



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

B49250

STATE BOARD OF ACCOUNTS
302 WEST WASHINGTON STREET
ROOM E418
INDIANAPOLIS, INDIANA 46204-2765

Telephone: (317) 232-2513
Fax: (317) 232-4711
Web Site: www.in.gov/sboa

December 28, 2017

Board of Trustees
Harrison County Hospital
1141 Hospital Drive, NW
Corydon, IN 47112

We have reviewed the report prepared by Harrison County Hospital and opined upon by Blue & Co., LLC, Independent Public Accountants, for the period January 1, 2016 to December 31, 2016. Per the *Report of Independent Auditors* the financial statements included in the report present fairly the financial condition of Harrison County Hospital as of December 31, 2016 and the results of its operations for the period then ended, on the basis of accounting described in the report.

In our opinion, Blue & Co., LLC prepared all required independent auditor's reports in accordance with generally accepted auditing standards and guidelines established by the State Board of Accounts.

The report is filed with this letter in our office as a matter of public record.

A handwritten signature in blue ink that reads "Paul D. Joyce".

Paul D. Joyce, CPA
State Examiner



**HARRISON COUNTY HOSPITAL
AND AFFILIATED ORGANIZATION**

CONSOLIDATED FINANCIAL STATEMENTS

AND

REQUIRED SUPPLEMENTARY INFORMATION

DECEMBER 31, 2016 AND 2015

CPAs / ADVISORS



HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

TABLE OF CONTENTS DECEMBER 31, 2016 AND 2015

	Page
Report of Independent Auditors	1
Required Supplementary Information	
Management’s Discussion and Analysis (Unaudited).....	i
Consolidated Financial Statements	
Consolidated Balance Sheets.....	3
Consolidated Statements of Operations.....	5
Consolidated Statements of Changes in Net Position.....	6
Consolidated Statements of Cash Flows.....	7
Notes to Consolidated Financial Statements.....	9



Blue & Co., LLC / 2650 Eastpoint Parkway, Suite 300 / Louisville, KY 40223
main 502.992.3500 fax 502.992.3509 email blue@blueandco.com

blueandco.com

REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Harrison County Hospital and
Affiliated Organization
Corydon, Indiana

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Harrison County Hospital and Affiliated Organization (collectively the "Hospital"), a component unit of Harrison County, Indiana, which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of operations, changes in net position, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of Harrison MOB, LLC ("MOB"), a majority-owned subsidiary, which statements reflect total assets of \$5,618,635 and \$5,856,294 as of December 31, 2016 and 2015, respectively, and total revenues of \$920,300 and \$925,851, respectively, for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the MOB, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the *Uniform Compliance Guidelines for Audits of Hospitals and State and Local Governments by Authorized Independent Public Accountants*, issued by the Indiana State Board of Accounts. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

Board of Trustees
Harrison County Hospital and
Affiliated Organization
Corydon, Indiana

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of December 31, 2016 and 2015, and the results of its operations, its changes in net position, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Blue & Co., LLC

Louisville, KY
November 10, 2017

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

Management's discussion and analysis of the financial performance of Harrison County Hospital ("HCH") and Affiliated Organizations, which include Harrison MOB, LLC ("the MOB"), (collectively described as "the Hospital") provides an overview of the Hospital's financial activities and performance for the years ended December 31, 2016 and 2015. This discussion and analysis should be read in conjunction with the accompanying the Hospital's consolidated financial statements.

FINANCIAL HIGHLIGHTS

The Hospital's net position increased \$1,184,351 from 2015 to 2016 and included income from operations of \$1,654,955. During 2016, the Hospital's total operating revenue increased by 5.8% to \$51,952,742, while total operating expenses increased to \$50,297,787. Non-operating expenses decreased by \$267,616, primarily due to lower interest due to the hospital's refinancing.

- The Hospital raised rates by 4.5% in 2016.
- In an effort to increase Medicaid reimbursement to hospitals, the State of Indiana implemented a Hospital Assessment Fee program in 2012. Indiana hospitals are assessed a fee which allows the state to access Federal funds allowing it to pay Medicaid patient claims at higher rates, not to exceed Medicare reimbursement. The Hospital incurred \$1,006,262 in Hospital Assessment Fees expense in 2016, an increase of \$258,154 over the \$748,108 incurred in 2015.
- An average 2.2% increase in wage and salary pay rates was implemented in May 2016.

FINANCIAL STATEMENTS

The consolidated financial statements of the Hospital present information about the Hospital using financial reporting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information. The consolidated balance sheet includes all of the Hospital's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to the Hospital's creditors (liabilities). It also provides the basis for compiling rate of return, evaluating the capital structure and assessing the liquidity and financial flexibility of the Hospital. All of the current and prior year's revenues and expenses are accounted for in the consolidated statement of operations. This statement measures the financial results of the Hospital's operations and presents revenues earned and expenses incurred. The consolidated statement of statement of changes in net position provide information concerning the components of changes to net position. In addition, this statement segregates the total amount of net position between controlling and noncontrolling interests. The consolidated statement of cash flows provides information about the Hospital's cash flows from operating activities, capital and related financing activities, and investing activities, plus provide information on the sources and uses of cash during both the current and prior year.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

FINANCIAL ANALYSIS

The consolidated balance sheet, consolidated statement of operations, and consolidated statement of changes in net position report information about the Hospital's activities. These three statements report the net position of the Hospital and its changes. Increases or decreases in the Hospital's net position are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in economic conditions, population changes (including uninsured and medically indigent individuals and families) and new or changed governmental legislation should also be considered.

CONDENSED FINANCIAL INFORMATION

A summary of the Hospital's consolidated balance sheets as of December 31, 2016 and 2015 is presented below:

	2016	2015	\$ Change	% Change
Assets				
Cash and investments	\$ 13,798,981	\$ 15,494,943	\$ (1,695,962)	-10.9%
Capital assets	32,340,214	33,947,300	(1,607,086)	-4.7%
Other assets	10,848,725	8,776,728	2,071,997	23.6%
Deferred outflows	286,581	308,563	(21,982)	-7.1%
Total assets and deferred outflows	<u>\$ 57,274,501</u>	<u>\$ 58,527,534</u>	<u>\$ (1,253,033)</u>	-2.1%
Liabilities				
Current liabilities	\$ 10,029,564	\$ 4,484,102	\$ 5,545,462	123.7%
Long-term liabilities	6,820,084	14,802,930	(7,982,846)	-53.9%
Total liabilities	16,849,648	19,287,032	(2,437,384)	-12.6%
Net position				
Net investment in capital assets	20,272,392	20,726,819	(454,427)	-2.2%
Restricted net position	-0-	1,683,185	(1,683,185)	-100.0%
Unrestricted	20,175,806	16,924,898	3,250,908	19.2%
Restricted non-expendable net position	(23,345)	(94,400)	71,055	75.3%
Total net position	<u>40,424,853</u>	<u>39,240,502</u>	<u>1,184,351</u>	3.0%
Total liabilities and net position	<u>\$ 57,274,501</u>	<u>\$ 58,527,534</u>	<u>\$ (1,253,033)</u>	-2.1%

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

A summary of the Hospital's consolidated balance sheets as of December 31, 2015 and 2014 is presented below:

	<u>2015</u>	<u>2014</u>	<u>\$ Change</u>	<u>% Change</u>
Assets				
Cash and investments	\$ 15,494,943	\$ 16,235,887	\$ (740,944)	-4.6%
Capital assets	33,947,300	37,173,051	(3,225,751)	-8.7%
Other assets	8,776,728	7,777,835	998,893	12.8%
Deferred outflows	<u>308,563</u>	<u>328,578</u>	<u>(20,015)</u>	-6.1%
Total assets and deferred outflows	<u>\$ 58,527,534</u>	<u>\$ 61,515,351</u>	<u>\$ (2,987,817)</u>	-4.9%
Liabilities				
Current liabilities	\$ 4,484,102	\$ 4,706,379	\$ (222,277)	-4.7%
Long-term liabilities	<u>14,802,930</u>	<u>15,636,896</u>	<u>(833,966)</u>	-5.3%
Total liabilities	19,287,032	20,343,275	(1,056,243)	-5.2%
Net position				
Investment in capital assets net of related debt	20,726,819	23,511,225	(2,784,406)	-11.8%
Restricted expendable net position	1,683,185	3,422,136	(1,738,951)	-50.8%
Unrestricted	16,924,898	14,392,858	2,532,040	17.6%
Restricted non-expendable net position	<u>(94,400)</u>	<u>(154,143)</u>	<u>59,743</u>	38.8%
Total net position	<u>39,240,502</u>	<u>41,172,076</u>	<u>(1,931,574)</u>	-4.7%
Total liabilities and net position	<u>\$ 58,527,534</u>	<u>\$ 61,515,351</u>	<u>\$ (2,987,817)</u>	-4.9%

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

A summary of the Hospital's consolidated statements of operations and changes in net position for the years ended December 31, 2016 and 2015 is presented below:

