

STATE BOARD OF ACCOUNTS
302 West Washington Street
Room E418
INDIANAPOLIS, INDIANA 46204-2769

AUDIT REPORT
OF

DAVISS COMMUNITY HOSPITAL
A COMPONENT UNIT OF
DAVISS COUNTY, INDIANA

January 1, 2008 to December 31, 2008



FILED
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HOSPITAL OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Executive Director	James Heckert Louis H. Bremer, Jr. (Interim) Gary Kendrick	01-01-07 to 02-29-08 03-01-08 to 07-31-08 08-11-08 to 12-31-09
Chief Financial Officer	Brad Hardcastle	01-01-08 to 12-31-09
Chairman of the Hospital Board	Brenda Sobecki Kenneth Parsons	07-01-07 to 06-30-08 07-01-08 to 06-30-09
President of the Board of County Commissioners	Steve Myers Tony Wichman	01-01-08 to 12-31-08 01-01-09 to 12-31-09



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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INDEPENDENT AUDITOR'S REPORT

TO: THE OFFICIALS OF THE DAVIESS COMMUNITY HOSPITAL, DAVIESS COUNTY, INDIANA

We have audited the accompanying basic financial statements of Daviess Community Hospital (Hospital), and its aggregate discretely presented component units as of and for the year ended December 31, 2008, as listed in the Table of Contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Hospital and its aggregate discretely presented component units as of December 31, 2008, and the respective changes in financial position and cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States.

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

STATE BOARD OF ACCOUNTS

August 13, 2009



Management's Discussion and Analysis

Our discussion and analysis of Davieess Community Hospital's (the Hospital) financial performance provides an overview of the Hospital's financial statements for the fiscal year ended December 31, 2008. Please read it in conjunction with the Hospital's financial statements and accompanying notes to the financial statements. Unless otherwise stated, amounts are presented in millions.

Using This Annual Report

This annual report consists of the ***Management's Discussion and Analysis***, and the ***Basic Financial Statements***.

- In the ***Management's Discussion and Analysis*** section of this report, the Hospital discusses various components of the annual report and provides an analysis of the current financial statement information.
- The ***Basic Financial Statement*** section of this report includes a series of financial statements which provide information about the activities of the Hospital as a whole. The Statement of Net Assets reveals the assets and liabilities of the Hospital on December 31, 2008 while the Statement of Revenues, Expenses and Changes in Net Assets summarize the change in cash and cash equivalents as a result of the financial activity during the year. The Notes to the Financial Statements disclose additional information addressed within the body of the financial statements.

Financial Highlights

- The Hospital's net assets decreased by \$0.1 million or 0.3% as a result of this year's operations.
- The Hospital's net operating revenues of \$48.8 million increased by \$4.2 million or 9.4% from prior year. Gross revenue for inpatients increased \$3.9 million while outpatient gross revenue increased \$3.6 million.
- The Hospital's operating expenses of \$49.5 million increased by \$4.3 million or 9.5% from the prior year. Salaries increased \$1.4 million, benefits, physician fees, and supplies increased by \$0.4 million each, interest by \$0.6 million, and bad debts by \$0.5 million.

Summarized Financial Statement Information

The following financial reports *Net Assets* and *Changes in Net Assets* document in summary form the financial information related to the activities of the Hospital for Calendar Year 2008 and Prior Year 2007. Related notes follow the financial reports.

NET ASSETS		
	2008	2007
Current Assets	\$12.6	\$14.6
Noncurrent Assets	12.9	11.4
Capital Assets	33.7	33.6
Total Assets	59.2	59.6
Current Liabilities	5.3	4.5
Long-Term Debt	18.6	19.6
Total Liabilities	23.9	24.1
Net Assets		
Invested in Capital Assets	13.6	12.5
Restricted	3.4	2.0
Unrestricted	18.4	21.0
Total Net Assets	\$35.4	\$35.5

Current Assets of \$12.6 million decreased \$2.0 million or 13.7% from the prior year. Receivables declined \$0.8 million and \$1.5 million of cash was reclassified to board designated funds.

Long-Term Debt of \$18.6 million decreased \$1.0 million or 5.1% from the prior year.

