	<u><u>11,729,356</u></u>	<u><u>4,869,777</u></u>
Reported as:			
Investment income	\$	5,517,536	3,411,534
Net unrealized investment gains		<u>6,211,820</u>	<u>1,458,243</u>
Total return on investments	\$	<u><u>11,729,356</u></u>	<u><u>4,869,777</u></u>

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

(5) Retirement Plans and Other Post Retirement Benefits

The Joint Commission has a noncontributory account-based defined benefit pension plan (the Pension Plan) that covers substantially all of its employees. the Joint Commission's funding policy is to contribute to the Pension Plan an annual amount necessary to meet or exceed the minimum funding standards under the Employee Retirement Income Security Act.

The Joint Commission also sponsors nonqualified supplemental defined benefit retirement plans for certain key executives (the Supplemental Plans). Benefit cost under the Supplemental Plans is accrued based on actuarial estimates over the expected service period of key executives. The Supplemental Plans are not funded; however, marketable securities totaling \$7,930,634 and \$6,039,706 at December 31, 2006 and 2005, respectively, have been designated for the payment of benefits under the Supplemental Plans when due. Management expects to contribute amounts sufficient to pay benefits when due under the Supplemental Plans. The Joint Commission also provides certain executives with defined benefit postretirement healthcare benefits on an unfunded basis. The amounts included in "Other benefits" in the following tables include the Supplemental Plans and the defined benefit postretirement health care benefits.

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (SFAS 158), requires an employer to recognize the over funded or under funded status of defined benefit pension and other postretirement plans as an asset or liability in its statement of financial position at year-end, and to recognize changes in the funded status directly to unrestricted net assets in the year in which the changes occur. The Joint Commission was required to adopt SFAS 158 by December 31, 2007, however The Joint Commission elected early adoption as of December 31, 2006 as permitted by SFAS 158.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

The following tables set forth information on the funded status, amounts recognized in the consolidated financial statements, and weighted average assumptions related to the Joint Commission's Pension Plan and other postretirement defined benefit plans for the years ended December 31, 2006 and 2005:

	Pension Plan		Other benefits	
	2006	2005	2006	2005
Change in projected benefit obligation:				
Projected benefit obligation at				
beginning of year	\$ 26,886,377	23,805,062	7,555,490	8,611,878
Service cost	1,866,785	1,779,241	990,525	933,423
Interest cost	1,465,480	1,405,808	439,239	366,089
Actuarial (gain) loss	532,569	1,584,259	273,790	(197,301)
Benefits paid	(1,444,199)	(1,687,993)	—	(1,463,345)
Plan amendments	—	—	—	(695,254)
Projected benefit obligation at				
end of year	<u>\$ 29,307,012</u>	<u>26,886,377</u>	<u>\$ 9,259,044</u>	<u>7,555,490</u>
Change in fair value of plan assets:				
Fair value of plan assets				
at beginning of year	\$ 23,848,426	18,635,039		
Actual gain on plan assets	3,565,313	1,471,380		
Employer contributions	3,880,000	5,430,000		
Benefits paid	(1,444,199)	(1,687,993)		
Fair value of plan assets at end of year	<u>\$ 29,849,540</u>	<u>23,848,426</u>		
Funded status	<u>\$ 542,528</u>	(3,037,951)	<u>(9,259,044)</u>	(7,555,490)
Unrecognized net actuarial loss		7,625,595		(234,565)
Unrecognized prior service cost		—		(208,056)
Net amount recognized in the				
statements of financial position		<u>\$ 4,587,644</u>		<u>(7,998,111)</u>
Amounts recognized in the statements of				
financial position consist of:				
Noncurrent assets	\$ 542,528	—	—	—
Current liabilities	—	—	(1,671,116)	—
Noncurrent liabilities	—	(938,049)	(7,587,928)	(7,998,111)
Accumulated charge to unrestricted				
net assets	<u>6,030,289</u>	<u>5,525,693</u>	<u>(162,558)</u>	<u>—</u>
	<u>\$ 6,572,817</u>	<u>4,587,644</u>	<u>(9,421,602)</u>	<u>(7,998,111)</u>

The accumulated charge to unrestricted net assets as of December 31, 2006 represents charges or credits arising from the defined benefit plans, but not yet recognized as components of net periodic benefit cost. The accumulated charge to unrestricted net assets at December 31, 2006 of \$5,867,730 is comprised of \$6,059,342 of unrecognized net actuarial losses and \$191,611 of unrecognized prior service credits.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

During 2007, approximately \$309,000 is expected to be reclassified from the accumulated charge to unrestricted net assets for defined benefit plans to pension benefit cost.

The incremental effect for the adoption of SFAS 158 was an increase in accrued pension and postretirement benefits liability of \$5,867,730 with a corresponding decrease in unrestricted net assets. In addition, the noncurrent accrued pension and postretirement benefits liability was increased by \$543,528 through recognition of a noncurrent overfunded pension benefit asset and \$1,671,116 of the noncurrent liability was reclassified to current liabilities.

The accumulated benefit obligation for the pension plan was \$27,482,525 and \$24,786,475 at December 31, 2006 and 2005, respectively.