	2016	2015	\$ Change	% Change
Operating revenues				
Net patient service revenue	\$ 50,148,084	\$ 47,222,791	\$ 2,925,293	6.2%
Other revenue	<u>1,804,658</u>	<u>1,872,921</u>	<u>(68,263)</u>	-3.6%
Total operating revenues	51,952,742	49,095,712	2,857,030	5.8%
Operating expenses				
Salaries and benefits	29,512,500	29,413,513	98,987	0.3%
Supplies and drugs	5,902,482	5,571,392	331,090	5.9%
Depreciation and amortization	3,516,731	4,356,472	(839,741)	-19.3%
Other operating expenses	<u>11,366,074</u>	<u>10,948,058</u>	<u>418,016</u>	3.8%
Total operating expenses	<u>50,297,787</u>	<u>50,289,435</u>	<u>8,352</u>	0.0%
Income (loss) from operations	1,654,955	(1,193,723)	2,848,678	-238.6%
Nonoperating revenues (expenses)	(437,435)	(705,051)	267,616	38.0%
Member distributions	<u>(33,169)</u>	<u>(32,800)</u>	<u>(369)</u>	-1.1%
Change in net position	<u>\$ 1,184,351</u>	<u>\$ (1,931,574)</u>	<u>\$ 3,115,925</u>	161.3%
Net position, end of year	<u>\$ 40,424,853</u>	<u>\$ 39,240,502</u>	<u>\$ 1,184,351</u>	3.0%

A summary of the Hospital's consolidated statements of operations and changes in net position for the years ended December 31, 2015 and 2014 is presented below:

	2015	2014	\$ Change	% Change
Operating revenues				
Net patient service revenue	\$ 47,222,791	\$ 45,704,393	\$ 1,518,398	3.3%
Other revenue	<u>1,872,921</u>	<u>2,016,098</u>	<u>(143,177)</u>	-7.1%
Total operating revenues	49,095,712	47,720,491	1,375,221	2.9%
Operating expenses				
Salaries and benefits	29,413,513	27,616,789	1,796,724	6.5%
Supplies and drugs	5,571,392	5,572,263	(871)	0.0%
Depreciation and amortization	4,356,472	4,371,396	(14,924)	-0.3%
Other operating expenses	<u>10,948,058</u>	<u>10,981,237</u>	<u>(33,179)</u>	-0.3%
Total operating expenses	<u>50,289,435</u>	<u>48,541,685</u>	<u>1,747,750</u>	3.6%
Income from operations	(1,193,723)	(821,194)	(372,529)	45.4%
Nonoperating revenues (expenses)	<u>(705,051)</u>	<u>(1,013,941)</u>	<u>308,890</u>	30.5%
Member distributions	<u>(32,800)</u>	<u>(32,800)</u>	<u>-0-</u>	100.0%
Change in net position	<u>\$ (1,931,574)</u>	<u>\$ (1,867,935)</u>	<u>\$ (63,639)</u>	-3.4%
Net position, end of year	<u>\$ 39,240,502</u>	<u>\$ 41,172,076</u>	<u>\$ (1,931,574)</u>	-4.7%

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

SOURCES OF REVENUE

The Hospital derives the majority of its revenue from charges for patient care and related services. The Hospital is reimbursed for services from a variety of sources including the Medicare and Medicaid programs, insurance carriers, managed care plans, and patients. The Hospital has established payment arrangements with Medicare, Medicaid, and various commercial insurance carriers. Services provided under those arrangements are paid at predetermined rates and/or reimbursable cost as defined. Provisions have been made in the consolidated financial statements for contractual adjustments representing the difference between the standard charges for services and the actual or estimated payment.

The Hospital's percentages of gross revenue by payor for 2016, 2015 and 2014 are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Medicare	41 %	41 %	41 %
Medicaid	22	21	17
Blue Cross	17	16	15
Other third-party payors	18	19	18
Self-pay	<u>2</u>	<u>3</u>	<u>9</u>
Total	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

OPERATING AND FINANCIAL PERFORMANCE

The Hospital's financial performance from operations improved in 2016 in comparison to 2015. The Hospital's overall financial performance declined from 2014 to 2015. A discussion of the highlights of 2016 operations and changes in activity is presented below:

Revenues

Net patient service revenues of the Hospital increased by \$2,925,293 (6%) in 2016. Highlights of this are as follows:

- There was a 4.5% rate increase in 2016.
 - Contractual adjustments as a percent of gross revenue increased by 0.7% in 2016 due to impact of higher rates.
 - Gross revenues from the professional fees generated by Hospital-owned physician practices increased by \$914,287 (7%) in 2016 due to increased volumes primarily in Kids First Pediatrics. There was no rate increase for professional fees in 2016.
 - Patient volume increases for physician practices, After Hours Care, ambulance runs, emergency department, laboratory tests, and diagnostic imaging procedures.
-

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

Expenses

Total operating expenses increased by \$8,352 in 2016. Highlights of this increase are as follows:

- Salary costs increased by \$1,220,204 (5.3%) in 2016 over 2015. This was due to the annual pay rate increase, physician RVU bonuses, additional revenue staff for the physician practices, and employing a physician in the After Hours clinic.
- The total cost of Employee Benefits decreased by \$1,121,229 (17.8%) in 2016, primarily due to fewer health care and workers compensation claims on the hospital's self-insurance policies.
- Depreciation and Amortization decreased by \$839,406 (20.7%) due to the completed depreciation of the hospital's EHR system.
- The Hospital assessment fee increased by \$258,154 (34.5%) due to increased Medicaid volumes.

FINANCIAL ANALYSIS – CASH FLOWS

Net cash and cash equivalents decreased by \$1,991,023 in 2016. This is primarily due to the hospital's refinancing of its long-term debt and paying off its SWAP derivative.

Capital Assets

	2016	2015	\$ Change	% Change
Land and land improvements	\$ 6,380,571	\$ 6,341,056	\$ 39,515	0.6%
Leasehold improvements	3,605,135	3,605,135	-0-	0.0%
Buildings	40,884,171	40,874,173	9,998	0.0%
Equipment	26,949,510	25,436,742	1,512,768	5.9%
Construction in progress	420,580	101,507	319,073	314.3%
	<u>78,239,967</u>	<u>76,358,613</u>	<u>1,881,354</u>	<u>2.5%</u>
Less accumulated depreciation	<u>45,899,753</u>	<u>42,411,313</u>	<u>3,488,440</u>	<u>8.2%</u>
Capital assets, net	<u>\$ 32,340,214</u>	<u>\$ 33,947,300</u>	<u>\$ (1,607,086)</u>	<u>-4.7%</u>

	2015	2014	\$ Change	% Change
Land and land improvements	\$ 6,341,056	\$ 6,332,256	\$ 8,800	0.1%
Leasehold improvements	3,605,135	3,595,332	9,803	0.3%
Buildings	40,874,173	40,834,597	39,576	0.1%
Equipment	25,436,742	24,426,574	1,010,168	4.1%
Construction in progress	101,507	64,691	36,816	56.9%
	<u>76,358,613</u>	<u>75,253,450</u>	<u>1,105,163</u>	<u>1.5%</u>
Less accumulated depreciation	<u>42,411,313</u>	<u>38,080,399</u>	<u>4,330,914</u>	<u>11.4%</u>
Capital assets, net	<u>\$ 33,947,300</u>	<u>\$ 37,173,051</u>	<u>\$ (3,225,751)</u>	<u>-8.7%</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

The Hospital's capital assets increased \$1,881,354 in 2016. Major capital expenditures included \$135,012 for an ultrasound system, \$447,995 for a 3D mammography scanner, and \$102,000 for a portable x-ray machine.

See additional information on capital assets in the notes to the consolidated financial statements in footnote number 5.

Long-Term Debt

At December 31, 2016, the Hospital had total long-term debt (including \$5,494,042 current portion) of \$12,217,710. This is comprised of \$7,335,549 in Hospital revenue bonds outstanding and \$4,882,161 in MOB notes payable.

See additional information on long-term debt in the notes to the consolidated financial statements in footnote number 11.