CHANGES IN NET ASSETS		
	2008	2007
Revenue		
Net Patient Service Revenue	\$47.9	\$43.9
Other Revenues	0.9	0.7
Total Revenues	48.8	44.6
Expenses		
Salaries and Benefits	25.7	24.0
Medical Supplies and Drugs	4.2	3.9
Insurance	0.6	0.6
Other Supplies	1.3	1.2
Depreciation and Amortization	2.7	2.9
Other Expenses	15.0	12.6
Total Expenses	49.5	45.2
Operating Income (Loss)	-0.7	-0.6
Non-operating Revenues (Expenses)	0.5	1.0
Increase (Decrease) In Net Assets	-0.1	0.4
Net Assets Beginning of the Year	35.5	35.1
Net Assets End of the Year	\$35.4	\$35.5

The Hospital reported a \$0.1 million decrease in net assets for Calendar Year 2008. Net assets is the difference between net patient service revenues and the expenses incurred to perform those services.

The primary components for net assets in 2008 are:

- The Hospital's net operating revenues of \$48.8 million increased by \$4.2 million or 9.4% from prior year. Inpatient service revenue increased 13% and outpatient revenue increased 7%. Inpatient Behavioral Health patient days increased 20% as a result of increasing beds in service from 14 to 20.
- The Hospital's operating expenses of \$49.5 million increased by \$4.3 million or 9.5% from prior year. Salaries increased \$1.4 million, benefits, physician fees, and supplies increased by \$0.4 million each, interest increased \$0.6 million, and bad debts increased \$0.5 million. Self pay revenue increased \$1.2 million or 22% in 2008.

Capital Assets and Debt Administration

Capital Assets

At the end of 2008, the Hospital had \$33.7 million invested in capital assets. The Hospital had a net increase of \$0.1 million over prior year. The table displayed below documents the type of assets that makeup the capital assets held by the hospital as of December 31, 2008.

Capital Assets at Year-End Net of Depreciation		
	2008	2007
Land	\$1.2	\$1.2
Land Improvements/Leasehold Improvements	0.8	0.7
Building	37.9	36.2
Equipment	22.4	21.6
Total	62.3	59.7
Less Accumulated Depreciation	29.1	26.7
Subtotal	33.2	33.0
Construction In Progress	0.5	0.6
Capital Assets (Net)	\$33.7	\$33.6

Debt

At year-end, the Hospital had approximately \$21.4 million in long-term debt (financial statements are shown net of bond discount). The table below documents the debt held.

Outstanding Debt at Year End		
	2008	2007
Variable Rate Hospital Revenue Bonds		
2001 Revenue Bonds	\$2.3	\$3.0
Indiana Health Facility Financing Authority (IHFFA)		
1998/1999 Revenue Bonds	0.1	0.2
2006 Revenue Bond (Refunded 1998 and 1999 series)	18.3	18.4
PACS Capital Lease	0.7	0.9
Total Debt	\$21.4	\$22.5

Contacting the Hospital's Management

This financial report is designed to provide our citizens, taxpayers, patients, and other interested parties with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it received. If you have questions about this report or need additional financial information, please contact Daviess Community Hospital, Department of Finance, 1314 East Walnut Street, PO Box 760, Washington, IN 47501.

DAVIESS COMMUNITY HOSPITAL
STATEMENT OF NET ASSETS
December 31, 2008

Assets

Current assets:	
Cash and cash equivalents	\$ 1,354,447
Patient accounts receivable, net of estimated uncollectibles of \$4,536,562	7,074,848
Supplies and other current assets	3,285,442
Noncurrent cash and investments:	
Internally designated	9,516,668
Held by trustee for debt service	3,396,393
Capital assets:	
Land and construction in progress	1,753,902
Depreciable capital assets, net of accumulated depreciation	31,938,061
Other assets	<u>904,674</u>
 Total assets	 <u><u>\$ 59,224,435</u></u>