Net periodic benefit cost, which is calculated using the projected unit credit method, for the plans for the years ended December 31, 2006 and 2005 included the following components:

	<u>Pension Plan</u>		<u>Other benefits</u>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Components of net periodic benefit cost:				
Service cost	\$ 1,866,785	1,779,241	990,525	933,423
Interest cost	1,465,480	1,405,808	439,239	366,089
Expected return on plan assets	(1,927,874)	(1,554,709)	—	—
Net amortization of actuarial losses and prior service cost	490,436	451,187	(6,271)	(28,461)
Net periodic benefit cost	<u>\$ 1,894,827</u>	<u>2,081,527</u>	<u>1,423,493</u>	<u>1,271,051</u>

Weighted average assumptions:

Discount rate used to determine obligations at year-end	5.75%	5.50%	5.75%	5.50%
Discount rate used to determine net periodic benefit cost	5.50	5.50	5.50	5.50
Rate of compensation increase	4.75	4.75	4.75	4.75
Expected return on plan assets	8.00	8.00	—	—

The discount rates were selected by taking into account the rates of return on high quality fixed income securities as of the measurement date, using the Moody's Aa corporate bond index as a proxy for this rate. The duration of the liabilities calculated is similar to those from the Moody's Aa corporate bond index.

The assumed healthcare trend rates for the postretirement medical benefits were: 9% grading to 5% for 2006, and 10% grading to 5% for 2005. Actuarial gains and losses, calculated as the difference between estimates and actual amounts of plan assets and the projected benefit obligation, are amortized over the expected future service period. Prior service cost is amortized over the expected future service period.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

The Pension Plan's assets are invested according to target allocations, as outlined in the table below. Management seeks to maximize return with a minimal amount of risk by diversifying the risks of the portfolio over different industries and sectors. Management reviews this investment policy on an ongoing basis.

<u>Asset category</u>	<u>Target allocation</u>	<u>Percentage plan assets at December 31</u>	
		<u>2006</u>	<u>2005</u>
Equity securities	60-80%	72%	71%
Debt securities	20-40	28	29
Total		<u>100%</u>	<u>100%</u>

The expected return on plan assets, using a rate assumption of 8%, is based upon the average income that management anticipates a portfolio allocated according to the Joint Commission's target asset allocation will earn. Management monitors this assumption on an ongoing basis.

For the year ended December 31, 2007, there is no minimum funding requirement for the Plan; however, management expects to contribute \$2,500,000 to the Pension Plan. Estimated future benefit payments from the Pension Plan are as follows:

2007	\$ 2,200,000
2008	1,850,000
2009	2,520,000
2010	2,880,000
2011	2,340,000
2012 through 2015	<u>17,100,000</u>
Total	<u>\$ 28,890,000</u>

The Joint Commission expects to designate an additional \$1,680,000 in marketable securities during 2007 for the Supplemental Plans. Estimated annual future benefit payments from the Supplemental Plans are anticipated to range from \$1,035,000 to \$3,277,000 during the period from 2007 through 2011 and are expected to total \$2,955,000 during the period from 2012 through 2016.

The Joint Commission also sponsors a 401(k) Smart Saver Plan whereby employees may contribute between 1% and 20% of current earnings to the plan and the Joint Commission makes a matching contribution equal to 50% of the first 6% of annual salary contributed by the employee. The Joint Commission's expense under this plan was limited to its contributions, which were \$1,406,671 in 2006 and \$1,268,750 in 2005. The Joint Commission funds this plan on a current basis.

**THE JOINT COMMISSION ON ACCREDITATION
OF HEALTHCARE ORGANIZATIONS AND AFFILIATES**

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

(6) Functional Expenses

The Joint Commission provides services and products which promote patient safety and quality in the delivery of healthcare services. Expenses related to providing these services and products approximated 76% and 78% of total expenses in 2006 and 2005. Expenses incurred were for:

	Program services		Management and general		Total	
	2006	2005	2006	2005	2006	2005
Salaries and benefits	\$ 69,889,880	65,734,441	16,755,387	15,551,504	86,645,267	81,285,945
Travel costs	16,846,147	15,437,192	1,213,242	812,591	18,059,389	16,249,783
Publishing and printing	3,886,915	4,024,090	270,748	259,167	4,157,663	4,283,257
Occupancy	1,648,079	1,789,237	1,819,290	2,036,209	3,467,369	3,825,446
Fees and services	3,312,781	4,762,723	5,449,052	2,948,703	8,761,833	7,711,426
Depreciation and amortization	1,893,322	1,706,424	2,286,084	2,332,274	4,179,406	4,038,698
General and administrative	6,071,942	7,748,563	4,453,099	4,629,139	10,525,041	12,377,702
Total expenses	\$ 103,549,066	101,202,670	32,246,902	28,569,587	135,795,968	129,772,257

(7) Commitments and Contingencies

The Joint Commission is subject to legal proceedings and regulatory investigations arising in the course of its normal business activities. In the opinion of management, any such matters will be resolved without material adverse effect on the Joint Commission's financial position or results of operations.

(8) Joint Venture

In March 2003, the Joint Commission, in furtherance of its mission, entered into an agreement with a third-party tax-exempt nonprofit corporation to establish a not-for-profit corporation, the partnership for Human Research Protection, Inc. (PHRP), as a new accreditation program to protect the safety and rights of participants in clinical trials and research programs. Under the terms of the joint venture agreement, the Joint Commission made cash advances totaling \$1,212,500, of which \$252,500 were made in 2005. These advances were to be repaid once the new entity had sufficient operating revenues and met certain financial conditions. From inception to its termination in November 2005, PHRP recorded a loss from operations. Because of uncertainties in the ability of PHRP to repay the advances, the Joint Commission had fully reserved for all advances made through December 31, 2004, as well as for those made in 2005 prior to the termination of the joint venture. The resulting expense is included in 2005 general and administrative expenses.