ECONOMIC FACTORS AND 2017 BUDGET

The Hospital's Board and management considered many factors when establishing the 2017 budget. Included was the status of the economy, which takes into consideration market factors and other environmental factors such as the following items:

- Advances in medical equipment and information systems technology and the need to replace obsolete equipment
- Decreasing reimbursement from governmental and commercial insurance payors
- Changes in number of uninsured, underinsured and/or indigent patients
- Increasing costs of medical supplies and pharmaceuticals
- Nationwide workforce shortages in nursing and other healthcare specialist positions
- Increasing awareness and expectations from the public on the quality of services
- Increased competition from niche providers
- Size, composition, and needs of the Hospital's physician medical staff

CONTACTING THE HOSPITAL

This report is designed to provide our citizens, customers, and creditors with a general overview of the Hospital's finances. These consolidated financial statements include the activities of Harrison County Hospital ("HCH"), and Harrison MOB, LLC ("MOB"). Separately-issued audited financial statements are available for the MOB. If you have questions about this report or need additional information, contact Jeff Davis, Chief Financial Officer at 812-738-4251.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2016 AND 2015

	ASSETS	
	<u>2016</u>	<u>2015</u>
Current assets		
Cash and cash equivalents	\$ 5,349,449	\$ 7,696,622
Patient accounts receivable, net of estimated uncollectibles of \$5,521,421 in 2016 and \$4,676,068 in 2015	7,105,129	6,044,579
Inventories	1,088,603	1,108,496
Prepaid expenses and other current assets	1,100,017	1,454,953
Estimated third-party payor settlements	1,528,871	100,387
Other assets, current portion	14,423	25,000
Total current assets	<u>16,186,492</u>	<u>16,430,037</u>
Assets whose use is limited	8,449,532	7,798,321
Property and equipment, net	32,340,214	33,947,300
Other assets, net of current portion	<u>11,682</u>	<u>43,313</u>
Total assets	56,987,920	58,218,971
Deferred outflows - deferred loss on bond refunding	<u>286,581</u>	<u>308,563</u>
Total assets and deferred outflows	<u>\$ 57,274,501</u>	<u>\$ 58,527,534</u>

See accompanying notes to consolidated financial statements.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2016 AND 2015

LIABILITIES AND NET POSITION

	2016	2015
Current liabilities		
Accounts payable	\$ 1,521,097	\$ 1,669,628
Accrued personnel costs	2,291,626	1,853,598
Accrued expenses	548,680	369,369
Current portion of obligations under capital leases	40,277	38,309
Current portion of long-term debt	5,494,042	553,198
Interest rate swap	133,842	-0-
Total current liabilities	<u>10,029,564</u>	<u>4,484,102</u>
Long-term liabilities		
Obligations under capital leases, net of current portion	96,416	136,904
Long-term debt, net of current portion	6,723,668	12,800,633
Interest rate swap	-0-	1,865,393
Total long-term liabilities	<u>6,820,084</u>	<u>14,802,930</u>
Total liabilities	16,849,648	19,287,032
Net position		
Controlling interest net position		
Net investment in capital assets	20,272,392	20,726,819
Restricted		
Expendable for interest rate swaps	-0-	1,683,185
Unrestricted	<u>20,175,806</u>	<u>16,924,898</u>
Total controlling interest net position	40,448,198	39,334,902
Restricted net position - non-expendable	<u>(23,345)</u>	<u>(94,400)</u>
Total net position	<u>40,424,853</u>	<u>39,240,502</u>
Total liabilities and net position	<u>\$ 57,274,501</u>	<u>\$ 58,527,534</u>

See accompanying notes to consolidated financial statements.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

CONSOLIDATED STATEMENTS OF OPERATIONS YEARS ENDED DECEMBER 31, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
Operating revenues		
Net patient service revenue	\$ 50,148,084	\$ 47,222,791
Rent revenue	405,310	400,400
Other revenue	<u>1,399,348</u>	<u>1,472,521</u>
Total operating revenues	51,952,742	49,095,712
Operating expenses		
Salaries and wages	24,334,825	23,114,616
Employee benefits and payroll taxes	5,177,675	6,298,897
Professional medical fees	1,747,093	1,707,978
Medical supplies	3,290,912	2,939,827
Other supplies	1,081,870	1,010,931
Drugs	1,529,700	1,620,634
Purchased services	5,490,923	5,405,678
Utilities	1,238,445	1,212,106
Insurance	612,326	590,088
Depreciation and amortization	3,516,731	4,356,472
Hospital assessment fee	1,007,906	755,843
Other operating expenses	<u>1,269,381</u>	<u>1,276,365</u>
Total operating expenses	<u>50,297,787</u>	<u>50,289,435</u>
Income (loss) from operations	1,654,955	(1,193,723)
Nonoperating revenues (expenses)	<u>(437,435)</u>	<u>(705,051)</u>
Excess revenues (expenses)	1,217,520	(1,898,774)
Member distributions	<u>(33,169)</u>	<u>(32,800)</u>
Change in net position	1,184,351	(1,931,574)
Net position, beginning of year	<u>39,240,502</u>	<u>41,172,076</u>
Net position, end of year	<u>\$ 40,424,853</u>	<u>\$ 39,240,502</u>

See accompanying notes to consolidated financial statements.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

CONSOLIDATED STATEMENTS OF CHANGES IN NET POSITION YEARS ENDED DECEMBER 31, 2016 AND 2015

	Controlling Interest	Restricted Net Position - Non-Expendable	Total
Net position balances			
December 31, 2014	\$ 41,326,219	\$ (154,143)	\$ 41,172,076
Excess revenues (expenses)	(1,991,317)	92,543	(1,898,774)
Distributions	-0-	(32,800)	(32,800)
Change in net position	(1,991,317)	59,743	(1,931,574)
December 31, 2015	\$ 39,334,902	\$ (94,400)	\$ 39,240,502
Excess revenues (expenses)	1,113,296	104,224	1,217,520
Distributions	-0-	(33,169)	(33,169)
Change in net position	1,113,296	71,055	1,184,351
December 31, 2016	<u>\$ 40,448,198</u>	<u>\$ (23,345)</u>	<u>\$ 40,424,853</u>

See accompanying notes to consolidated financial statements.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
Operating activities		
Cash received for patient services	\$ 47,659,050	\$ 47,015,629
Cash paid to/for employees	(29,074,472)	(29,870,315)
Cash paid to vendors and suppliers	(16,875,450)	(17,117,669)
Other receipts, net	1,804,658	1,872,921
Net cash flows from operating activities	3,513,786	1,900,566
Noncapital financing activities		
Noncapital contributions	25,508	4,483
Capital and related financing activities		
Principal payments on obligations under capital leases	(38,520)	(43,302)
Principal payments on long-term debt	(8,636,121)	(530,452)
Interest paid	(893,346)	(1,017,010)
Purchase of capital assets	(1,880,434)	(993,103)
Proceeds from sale of capital assets	9,097	-0-
Gain on disposal of capital assets	(8,597)	-0-
Payments on interest rate swap	(1,555,200)	-0-
Borrowings on long-term debt	7,500,000	-0-
Change in deferred outflows	21,982	20,015
Member distributions	(33,169)	(32,800)
Net cash flows from capital and related financing activities	(5,514,308)	(2,596,652)
Investing activities		
Investment income	145,014	39,834
Other nonoperating revenues (expenses)	109,038	(65,137)
Change in assets whose use is limited	(295,061)	(884,433)
Change in other assets	25,000	(24,038)
Net cash flows from investing activities	(16,009)	(933,774)
Net change in cash and cash equivalents	(1,991,023)	(1,625,377)
Cash and cash equivalents, beginning of year	14,610,510	16,235,887
Cash and cash equivalents, end of year	\$ 12,619,487	\$ 14,610,510
Reconciliation of cash and cash equivalents to the balance sheets		
Cash and cash equivalents in current assets	\$ 5,349,449	\$ 7,696,622
Cash and cash equivalents in assets whose use is limited	7,270,038	6,913,888
Total cash and cash equivalents	\$ 12,619,487	\$ 14,610,510

See accompanying notes to consolidated financial statements.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
Reconciliation of income from operations to net cash flows from operating activities		
Income (loss) from operations	\$ 1,654,955	\$ (1,193,723)
Adjustments to reconcile income (loss) from operations to net cash flows from operating activities		
Depreciation	3,499,523	4,339,265
Amortization	17,208	17,207
Provision for bad debts	5,967,387	(4,547,236)
Changes in operating assets and liabilities		
Patient accounts receivable	(7,027,937)	4,215,461
Inventories	19,893	(246,916)
Prepaid expenses and other current assets	354,936	(537,984)
Accounts payable	(161,034)	458,308
Accrued personnel costs	438,028	(456,802)
Accrued expenses	179,311	(271,627)
Estimated third-party payor settlements	(1,428,484)	124,613
Net cash flows from operating activities	<u>\$ 3,513,786</u>	<u>\$ 1,900,566</u>
Supplemental disclosures of noncash activities		
Property and equipment acquired included in accounts payable	\$ 12,503	\$ 8,017
Property and equipment acquired under capital lease obligations	\$ -0-	\$ 112,394
Change in interest rate swap	\$ (176,351)	\$ (332,779)

See accompanying notes to consolidated financial statements.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Harrison County Hospital ("HCH") is a not-for-profit, acute care hospital located in Corydon, Indiana. The Hospital is county owned and operates under the Indiana County Hospital Law, Indiana Code 16-22. The Hospital is organized for the purpose of providing healthcare services to the residents of Harrison County and the surrounding area. The Hospital's primary sources of support are from patient revenues and other ancillary income. Patient revenues include funds received from Medicare, state agencies, insurance companies, and the patients themselves.

Harrison MOB, LLC ("MOB") is a limited liability company that is majority-owned by the Hospital and minority-owned by individual physicians. MOB was organized to construct, own, and operate a medical office building adjacent to the Hospital in Corydon, Indiana. MOB's primary source of revenue is from rental income.