Liabilities and Net Assets

Current liabilities:	
Current maturities of long-term debt	\$ 1,562,955
Accounts payable and accrued expenses	2,516,488
Other current liabilities	1,245,607
Long-term debt, net of current maturities	<u>18,548,296</u>
 Total liabilities	 <u>23,873,346</u>
Net assets:	
Invested in capital assets, net of related debt	13,580,712
Restricted:	
For debt service	3,396,393
Unrestricted	<u>18,373,984</u>
 Total net assets	 <u>35,351,089</u>
 Total liabilities and net assets	 <u><u>\$ 59,224,435</u></u>

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

DAVIESS COMMUNITY HOSPITAL
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
Year Ended December 31, 2008

Operating revenues:	
Net patient service revenue (net of provision for bad debt)	\$ 47,988,245
Other	<u>857,844</u>
Total operating revenues	<u>48,846,089</u>
Operating expenses:	
Salaries and benefits	25,772,755
Medical supplies and drugs	4,199,964
Insurance	597,635
Other supplies	1,278,749
Other expenses	14,991,929
Depreciation and amortization	<u>2,696,743</u>
Total operating expenses	<u>49,537,775</u>
Operating loss	<u>(691,686)</u>
Nonoperating revenues:	
Investment income	485,816
Gain on sale of equipment	3,922
Other	<u>58,426</u>
Total nonoperating revenues	<u>548,164</u>
Decrease in net assets	(143,522)
Net assets beginning of the year	<u>35,494,611</u>
Net assets end of the year	<u><u>\$ 35,351,089</u></u>

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

DAVIESS COMMUNITY HOSPITAL
STATEMENT OF CASH FLOWS - RESTRICTED AND UNRESTRICTED FUNDS
Year Ended December 31, 2008

Cash flows from operating activities:	
Receipts from and on behalf of patients	\$ 48,276,756
Payments to suppliers and contractors	(5,177,286)
Payments to employees	(25,772,755)
Other receipts and payments, net	<u>(12,714,751)</u>
Net cash provided by operating activities	<u>4,611,964</u>
Cash flows from capital and related financing activities:	
Principal paid on long-term debt	(1,072,536)
Interest paid on long-term debt	(1,036,743)
Purchase of capital assets	<u>(2,716,257)</u>
Net cash used by capital and related financing activities	<u>(4,825,536)</u>
Cash flows from investing activities:	
Interest and dividends on investments	485,816
Proceeds from sale of investments	<u>643,000</u>
Net cash provided by investing activities	<u>1,128,816</u>
Net increase in cash and cash equivalents	915,244
Cash and cash equivalents at beginning of year	<u>6,802,264</u>
Cash and cash equivalents at end of year	<u>\$ 7,717,508</u>
Reconciliation of cash and cash equivalents to the Statement of Net Assets:	
Cash and cash equivalents in current assets	\$ 1,354,447
Restricted cash and cash equivalents	<u>6,363,061</u>
Total cash and cash equivalents	<u>\$ 7,717,508</u>
Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	\$ (691,686)
Adjustments to reconcile operating loss to net cash flows used in operating activities:	
Depreciation and amortization	2,696,743
Provision for bad debts	3,308,638
Other nonoperating revenues	58,426
Gain on sale of equipment	3,922
(Increase) decrease in current assets:	
Patient accounts receivable	(3,020,127)
Supplies and other current assets	409,397
Other assets	3,724
Increase in current liabilities:	
Accounts payable and accrued expenses	489,665
Other current liabilities	<u>1,353,262</u>
Net cash provided in operating activities	<u>\$ 4,611,964</u>

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

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS

I. Summary of Significant Accounting Policies

A. Reporting Entity

Daviess Community Hospital (Hospital) is a County-owned facility and operates under the Indiana County Hospital Law, Indiana Code 16-22. The Hospital provides short-term inpatient and out-patient health care.

The Board of County Commissioners of Daviess County appoints the Governing Board of the Hospital and a financial benefit/burden relationship exists between the County and the Hospital. For these reasons, the Hospital is considered a component unit of Daviess County.

On October 19, 1967, the Board of County Commissioners of Daviess County, upon written request of the Hospital Board of Trustees, created the Daviess Community Hospital Association. The Association was created pursuant to the provisions of Indiana Code 16-22-6 for the exclusive purpose of financing and constructing Hospital facilities for the Hospital.