The significant accounting policies followed by HCH and MOB (collectively the "Hospital") in the preparation of the consolidated financial statements are summarized below:

Reporting Entity and Consolidation Policy

The accompanying consolidated financial statements include the accounts of HCH and MOB. The Board of County Commissioners of Harrison County appoints the Governing Board of HCH and a financial benefit/burden relationship exists between the County and HCH. For these reasons, the HCH is considered a component unit of Harrison County. Similarly, due to its organized purpose, MOB is considered a blended component unit of HCH. Intercompany transactions and balances have been eliminated in consolidation. The separate audited financial statements of MOB may be obtained by contacting HCH as follows:

Harrison County Hospital
1141 Hospital Drive NW
Corydon, IN 47112

Management's Estimates

Management uses estimates and assumptions in preparing the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, if any, and the reported revenues and expenses. Actual results could vary from the estimates that were used.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

New Accounting Standards

During 2016, the Hospital implemented GASB Statement No. 72 *Fair Value Measurement and Application*. This statement addressed accounting and financial reporting issues related to fair value measurements. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. There was no impact to these financial statement disclosures as a result of adoption of this standard as these disclosures have been provided historically.

During 2016, the Hospital implemented GASB Statement No., 76 *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addressed the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. There was no impact to these financial statement disclosures as a result of adoption of this standard.

When both restricted and unrestricted resources are available for use, the Hospital's policy is to use restricted resources first, then unrestricted resources as they are needed.

Measurement Focus and Basis of Accounting

The Hospital utilizes the proprietary fund method of accounting whereby revenues and expenses are recognized on the accrual basis of accounting using the economic resources measurement focus. Substantially all revenues and expenses are subject to accrual.

When both restricted and unrestricted resources are available for use, the Hospital's policy is to use restricted resources first, then unrestricted resources as they are needed.

Risk Management

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

Cash and Cash Equivalents

Cash and cash equivalents as reported on the consolidated balance sheet include petty cash and other cash on hand amounts, checking accounts, and savings accounts that are readily available for use. Cash and cash equivalents as reported on the consolidated statement of cash flows include investments in highly liquid assets with maturity dates of 90 days or less when purchased.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

Investment Derivative Instrument - Interest Rate Swap

The Hospital uses interest rate swap agreements to manage financial risks related to interest rate movements and the effects on its cash flows. The Hospital accounts for the interest rate swap agreements as investment derivative instruments. As a result, the agreements are recorded at fair value on the consolidated balance sheet. The net cash payments or receipts under the interest rate swap agreements are recorded as an increase or decrease to interest expense, which is included in nonoperating revenues (expenses) on the consolidated statements of operations.

Patient Accounts Receivable and Net Patient Service Revenue

The Hospital recognizes net patient service revenues on the accrual basis of accounting in the reporting period in which services are performed based on the current gross charge structure, less actual adjustments and estimated discounts for contractual allowances, principally for patients covered by Medicare, Medicaid, managed care, and other health plans. Gross patient service revenue is recorded in the accounting records using the established rates for the types of service provided to the patient. The Hospital recognizes an estimated contractual allowance to reduce gross patient charges to the estimated net realizable amount for service rendered based upon previously agreed-to rates with a payor. The Hospital utilizes the patient accounting system to calculate contractual allowances on a payor-by-payor basis based on the rates in effect for each primary third-party payor. Another factor that is considered and could further influence the level of the contractual reserves includes the status of accounts receivable balances as inpatient or outpatient. The Hospital's management continually reviews the contractual estimation process to consider and incorporate updated laws and regulations and the frequent changes in managed care contractual terms that result from contract negotiations and renewals.

Payors include federal and state agencies, including Medicare and Medicaid, managed care health plans, commercial insurance companies, and patients. These third-party payors provide payments to the Hospital at amounts different from its established rates based on negotiated reimbursement agreements. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and fee schedule payments. Retroactive adjustments under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Allowance for Doubtful Accounts

Accounts receivable are reduced by an allowance for doubtful accounts based on the Hospital's evaluation of its major payor sources of revenue, the aging of the accounts, historical losses, current economic conditions, and other factors unique to the service area and the healthcare industry. Management regularly reviews data about the major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party payor coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, expected uncollectible deductibles and

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulty that make the realization of amounts due unlikely). For receivables associated with self-pay payments, which includes both patients without insurance and patient with deductible and copayment balances due for which third-party coverage exists for part of the bill, the Hospital records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts. The December 31, 2016 and 2015 allowance for doubtful accounts balance was comprised of the following:

	<u>2016</u>	<u>2015</u>
Reserve for third-party payor balances	\$ 856,654	\$ 909,796
Reserve for self-pay balances	<u>4,664,767</u>	<u>3,766,272</u>
Total allowance for doubtful accounts	<u>\$ 5,521,421</u>	<u>\$ 4,676,068</u>

The increase in the allowance for doubtful accounts is a result of changes in the payor mix from 2015 to 2016.

Inventories

Inventories consist of medical supplies, pharmaceuticals, and office supplies and are valued at the lower of cost or market, with cost being determined on the first-in, first-out (FIFO) method.

Assets Whose Use is Limited

Assets whose use is limited include assets set aside by the respective Boards for future capital improvements, over which the Boards retain control and may at their discretion subsequently use for other purposes; assets held by trustees under indenture agreements; assets that have been restricted by donors for specific purposes; and amounts that have been set aside as part of deferred compensation plans. Investment income or loss, including realized gains and losses on investments and assets whose use is limited, net change in the market value of assets whose use is limited, and interest, is included in nonoperating revenues (expenses) when earned.

Statutes authorize the Hospital to invest in interest-bearing deposit accounts, passbook savings accounts, certificates of deposit, money market deposit accounts, mutual funds, pooled fund investments, securities backed by the full faith and credit of the United States Treasury, and repurchase agreements. The statutes require that repurchase agreements be fully collateralized by U.S. Government or U.S. Government Agency obligations.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

Nonparticipating certificates of deposit, demand deposits, and similar nonparticipating negotiable instruments that are not reported as cash and cash equivalents, if any, are reported as investments at cost.

Capital Assets

The Hospital's capital assets are reported at historical cost and include expenditures for additions and repairs which substantially increase the useful lives of capital assets. Maintenance, repairs, and minor improvements are expensed as incurred. Contributed capital assets are reported at their estimated fair value at the time of their donation. All capital assets other than land and construction in progress are depreciated using the straight-line method of depreciation over their estimated useful lives based upon the American Hospital Association Guide for Estimated Useful Lives for Fixed Assets.

Classification of Net Position

The net position of the Hospital is classified in four components. (1) *Net investment in capital assets* consists of capital assets net of accumulated depreciation plus deferred outflows related to losses on bond refunding which are reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. (2) *Restricted expendable net position* includes assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures. (3) *Restricted nonexpendable net position* includes the principal portion of permanent endowments and non-controlling interests owned by external investors. (4) *Unrestricted net position* is the remaining net position that does not meet the definition of *net investment in capital assets or restricted*.

Consolidated Statements of Operations

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenues and expenses. Peripheral and incidental transactions are reported as nonoperating revenues (expenses). Nonoperating revenues (expenses) which are excluded from income from operations include investment income, contributions received, interest expense, restricted expenditures, and the net change in the market value of assets whose use is limited.

Advertising and Marketing Costs

Advertising and marketing costs are charged to operations when incurred. Advertising and marketing costs charged to operations were \$281,378 and \$301,438 for the years ended December 31, 2016 and 2015, respectively, and are included within the line item purchased services on the consolidated statements of operations.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

Income Taxes

HCH has been granted exemption from taxation as a not-for-profit organization by the Internal Revenue Service under Section 115, and in 2005 was also granted exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code for purposes of maintaining a 403b deferred compensation plan. Therefore, no provision for income taxes has been provided in the consolidated statement of operations. The MOB has elected to be treated as a partnership for federal and state income tax purposes. Under existing provisions of the Internal Revenue Code, a partnership is not a taxpaying entity for federal or state income tax purposes. Accordingly, no income tax expense has been recorded in the consolidated financial statements.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by each entity comprising the Hospital and recognize a tax liability if any Hospital entity has taken an uncertain tax position that more likely than not would not be sustained upon examination by various federal and state taxing authorities. Management has analyzed the tax positions taken by each entity of the Hospital, and has concluded that as of December 31, 2016, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying consolidated financial statements. Each entity of the Hospital is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

Grants and Contributions

From time to time, the Hospital receives grants as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues.

Subsequent Events

The Hospital has evaluated events or transactions occurring subsequent to the consolidated balance sheet date for recognition and disclosure in the accompanying consolidated financial statements through the date the consolidated financial statements are issued, which is November 10, 2017.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

2. DEPOSITS AND INVESTMENTS

Deposits and investments are comprised of the following at December 31, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Carrying amount:		
Cash and cash equivalents	\$ 12,619,487	\$ 14,527,587
Money market mutual funds	-0-	82,923
Mutual funds	<u>1,179,494</u>	<u>884,433</u>
Total	<u>\$ 13,798,981</u>	<u>\$ 15,494,943</u>
Included in the consolidated balance sheet captions:		
Cash and cash equivalents	\$ 5,349,449	\$ 7,696,622
Assets whose use is limited	<u>8,449,532</u>	<u>7,798,321</u>
Total	<u>\$ 13,798,981</u>	<u>\$ 15,494,943</u>

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that, in the event of a bank failure, the Hospital's deposits may not be returned to it. The Hospital does not have a deposit policy for custodial credit risk. Deposits with financial institutions are insured by the Federal Deposit Insurance Corporation ("FDIC") up to FDIC limits or the Public Deposit Insurance Fund, which covers all public funds held in approved depositories. This includes any deposit accounts issued or offered by a qualifying institution. The Hospital maintains its cash in bank deposit accounts, which at times, may exceed federally insured limits. The Hospital has not experienced any losses on such accounts. The Hospital believes it is not exposed to any significant credit risk on cash.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. The Hospital does not have a formal investment policy for interest rate risk for investments. The Hospital believes it is not exposed to any significant interest rate risk on investments.