The accompanying financial statements present the activities of the Hospital (primary government) and its significant component units. The component units discussed below are included in the Hospital's reporting entity because of the significance of their operational or financial relationships with the Hospital. Blended component units, although legally separate entities, are in substance part of the government's operations and exist solely to provide services for the government; data from these units is combined with data of the primary government. Discretely presented component units are involved in activities of an operational nature independent from the government; their transactions are reported in a separate column in the basic financial statements to emphasize that it is legally separate from the Hospital.

Management has chosen to omit from these financial statements component units that have significant operational or financial relationships with the Hospital. Accordingly, the financial statements do not include the data of all of the Hospital's component units necessary for reporting in conformity with accounting principles generally accepted in the United States.

Blended Component Units

The Daviess Community Hospital Foundation (Foundation) is a significant blended component unit of the Hospital. The primary government appoints a voting majority of the Foundation's Board and a financial benefit/burden relationship exists between the Hospital and the Foundation. Although it is legally separate from the Hospital, the Foundation is reported as if it were a part of the Hospital because it provides services entirely or almost entirely to the Hospital.

B. Enterprise Fund Accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

C. Assets, Liabilities and Net Assets or Equity

1. Deposits and Investments

Cash and cash equivalents include demand deposits and investments in highly liquid debt instruments with an original maturity date of three months or less.

Short-term investments are investments with remaining maturities of up to 90 days.

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.

Other investments are generally reported at fair value.

Investment income, including changes in the fair value of investments, is reported as non-operating revenues in the Statement of Revenues, Expenses, and Changes in Net Assets.

2. Use of Estimates

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

3. Capital Assets

Capital assets, which include land, land improvements, buildings and improvements, and equipment, are reported at actual or estimated historical cost based on appraisals or deflated current replacement cost. Contributed or donated assets are reported at estimated fair value at the time received.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods and estimated useful lives of capital assets reported in the financial statements are as follows:

	Capitalization Threshold	Depreciation Method	Estimated Useful Life
Land improvements	\$ 500	Straight-line	*
Buildings and improvements	500	Straight-line	*
Equipment	500	Straight-line	*

*Estimated lives have been assigned in accordance with the American Hospital Association Uniform Chart of Accounts and the Hospital's actual life experience.

For depreciated assets, the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed.

4. Net Assets

Net assets of the Hospital are classified in three components.

Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets.

Restricted expendable net assets are noncapital net 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, discussed in Note II.H.

Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

D. Grants and Contributions

From time to time, the Hospital receives grants from Daviess County and the State of Indiana 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. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

E. Restricted Resources

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.

F. Operating Revenues and Expenses

The Hospital's Statement of Revenues, Expenses, and Changes in Net Assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Hospital's principal activity. Nonexchange revenues, including grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

G. Compensated Absences

The Hospital's policy on paid days-off (which includes vacation, sick leave, and holidays) allows full-time employees and regular part-time employees to accrue paid days-off, to a maximum of 265 hours.

Paid days-off are accrued when incurred and reported as a liability.

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

II. Detailed Notes

A. Deposits and Investments

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Indiana Code 5-13-8-1 allows a political subdivision of the State of Indiana to deposit public funds in a financial institution only if the financial institution is a depository eligible to receive state funds; and has a principal office or branch that qualifies to receive public funds of the political subdivision. Balances were insured by the Federal Deposit Insurance Corporation or the Public Deposit Insurance Fund, which covers all public funds held in approved depositories. Deposits with financial institutions in the State of Indiana at year end were entirely insured by the Federal Depository Insurance Corporation or by the Indiana Public Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

B. Accounts Receivable and Payable

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the Hospital at year end consisted of these amounts:

Patient Accounts Receivable

Receivable from patients and their insurance carriers	\$ 6,925,856
Receivable from Medicare	3,485,814
Receivable from Medicaid	<u>1,199,740</u>

Total patient accounts receivable	11,611,410
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Less allowance for uncollectible amounts	<u>4,536,562</u>
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Patient accounts receivable, net	<u><u>\$ 7,074,848</u></u>
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Accounts Payable and Accrued Expenses

Payable to employees (including payroll taxes)	\$ 1,176,122
Payable to suppliers	<u>1,340,366</u>