Credit Risk – Investments

Credit risk is the risk that, in the event of a failure of a financial institution, the Hospital would not be able to recover deposits, the value of its investments, or collateral securities that are in the possession of an outside party. The Hospital does not have a formal investment policy for credit

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

risk for investments. The Hospital believes it is not exposed to any significant credit risk on investments.

Concentration of Credit Risk

The Hospital places no limit on the amount it may invest in any one issuer. The Hospital maintains its investments, which at times may exceed federally insured limits. The Hospital has not experienced any losses in such accounts. The Hospital believes that it is not exposed to any significant credit risk on investments.

Foreign Currency Risk

The Hospital does not have a formal policy in regards to foreign currency risk. The Hospital's investments did not have foreign currency risk.

Fair Value Measurements and Disclosures

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active market for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Hospital has the ability to access.
- Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.
- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value. There have been no changes in the methodologies used at December 31, 2016 and 2015:

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

- *Money market mutual funds:* Generally transact subscription and redemption activity at a \$1 stable net asset value (NAV) however, on a daily basis the funds are valued at their daily NAV calculated using the amortized cost of the securities held in the fund.
- *Mutual funds:* Valued at the daily closing price as reported by the fund. Mutual funds held by the Hospital are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value and to transact at that price. The mutual funds held by the Hospital are deemed to be actively traded.
- *Interest rate swap agreements:* Valued using pricing models that are derived principally from observable market data based on discounted cash flows and interest rate yield curves at quoted intervals for the full term of the swap.

The following table set forth by level, within the hierarchy, the Hospital's asset and liability measured at fair value on a recurring basis as of December 31, 2016 are as follows:

	Level 1	Level 2	Level 3	Total
<u>Assets</u>				
Mutual funds				
Large cap value	\$ 535,965	\$ -0-	\$ -0-	\$ 535,965
World allocation	643,529	-0-	-0-	643,529
Total assets at fair value	<u>\$ 1,179,494</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	1,179,494
Cash and cash equivalents				12,619,487
Total deposits and investments				<u>\$ 13,798,981</u>
<u>Liabilities</u>				
Interest rate swaps	<u>\$ -0-</u>	<u>\$ 133,842</u>	<u>\$ -0-</u>	<u>\$ 133,842</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

The following table set forth by level, within the hierarchy, the Hospital's asset and liability measured at fair value on a recurring basis as of December 31, 2015 are as follows:

	Level 1	Level 2	Level 3	Total
<u>Assets</u>				
Money market mutual funds	\$ -0-	\$ 82,923	\$ -0-	\$ 82,923
Mutual funds				
Large cap	141,966	-0-	-0-	141,966
Mid cap	251,051	-0-	-0-	251,051
World allocation	491,416	-0-	-0-	491,416
	<u>884,433</u>	<u>-0-</u>	<u>-0-</u>	<u>884,433</u>
Total assets at fair value	<u>\$ 884,433</u>	<u>\$ 82,923</u>	<u>\$ -0-</u>	967,356
Cash and cash equivalents				<u>14,527,587</u>
Total deposits and investments				<u>\$ 15,494,943</u>
<u>Liabilities</u>				
Interest rate swaps	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

3. PATIENT ACCOUNTS RECEIVABLE

Patient accounts receivable amounts are reported as current assets at December 31, 2016 and 2015 consist of the following:

	2016	2015
Medicare	\$ 6,819,916	\$ 6,121,260
Medicaid	4,929,532	4,533,225
Blue Cross	2,268,099	2,507,971
Other insurance carriers	5,488,677	4,999,987
Patients	<u>4,993,999</u>	<u>4,240,796</u>
Total patient accounts receivable	24,500,223	22,403,239
Less allowance for contractals	11,873,673	11,682,592
Less allowance for uncollectible amounts	<u>5,521,421</u>	<u>4,676,068</u>
 Patient accounts receivable, net	 <u>\$ 7,105,129</u>	 <u>\$ 6,044,579</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

4. ASSETS WHOSE USE IS LIMITED

Assets whose use is limited that are required for obligations classified as current liabilities are reported in current assets. Assets whose use is limited are reported at market value and include the following at December 31, 2016 and 2015:

Investment Summary by Type

	2016	%	2015	%
Cash and cash equivalents	\$ 7,270,038	86.0 %	\$ 6,830,965	87.6 %
Money market mutual funds	-0-	0.0	82,923	1.1
Mutual funds	1,179,494	14.0	884,433	11.3
Total assets whose use is limited	<u>\$ 8,449,532</u>	<u>100.0 %</u>	<u>\$ 7,798,321</u>	<u>100.0 %</u>

Investment Summary by Fund

Board-Designated Funds	\$ 8,449,532	100.0 %	\$ 6,115,136	78.4 %
Swap-Restricted Funds	-0-	0.0	1,683,185	21.6
Total	<u>\$ 8,449,532</u>	<u>100.0 %</u>	<u>\$ 7,798,321</u>	<u>100.0 %</u>

Board-Designated Funds

The Hospital's Board of Trustees approved the funding of depreciation expense to meet the capital asset replacement needs of the facility. Depreciation is funded totally with expenditures for capital items reducing the funded depreciation balance. Board-designated funds also include amounts intended for specific purposes, as established by the Hospital's Board. All income earned by the board-designated accounts is left to accumulate as additions to the funds. Board-designated funds remain under the control of the Board, which may at their discretion later use for other purposes. Therefore, all board-designated funds are included in unrestricted net position.

Swap-Restricted Funds

Swap-restricted funds represent amounts that have been restricted by creditors for the potential payoff of the Hospital's interest rate swaps (see Note 11).

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

5. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2016, was as follows:

	Beginning Balance	Additions	Retirements/ Transfers	Ending Balance
Land	\$ 3,001,138	\$ -0-	\$ -0-	\$ 3,001,138
Land improvements	3,339,918	39,515	-0-	3,379,433
Leasehold improvements	3,605,135	-0-	-0-	3,605,135
Buildings	40,874,173	9,998	-0-	40,884,171
Fixed equipment	25,436,742	1,465,881	46,887	26,949,510
Construction in progress	<u>101,507</u>	<u>377,543</u>	<u>(58,470)</u>	<u>420,580</u>
Total historical cost	76,358,613	1,892,937	(11,583)	78,239,967
Less accumulated depreciation for				
Land improvements	(1,950,924)	(160,680)	-0-	(2,111,604)
Leasehold improvements	(1,493,138)	(229,961)	-0-	(1,723,099)
Buildings	(16,359,103)	(2,020,567)	354	(18,379,316)
Fixed equipment	<u>(22,608,148)</u>	<u>(1,088,315)</u>	<u>10,729</u>	<u>(23,685,734)</u>
Total accumulated depreciation	<u>(42,411,313)</u>	<u>(3,499,523)</u>	<u>11,083</u>	<u>(45,899,753)</u>
Capital assets, net	<u>\$ 33,947,300</u>	<u>\$ (1,606,586)</u>	<u>\$ (500)</u>	<u>\$ 32,340,214</u>

Capital asset activity for the year ended December 31, 2015, was as follows:

	Beginning Balance	Additions	Retirements/ Transfers	Ending Balance
Land	\$ 3,001,138	\$ -0-	\$ -0-	\$ 3,001,138
Land improvements	3,331,118	8,800	-0-	3,339,918
Leasehold improvements	3,595,332	9,803	-0-	3,605,135
Buildings	40,834,597	42,058	(2,482)	40,874,173
Fixed equipment	24,426,574	1,010,168	-0-	25,436,742
Construction in progress	<u>64,691</u>	<u>42,685</u>	<u>(5,869)</u>	<u>101,507</u>
Total historical cost	75,253,450	1,113,514	(8,351)	76,358,613
Less accumulated depreciation for				
Land improvements	(1,715,394)	(235,530)	-0-	(1,950,924)
Leasehold improvements	(1,254,113)	(239,025)	-0-	(1,493,138)
Buildings	(14,313,799)	(2,053,655)	8,351	(16,359,103)
Fixed equipment	<u>(20,797,093)</u>	<u>(1,811,055)</u>	<u>-0-</u>	<u>(22,608,148)</u>
Total accumulated depreciation	<u>(38,080,399)</u>	<u>(4,339,265)</u>	<u>8,351</u>	<u>(42,411,313)</u>
Capital assets, net	<u>\$ 37,173,051</u>	<u>\$ (3,225,751)</u>	<u>\$ -0-</u>	<u>\$ 33,947,300</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

6. OTHER ASSETS

At December 31, 2016 and 2015, other assets consist of the following:

	<u>2016</u>	<u>2015</u>
Physician notes receivable	\$ 14,423	\$ 39,423
Intangible assets	<u>11,682</u>	<u>28,890</u>
Total other assets	26,105	68,313
Other assets, current portion	<u>(14,423)</u>	<u>(25,000)</u>
Other assets, net of current portion	<u>\$ 11,682</u>	<u>\$ 43,313</u>

Physician notes receivable are in varying amounts maturing through July 2017. If the physicians meet the period of service requirement, the Hospital will forgive these notes. If the physicians do not meet the period-of-service requirement, the notes are immediately due in full. Interest rates are prime rate + 1 percent (4.25 percent at both December 31, 2016 and 2015).

The Hospital has intangible assets that are being amortized over their remaining estimated useful life using the straight line method.

7. COMPENSATED ABSENCES

The Hospital's policy on paid days off (which includes vacation, sick leave, personal leave, and holidays) allows full-time employees and regular part-time employees to accrue paid days off, to a maximum of 60 days.

Paid days off are accrued when incurred and reported as a liability. The paid days off accrual at December 31, 2016 and 2015 was \$1,019,179 and \$952,424, respectively, and is reported in accrued personnel costs in the consolidated financial statements.

8. EMPLOYEE HEALTH BENEFIT PLAN

The Hospital operates a self-funded health plan covering substantially all employees. The Hospital has an annual stop loss limit on the plan of \$60,000 per insured per year. Claim expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. Claims liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amounts of pay out, and other economic and social factors. The accrued liability for claims liabilities is recorded in accrued expenses on the consolidated balance sheets.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

Changes in the balance of claims liabilities during the years ended December 31, 2016 and 2015 were as follows:

	<u>2016</u>	<u>2015</u>
Accrued liability, beginning of year	\$ 43,000	\$ 239,474
Incurred claims, changes in estimates, and fees/premiums	1,940,536	3,048,704
Claim payments	<u>(1,788,378)</u>	<u>(3,245,178)</u>
Accrued liability, end of year	<u>\$ 195,158</u>	<u>\$ 43,000</u>

9. DEFINED CONTRIBUTION PENSION PLAN

Plan Description

The Hospital has a defined contribution pension plan administered by MetLife as authorized by Indiana Code 16-22-3-11. The plan provides retirement, disability, and death benefits to plan members and beneficiaries. The plan was established by written agreement between the Hospital Board of Trustees and the Plan Administrator. The Plan Administrator issues a publicly available financial report that includes financial statements and required supplementary information of the plan. That report may be obtained by contacting:

MetLife
c/o FasCare, LLC
P.O. Box 173768
Denver, Colorado 80217-3768
Ph. (800) 543-2520

Funding Policy and Annual Pension Cost

The contribution requirements of plan members are established by the written agreement between the Hospital Board of Trustees and the Plan Administrator. Plan members are voluntary and are established by written authorization for payroll deduction into an annuity savings account. The current rate is 5 percent of annual covered payroll. Employer contributions to the plan were \$927,544 and \$874,968 for the years ended December 31, 2016 and 2015, respectively.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

10. OBLIGATIONS UNDER CAPITAL LEASES

The Hospital is the lessee of certain equipment under interest bearing capital leases that expire in various years through 2020. The assets and liabilities under capital leases are initially recorded at the lower of the present value of the minimum lease payments or the fair value of the asset. Amortization of assets held under capital leases is included in depreciation expense and was \$42,678 and \$24,312 for the years ended December 31, 2016 and 2015, respectively.

Following is a summary of property held under capital leases:

	<u>2016</u>	<u>2015</u>
Equipment	\$ 204,015	\$ 204,015
Less accumulated depreciation	<u>(74,620)</u>	<u>(31,942)</u>
Other assets, net of current portion	<u>\$ 129,395</u>	<u>\$ 172,073</u>

Minimum future lease payments under capital leases as of December 31, 2016 are as follows:

<u>Year Ending December 31,</u>	<u>Amount</u>
2017	\$ 46,200
2018	46,200
2019	37,859
2020	<u>18,487</u>
	148,746
Less: amount representing interest	<u>12,053</u>
Present value of minimum lease payments	<u>\$ 136,693</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

11. LONG-TERM DEBT

At December 31, 2016 and 2015, the Hospital was obligated for long-term debt agreements as follows:

	2016	2015
Harrison County, Indiana Economic Development Revenue Refunding Bonds, Series 2011, refunded in 2016 by proceeds from Series 2016 Revenue Refunding Bonds.	\$ -0-	\$ 8,325,664
Harrison County, Indiana Economic Development Revenue Refunding Bonds, Series 2016 (Harrison County Hospital Project) dated September 2016, payable in monthly principal installments of \$71,207 commencing October 2016 through October 2026. Bank Qualified Tax-Exempt interest rate is fixed at 2.61% (if Hospital fails to remain Bank Qualified, rate reverts to 2.00% fixed). Secured by first mortgage on Hospital property.	7,335,549	-0-
Mortgage note payable to bank, due July 2017; payable in annual principal installments, in amounts ranging from \$70,698 to \$134,206; variable interest rate at one month LIBOR plus 1.25% (1.97% and 1.61% at December 31, 2016 and 2015, respectively). Secured by substantially all assets.	4,599,570	4,735,002
Mortgage note payable to bank, due September 2017; monthly payments, including interest of \$2,103; Fixed interest at 5.00%. Secured by substantially all assets.	282,591	293,165
	12,217,710	13,353,831
Less current portion	(5,494,042)	(553,198)
Long-term debt, net of current portion	\$ 6,723,668	\$ 12,800,633

In September 2016, the Hospital defeased the 2011 bonds with proceeds from the issuance of the 2016 bonds and current cash. The swap agreement associated with the 2011 bonds was also terminated as part of the defeasance. The 2011 bonds required that the Hospital establish and maintain a separate deposit account (cash reserve), so long as the swap agreement was in full force and effect. The Hospital was to maintain a cash reserve in an amount equal to any payment that may be due by the Hospital under the swap master agreement due to the termination of the swap agreement. The remaining balance in the cash reserve account was utilized to make the termination payment amount at the termination settlement date and date of the 2016 bonds, September 13, 2016.

The amount of cash and investments set aside in assets whose use is limited was \$-0- and \$1,683,185 at December 31, 2016 and 2015, respectively, as the swap agreement originally associated with the 2005 bonds was paid off in 2016.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

Long-term debt activity for the years ended December 31, 2016 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance	Current Portion
Revenue bonds, series 2011	\$ 8,325,664	\$ -0-	\$ 8,325,664	\$ -0-	\$ -0-
Revenue bonds, series 2016	-0-	7,500,000	164,451	7,335,549	611,881
Mortgage note payable	4,735,002	-0-	135,432	4,599,570	4,599,570
Mortgage note payable	<u>293,165</u>	<u>-0-</u>	<u>10,574</u>	<u>282,591</u>	<u>282,591</u>
Total long-term debt	<u>\$ 13,353,831</u>	<u>\$ 7,500,000</u>	<u>\$ 8,636,121</u>	<u>\$ 12,217,710</u>	<u>\$ 5,494,042</u>

Long-term debt activity for the years ended December 31, 2015 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance	Current Portion
Revenue bonds, series 2016	\$ 8,719,997	\$ -0-	\$ 394,333	\$ 8,325,664	\$ 408,277
Mortgage note payable	4,861,029	-0-	126,027	4,735,002	134,206
Mortgage note payable	<u>303,257</u>	<u>-0-</u>	<u>10,092</u>	<u>293,165</u>	<u>10,715</u>
Total long-term debt	<u>\$ 13,884,283</u>	<u>\$ -0-</u>	<u>\$ 530,452</u>	<u>\$ 13,353,831</u>	<u>\$ 553,198</u>

Debt service requirements on long-term debt at December 31, 2016 are based on the interest rate modes in effect and are as follows:

Year Ending December 31,	Principal	Interest
2017	\$ 5,494,042	\$ 320,501
2018	684,834	169,646
2019	703,178	151,302
2020	721,627	132,852
2021	741,342	113,137
2022 - 2026	<u>3,872,687</u>	<u>257,296</u>
Total	<u>\$ 12,217,710</u>	<u>\$ 1,144,734</u>

The Hospital's debt agreements contain various restrictive covenants, including debt service coverage ratio and audited financial statement submission requirements. The Hospital is in violation of the audit submission requirements and has obtained a covenant waiver for the violation.

12. DERIVATIVE INSTRUMENTS - INTEREST RATE SWAPS

In accordance with GASB Codification Section D40, governmental entities are required to evaluate each derivative instrument to determine whether the instrument is an effective hedge.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

For those instruments deemed to be an effective hedge, governmental entities are required to practice hedge accounting and the instrument continues to be reevaluated at the end of each future reporting period. Under hedge accounting, the fair value of the instrument is recorded on the consolidated balance sheets with the offsetting entry to deferred outflows or deferred inflows, which is reported on the consolidated balance sheets.

For those instruments deemed to be an ineffective hedge, governmental entities are required to practice investment accounting and the instruments are not evaluated in future reporting periods. Once deemed ineffective, the instrument is considered ineffective for the remainder of its term. Under investment accounting, the fair value of the instrument is recorded on the consolidated balance sheets with the offsetting entry posted to investment income within nonoperating revenues (expenses) on the consolidated statements of operations.