Total accounts payable and accrued expenses	<u><u>\$ 2,516,488</u></u>
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C. Capital Assets

Capital asset activity for the year ended December 31, 2008, was as follows:

DAVISS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

<u>Primary Government</u>	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 1,170,484	\$ 62,184	\$ -	\$ 1,232,668
Construction in progress	<u>576,959</u>	<u>1,810,313</u>	<u>1,866,038</u>	<u>521,234</u>
Total capital assets, not being depreciated	<u>1,747,443</u>	<u>1,872,497</u>	<u>1,866,038</u>	<u>1,753,902</u>
Capital assets, being depreciated:				
Land improvements	729,118	49,637	3,325	775,430
Buildings and improvements	36,158,396	1,798,886	75,915	37,881,367
Equipment	<u>21,630,475</u>	<u>990,180</u>	<u>259,759</u>	<u>22,360,896</u>
Totals	<u>58,517,989</u>	<u>2,838,703</u>	<u>338,999</u>	<u>61,017,693</u>
Less accumulated depreciation for:				
Land improvements	366,242	20,112	1,972	384,382
Buildings and improvements	10,348,863	1,107,821	98,438	11,358,246
Equipment	<u>15,978,377</u>	<u>1,683,284</u>	<u>324,657</u>	<u>17,337,004</u>
Totals	<u>26,693,482</u>	<u>2,811,217</u>	<u>425,067</u>	<u>29,079,632</u>
Total capital assets, being depreciated, net	<u>31,824,507</u>	<u>27,486</u>	<u>(86,068)</u>	<u>31,938,061</u>
Total primary government capital assets, net	<u>\$ 33,571,950</u>	<u>\$ 1,899,983</u>	<u>\$ 1,779,970</u>	<u>\$ 33,691,963</u>

D. Construction Commitments

Construction work in progress is composed of the following:

<u>Project</u>	<u>Total Project Authorized</u>	<u>Expended to December 31, 2008</u>	<u>Required Future Funding</u>
CT project	\$ 27,868	\$ 22,000	\$ 5,868
Phone project	351,045	234,505	116,540
Capital equipment	245,255	245,255	-
McKesson project	<u>19,474</u>	<u>19,474</u>	<u>-</u>
Totals	<u>\$ 643,642</u>	<u>\$ 521,234</u>	<u>\$ 122,408</u>

DAVISS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

E. Leases

Capital Leases

The Hospital has entered into a capital lease for a PACS system. Future minimum lease payments and present values of the net minimum lease payments under the capital lease as of December 31, 2008, are as follows:

2009	\$	258,409
2010		258,409
2011		<u>193,807</u>
Total minimum lease payments		710,625
Less amount representing interest		<u>44,215</u>
Present value of net minimum lease payments		<u><u>\$ 666,410</u></u>

Assets acquired through capital leases still in effect are as follows:

Equipment	\$	1,152,251
Accumulated depreciation		<u>556,921</u>
Total	\$	<u><u>595,330</u></u>

F. Long-Term Liabilities

1. Revenue Bonds

The Hospital issues bonds to be paid by income derived from the acquired or constructed assets. Revenue bonds outstanding at year end are as follows:

Purpose	Interest Rates	Amount
1998 Variable rate revenue bonds for hospital construction	Variable	\$ 100,000
2001 Variable rate revenue bonds for hospital construction	Variable	2,265,840
2006 Refunding revenue bonds for hospital improvements	Variable	<u>18,350,000</u>
Total		<u><u>\$ 20,715,840</u></u>

DAVISS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

Revenue bonds debt service requirements to maturity are as follows:

Year Ended December 31	Principal	Interest
2009	\$ 1,330,280	\$ 922,390
2010	1,360,280	863,057
2011	1,385,280	799,957
2012	655,000	751,630
2013	680,000	720,973
2014-2018	3,815,000	3,102,077
2019-2023	4,625,000	2,136,250
2024-2028	5,610,000	964,563
2029-2033	1,255,000	31,270
Totals	<u>\$ 20,715,840</u>	<u>\$ 10,292,167</u>