During 2011, the Hospital's interest rate swap on the 2011 revenue bonds (previously 2005 revenue bonds refinanced with 2011 revenue bonds) was determined to be an ineffective hedge. During 2013, the Hospital's interest rate swap on the mortgage note payable was determined to be an ineffective hedge. Therefore, the interest rate swap agreements are ineffective through the remainder of their terms. As a result, the fair value of the instruments have been recorded as liabilities on the consolidated balance sheets with the offsetting entries recorded under nonoperating revenues (expenses) in the consolidated statements of operations.

Contracts

The Hospital has one interest rate swap agreement in effect as of December 31, 2016, and two interest rate swap agreements in effect as of December 31, 2015, for the 2011 revenue bonds and the mortgage note payable. The 2011 revenue bonds swap agreement was paid off in 2016.

Objectives and Strategies for Using Derivatives

As a means to manage the risk associated with interest rate risk on its variable rate debt, the Hospital entered into interest rate swap agreements in connection with its 2011 revenue bonds and mortgage note payable. The intention of the swap agreements was to effectively change the Hospital's variable interest rate on the Series 2011 Bonds to a fixed rate of 3.81% and change the Hospital's variable interest rate on the mortgage note payable to a fixed rate of 5.97% plus an additional 1.25% credit spread as noted in Note 11.

Terms, Fair Values, and Credit Risk

The swap agreements relate to the 2011 revenue bonds and mortgage note payable with original notional amounts of \$25,000,000 and \$5,600,000, respectively. The counter party to the swap agreements is U.S. Bank for the 2011 revenue bonds and Regions Bank for the mortgage note payable.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

The terms and fair values of the outstanding swaps as of December 31, 2016 are as follows:

	2011 Revenue Bonds	Mortgage note payable
Original notional amount	\$ 25,000,000	\$ 5,600,000
Current notional amount	\$ -0-	\$ 4,759,570
Effective date	December 1, 2005	February 15, 2009
Fixed rate	3.81%	5.97%
	70% of USD-LIBOR-	
Variable rate	BBA	USD-LIBOR-BBA
Fair value	\$ -0-	\$ (133,842)
Termination date	Paid off	July 1, 2017
Counterparty credit rating (1)	AA-	BBB

(1) As rated by Fitch

The terms and fair values of the outstanding swaps as of December 31, 2015 are as follows:

	2011 Revenue Bonds	Mortgage note payable
Original notional amount	\$ 25,000,000	\$ 5,600,000
Current notional amount	\$ 7,986,000	\$ 4,895,002
Effective date	December 1, 2005	February 15, 2009
Fixed rate	3.81%	5.97%
	70% of USD-LIBOR-	
Variable rate	BBA	USD-LIBOR-BBA
Fair value	\$ (1,480,475)	\$ (384,918)
Termination date	October 1, 2030	July 1, 2017
Counterparty credit rating (1)	AA-	BBB

(1) As rated by Fitch

As of December 31, 2016, the negative fair values of the agreement may be countered by reductions in total interest payments under the swap agreement should the variable rate on the mortgage note payable increase.

Basis Risk

The swap variable rate is pegged to USD-LIBOR-BBA index. The mortgage note payable variable rate is determined based on LIBOR. Therefore basis risk relating to the swap could be significant.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

Termination Risk

The Hospital or the counter party may terminate the swap if the other party fails to perform under the terms of the contract. If at the time of termination, the swap has a negative fair value, the Hospital could be liable to the counter party for a payment equal to the swap's fair values. As of December 31, 2016 and 2015, the Hospital was in compliance with the terms of the swap contract.

Swap Payments and Associated Debt

Debt service requirements of the variable rate debt and net swap payments of the mortgage note payable, assuming current interest rates remain the same for the term of the bonds, are disclosed in the Long Term Debt note. As rates vary, variable-rate bond interest payments and net swap payments will vary.

The Hospital has determined the swaps to be ineffective hedges. Accordingly, the fair value of the swaps have been recorded and subsequent changes in fair value will be recorded in the consolidated balance sheets with the offsetting entry recorded under nonoperating revenues (expenses) in the consolidated statements of operations.

Following is an analysis of the recording of the interest rate swap agreements as of, and for the year ended December 31, 2016:

Swap agreement	Change in market value	Interest rate swap liability
2011 Revenue Bonds	\$ (74,725)	\$ -0-
Mortgage note payable	251,076	133,842
	\$ 176,351	\$ 133,842

Following is an analysis of the recording of the interest rate swap agreements as of, and for the year ended December 31, 2015:

Swap agreement	Change in market value	Interest rate swap liability
2011 Revenue Bonds	\$ 92,693	\$ 1,480,475
Mortgage note payable	240,086	384,918
	\$ 332,779	\$ 1,865,393

See the Fair Value Measurements and Long Term Debt footnotes for additional information.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

13. NET PATIENT SERVICE REVENUE

For the years ended December 31, 2016 and 2015, net patient service revenue was as follows:

	2016	2015
Gross patient service revenue		
Inpatient services	\$ 27,203,804	\$ 29,485,452
Outpatient services	118,855,385	105,140,488
Total gross patient service revenue	146,059,189	134,625,940
Deductions from revenue		
Contractual allowances	(92,074,142)	(83,659,842)
Charity care	(770,674)	(2,019,352)
Bad debts	(5,967,387)	(4,547,236)
Medicaid DSH payments recognized	2,901,098	2,823,281
Total deductions from revenue	(95,911,105)	(87,403,149)
Total net patient service revenue	\$ 50,148,084	\$ 47,222,791

The Hospital grants credit without collateral to its patients, most of whom are local residents and insured under third-party payor agreements.

The mix of gross revenues and receivables from patients and third-party payors at December 31, 2016 and 2015 was as follows:

	2016		2015	
	Revenues	Receivables	Revenues	Receivables
Medicare	41 %	28 %	41 %	27 %
Medicaid	22	20	21	20
Blue Cross	17	9	16	11
Other third-party payors	18	22	19	22
Patients	2	21	3	20
	100 %	100 %	100 %	100 %

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

- **Medicare.** The Hospital is a provider of services to patients entitled to coverage under Title XVIII (Medicare) of the Health Insurance Act. The Hospital is classified as Critical Access Status by Medicare and is paid for Medicare services based upon a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at an interim rate, with final settlement determined after submission of annual cost reports. Differences between the total program billed charges and the payments received are reflected as deductions from

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

revenue. At the Hospital's year-end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients. As of December 31, 2016, the Hospital's submitted Medicare cost reports have been final settled with the Fiscal Intermediary through December 31, 2014.

- **Medicaid.** The Hospital is a provider of services to patients entitled to coverage under Title XIX (Medicaid) of the Health Insurance Act. The Hospital is reimbursed for Medicaid inpatient services under a prospectively determined rate-per-discharge and is not subject to retroactive adjustment. The differences between standard charges and reimbursement from these programs are recorded as contractual adjustments. Reimbursement for Medicaid outpatient services is based on predetermined rates, and is not subject to retroactive cost based settlements.
- **Charity Care.** The Hospital provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Because the Hospital does not collect amounts deemed to be charity care, they are not reported as revenue. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the Hospital's total operating expenses divided by gross patient service revenue. For the years ended December 31, 2016 and 2015, the Hospital incurred estimated costs of \$269,848 and \$769,534, respectively.
- **Other.** The Hospital has also entered into preferred provider agreements with certain commercial insurance carriers. The basis for payment to the Hospital under these agreements includes discounts from established charges, fee schedules, as well as inpatient diagnosis-related group reimbursement methodologies.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Final determination of compliance with such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. The Hospital believes that it is in compliance with all applicable laws and regulations.

14. ELECTRONIC HEALTH RECORDS (EHR) INCENTIVE PAYMENTS

The Hospital receives EHR incentive payments under the Medicare and Medicaid programs. To qualify for EHR incentive payments, the Hospital must meet "meaningful use" criteria that become more stringent over time. The Hospital periodically submits and attests to its use of certified EHR technology, satisfaction of meaningful use objectives, and various patient data. These submissions generally include performance measures for each annual EHR reporting period (Federal fiscal year ending on September 30th). The related EHR incentive payments are paid out over a four year

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

transition schedule and are based upon data that is captured in the Hospital's cost reports. For Critical Access Hospitals, the payment calculation is based upon the net book value of the qualifying assets, multiplied by the Medicare utilization using Medicare to total inpatient days plus 20%, not to exceed 100%. The total days are multiplied by a factor of total charges excluding charity care to total charges. Critical Access Hospitals can be reimbursed over a four year period for additional qualifying assets not claimed in the first year. The transitional factor ranges from 100% in first payment year and decreases by 25% each payment year until it is completely phased out in the fifth year.