2. Advance Refunding

In prior years, the Hospital defeased certain bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments of the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Hospital's financial statements. The following outstanding bonds, at December 31, 2008, were considered defeased:

	Amount
Hospital	<u>\$ 15,670,000</u>

3. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2008, was as follows:

<u>Primary Government</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable:					
Revenue:					
Hospital Association	\$ 3,021,120	\$ -	\$ 755,280	\$ 2,265,840	\$ 755,280
Indiana Health Facility Financing Authority	195,000	-	95,000	100,000	100,000
Other revenue bonds	18,350,000	-	-	18,350,000	475,000
Less deferred amount on refunding	<u>1,331,522</u>	-	<u>60,523</u>	<u>1,270,999</u>	-
Total bonds payable	20,234,598	-	789,757	19,444,841	1,330,280
Capital leases	<u>888,666</u>	-	<u>222,256</u>	<u>666,410</u>	<u>232,675</u>
Total long-term liabilities	<u>\$ 21,123,264</u>	<u>\$ -</u>	<u>\$ 1,012,013</u>	<u>\$ 20,111,251</u>	<u>\$ 1,562,955</u>

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

4. Net Revenue Available for Debt Service

The following disclosures concerning net revenue available for debt service applicable to the years ended December 31, 2008, are required by terms of the financing agreement between the Hospital and IHFFA:

Revenue from operations	\$ 48,846,089
Investment income	485,816
Net gain on disposal of assets	3,922
Less:	
Expenses (excluding depreciation, amortization and interest on funded debt)	45,804,289
Total net revenue available for debt service	\$ 3,531,538
Funded debt service for year	\$ 2,109,279
Historical debt service coverage ratio	1.67:1

G. Charity Care

Charges excluded from revenue under the Hospital's charity care policy were \$711,702 for 2008.

H. Internally Designated Assets

Noncurrent cash and investments internally designated include the following:

1. Funded Depreciation – Amounts transferred from the Operating Fund by the Hospital Board of Trustees through funding depreciation expense. Such amounts are to be used for equipment and building, remodeling, repairing, replacing, or making additions to the Hospital buildings as authorized by IC 16-22-3-13.
2. Capital Improvement Funds – Funds designated by the Hospital Board of Trustees for construction and other capital improvement.
3. Designated Funds – Assets set aside by the Hospital Board of Trustees for identified purposes and over which the Board retains control and may, at its discretion, subsequently use for other purposes.

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

Internally designated:	
Funded depreciation:	
Cash and cash equivalents	\$ 2,201,855
Investments	<u>6,550,000</u>
Total funded depreciation	<u>8,751,855</u>
Capital improvement:	
Cash and cash equivalents	<u>38,040</u>
Board designation:	
Cash and cash equivalents	<u>726,773</u>
Total internally designated	<u><u>\$ 9,516,668</u></u>

III. Other Information

A. Risk Management

The Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; medical benefits to employees, retirees, and dependents (excluding postemployment benefits); and natural disasters.

The risks of torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; and natural disasters are covered by commercial insurance from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. There were no significant reductions in insurance by major category of risk.

Medical Benefits to Employees

The Hospital has chosen to establish a risk financing fund for risks associated with medical benefits to employees. The risk financing fund is accounted for in the operating fund where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of \$60,000 per year. Settled claims resulting from this risk did not exceed commercial insurance coverage in the past three years.

Claim expenditures and liabilities of the fund 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 (IBNRs). Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amounts of payouts and other economic and social factors.

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

Changes in the balance of claim liabilities during the past two years are as follows:

	2008	2007
Unpaid claims, beginning of fiscal year	\$ 140,245	\$ 156,831
Incurred claims and changes in estimates	2,388,100	2,209,672
Claim payments	(2,343,656)	(2,226,258)
Unpaid claims, end of fiscal year	\$ 184,689	\$ 140,245

B. Contingent Liabilities

Litigation

The Hospital is involved in litigation and regulatory investigations arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Hospital's future financial position or results from operations.