The Hospital recognizes EHR incentive payments as grant income when there is reasonable assurance that the Hospital will comply with the conditions of the meaningful use objectives and any other specific grant requirements. In addition, the financial statement effects of the grants must be both recognizable and measurable. During the years ended December 31, 2016 and 2015, the Hospital recognized \$84,960 and \$81,111, respectively, in EHR incentive payments as grant income using the cliff recognition method. Under the cliff recognition method, the Hospital records income at the end of EHR reporting period in which compliance is achieved. EHR incentive income is included in other revenue on the consolidated statements of operations. EHR incentive income is recognized based on management's estimate and amounts are subject to change, with such changes impacting operations in the period the changes occur.

Receipt of these funds is subject to the fulfillment of certain obligations by the Hospital as prescribed by the program, subject to future audits and may be subject to repayment upon a determination of noncompliance.

15. HOSPITAL ASSESSMENT FEE

In 2012, Hospital Assessment Fee (HAF) Program was approved by Centers for Medicare and Medicaid Services (CMS). The purpose of the HAF Program is to fund the State share of enhanced Medicaid payments and Medicaid Disproportionate Share payments for Indiana hospitals. Previously, the State share was funded by governmental entities through intergovernmental transfers. The Medicaid enhanced payments relate to both fee for service and managed care claims. The Medicaid enhanced claims are designed to follow patients and result in increased Medicaid rates.

During the years ended December 31, 2016 and 2015, the Hospital recognized HAF program expense of \$1,007,906 and \$755,843, respectively, which resulted in Medicaid rate increases. The Medicaid rate increases under the HAF Program are included in net patient service revenue in the consolidated statements of operations. The HAF Program was approved for extension through June 30, 2017.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

16. NONOPERATING REVENUES (EXPENSES)

For the years ended December 31, 2016 and 2015, nonoperating revenues (expenses) were as follows:

	2016	2015
Investment income	\$ 145,014	\$ 39,834
Interest expense	(844,105)	(1,013,761)
Contributions and grants	25,508	(5,517)
Change in market value of interest rate swaps	176,351	332,779
Miscellaneous	<u>59,797</u>	<u>(58,386)</u>
Total nonoperating revenues (expenses)	<u>\$ (437,435)</u>	<u>\$ (705,051)</u>

GASB requires interest expense to be reported as nonoperating expense while FASB requires interest expense to be reported as an operating expense.

17. PROFESSIONAL LIABILITY INSURANCE

The Indiana Medical Malpractice Act, IC 34-18, provides a maximum recovery of \$250,000 for an occurrence of malpractice and \$1,250,000 for an injury or death of a patient due to an act of malpractice. The Act requires physicians to maintain medical malpractice liability insurance in the minimum amount of \$250,000 per occurrence and \$750,000 in the annual aggregate and hospitals to maintain medical malpractice liability insurance in the minimum amount of \$250,000 per occurrence and \$5,000,000 in the annual aggregate for hospitals with fewer than 100 occupied beds. The Act also requires the Hospital to pay a surcharge to the State Patient's Compensation Fund. This fund may be used to pay medical malpractice claims in excess of the annual aggregate amount noted above, under certain terms and conditions.

Liabilities for incurred but not reported losses at December 31, 2016 and 2015, respectively, are not determinable; however, in management's opinion, such liabilities, if any, will not have a material effect on the Hospital's financial position and its malpractice and general liability insurance is adequate to cover losses, if any. Should the policies not be renewed or replaced with appropriate insurance coverage, claims based upon occurrences during these terms, but reported subsequently, will be uninsured. The Hospital intends to continue carrying such insurance.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

18. OPERATING LEASES – LESSEE

The Hospital leases certain equipment under non-cancelable operating leases. Future payments under these non-cancelable operating leases at December 31, 2016 was as follows:

Year Ending December 31,	Amount
2017	\$ 241,122
2018	241,122
2019	116,640
2020	122,856
2021	122,856
2022-2025	52,056
Total minimum payments	<u>\$ 896,652</u>

The Hospital leases certain building space under cancelable operating leases. The Hospital incurred \$242,171 and \$234,368 in total rent expense for the years ended December 31, 2016 and 2015, respectively, under its cancelable and non-cancelable operating leases.

19. OPERATING LEASES – LESSOR

The Hospital leases certain space of the medical office building (with a net book value of \$3,765,711 at December 31, 2016) to tenants under operating leases expiring within the next five years. The leases contain annual escalation provisions which increase rentals relative to increases in the Consumer Price Index. The leases also contain provisions which require tenants to pay their proportionate share of certain expenses and costs in connection with the Hospital's ownership and operation of the building and common area.

Following is a schedule by years of future minimum rentals to be received under the operating leases with remaining non-cancelable lease terms in excess of one year as of December 31, 2016:

Year ended December 31:	Amount
2017	\$ 199,368
2018	104,024
Total minimum future rentals	<u>\$ 303,392</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

20. FAIR VALUE OF FINANCIAL INSTRUMENTS

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

Cash and Cash Equivalents

The carrying amount reported in the consolidated balance sheets for cash and cash equivalents approximates its fair value based on the short maturities of those items.

Assets Whose Use is Limited

These assets are reported in the consolidated balance sheets at fair value. The fair value amounts are based on quoted market prices, if available, or are estimated using quoted market prices for similar securities.

Accounts Payable, Accrued Personnel Costs, and Accrued Expenses

The carrying amounts reported in the consolidated balance sheets for accounts payable, accrued personnel costs, and accrued expenses approximate their fair value based on the short maturities of those items.

Estimated Third-Party Payor Settlements

The carrying amount reported in the consolidated balance sheets for estimated third-party payor settlements approximates its fair value because they are expected to be settled in the near future.

Long-Term Debt

The carrying amount and fair value of long-term debt at December 31, 2016 was \$12,354,403 and \$12,267,757, respectively. The 2015 carrying amount reported in the consolidated balance sheets for long-term debt approximates its fair value because the vast majority of the outstanding debt carried variable interest rates.

Interest Rate Swap Agreements

Interest rate swap agreements are reported in the consolidated balance sheets at fair value. Interest rate swap agreements are valued using pricing models that are derived principally from observable market data based on discounted cash flows and interest rate yield curves at quoted intervals for the full term of the swap.

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

21. CONTINGENCIES

There are a variety of legal proceedings and claims by others against the Hospital in a variety of matters arising out of the conduct of the Hospital's business. The ultimate resolution of such claims would not, in the opinion of management, have a material adverse effect on the consolidated financial statements.

22. COMMITMENTS

As of December 31, 2016, the Hospital has construction and renovation project commitments as follows:

Project	Expected Date of Completion	Estimated Total Cost of Project	Costs Incurred as of 12/31/2016
Batch Scanning - Cerner	9/30/2017	\$ 85,000	\$ 70,490
PACS Project	6/1/2017	350,000	280,393
AP Automation Project	8/15/2017	49,300	39,180
Other	12/31/2017	35,000	30,517
		<u>\$ 519,300</u>	<u>\$ 420,580</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

23. CONDENSED FINANCIAL INFORMATION

The Hospital includes one blended component unit, the MOB, in its reporting entity. Condensed component unit information for its blended component unit as of and for the years ended December 31, 2016 and 2015 is as follows:

	<u>2016</u>	<u>2015</u>
Balance sheet		
Assets		
Current assets	\$ 180,369	\$ 135,656
Capital assets, net	5,426,584	5,691,748
Other assets	<u>11,682</u>	<u>28,890</u>
Total assets	<u>\$ 5,618,635</u>	<u>\$ 5,856,294</u>
Liabilities		
Current liabilities	\$ 5,084,149	\$ 229,183
Long-term liabilities	<u>18,294</u>	<u>5,288,769</u>
Total liabilities	5,102,443	5,517,952
Net position		
Net investment in capital assets	526,129	592,207
Unrestricted	<u>(9,937)</u>	<u>(253,865)</u>
Total net position	<u>516,192</u>	<u>338,342</u>
Total liabilities and net position	<u>\$ 5,618,635</u>	<u>\$ 5,856,294</u>

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

	2016	2015
Statement of operations and changes in net position		
Operating revenues		
Other operating revenue	\$ 920,300	\$ 925,851
Operating expenses		
Depreciation and amortization	292,370	291,828
Other operating expenses	248,109	251,932
Total operating expenses	<u>540,479</u>	<u>543,760</u>
Income from operations	379,821	382,091
Nonoperating revenues (expenses)	<u>(117,602)</u>	<u>(140,333)</u>
Change in net position	262,219	241,758
Member distributions	(84,369)	(84,000)
Net position - beginning of year	338,342	180,584
Net position - end of year	<u>\$ 516,192</u>	<u>\$ 338,342</u>
Statement of cash flows		
Cash provided by		
Operating activities	\$ 316,364	\$ 317,037
Capital and related financing activities	(293,453)	(266,374)
Total	<u>22,911</u>	<u>50,663</u>
Cash - beginning of year	112,787	62,124
Cash - end of year	<u>\$ 135,698</u>	<u>\$ 112,787</u>

24. RECENT GASB PRONOUNCEMENTS

Management has not currently determined what effects, if any, the implementation of the following recently enacted statements may have on its future financial statements:

GASB Statement No. 87, *Leases*, issued June 2017, will be effective for periods beginning after December 15, 2019. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were

HARRISON COUNTY HOSPITAL AND AFFILIATED ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.