C. Postemployment Benefits

In addition to the pension benefits described in Note III.G., the Hospital provides postemployment health insurance benefits, as authorized by IC 5-10-8, to all employees who retire from the Hospital on or after attaining age 62 with at least 10 years of service. Currently, two retirees meet these eligibility requirements. The Hospital provides 56% to 58% of these postemployment benefits. Expenditures for those postemployment benefits are recognized on a pay-as-you-go basis. During the year ended December 31, 2008, expenditures of \$2,393 were recognized for postemployment benefits.

D. 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 Statement of Net Assets for cash and cash equivalents approximates its fair value.

Short-Term Investments

The carrying amount reported in the Statement of Net Assets is the investment's fair value on the day it becomes a short-term investment.

Investments

Fair values, which are the amounts reported in the Statement of Net Assets, are based on quoted market prices, if available, or are estimated using quoted market prices for similar securities.

DAVIESS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

Accounts Payable and Accrued Expenses

The carrying amount reported in the Statement of Net Assets for accounts payable and accrued expenses approximates its fair value.

E. Fair Value Measurements

Statement on Financial Accounting Standards No. 157, Fair Value Measurements (as amended), requires certain disclosures regarding the fair value of financial instruments. Financial instruments held by the Hospital impacted by this pronouncement include the Hospital's investments and assets whose use is limited which are measured using quoted prices in active markets and other significant observable inputs.

The Hospital partially adopted the provisions of FAS 157 for fiscal year 2008, but will delay adoption of nonfinancial assets and nonfinancial liabilities covered by FASB Staff Position No. FAS 157-2. This Staff Position permits entities to partially defer the effective date of FAS 157 for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis, until fiscal year 2009.

When fully adopted, the Hospital will apply the provisions of FAS 157-2 to certain nonfinancial assets and liabilities and is currently evaluating the impact of the full adoption of this statement on the activities, changes in net assets and financial position. Using the provisions within SFAS No. 157, the Hospital has characterized its investments in securities, based on the priority of the inputs used to value the investments, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities [Level 1], and the lowest priority to unobservable inputs [Level 3]. If the inputs used to measure the investments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the investment.

Investments recorded in the statement of financial position are categorized based on the inputs to valuation techniques as follows:

Level 1 - These are investments where values are based on unadjusted quoted prices for identical assets in an active market the Hospital has the ability to access. Investments include mutual funds.

Level 2 - These are investments where values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the investments. These investments are comprised of U.S. government securities that trade infrequently and certificates of deposit.

Level 3 - These are investments where values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect assumptions of management about assumptions market participants would use in pricing the investments.

DAVISS COMMUNITY HOSPITAL
NOTES TO FINANCIAL STATEMENTS
(Continued)

Based upon the levels as defined the Hospital's investments as of December 31, 2008, are classified as follows:

Investment Type	December 31, 2008	Fair Value Measurements at Reporting Date Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Certificate of deposit	\$ 6,550,000	\$ -	\$ 6,550,000	\$ -

F. Estimated Third-Party Settlements

Regulations in effect require annual retroactive settlements for third-party settlements based upon cost reports filed by the Hospital. These retroactive settlements are estimated and recorded in the accompanying financial statements. Changes in these estimates are reflected in the year in which they occur. During 2008, net patient service revenues in the accompanying statements of operations were increased by \$55,890, to reflect changes in the estimated settlements for certain prior years.

G. Pension Plan

Daviss Community Hospital Money Purchase Plan

Plan Description

The Hospital has a defined benefit pension plan administered by Principal Financial Group as authorized by IC 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:

Principal Mutual Life Insurance Company
711 High Street
Des Moines, IA 50392-0001
Ph. (515) 247-5111

Information is not available to report additional disclosure required by GASB Statement No. 27.

DAVISS COMMUNITY HOSPITAL
AUDIT RESULTS AND COMMENTS

CREDIT CARDS

The Hospital is using credit cards to purchase items without an approved credit card policy.

The Hospital does have safekeeping procedures in place for the credit cards that they use.

The State Board of Accounts will not take exception to the use of credit cards by a governmental unit provided the following criteria are observed:

- (1) The governing board must authorize credit card use through an ordinance or resolution, which has been approved in the minutes.
- (2) Issuance and use should be handled by an official or employee designated by the board.
- (3) The purposes for which the credit card may be used must be specifically stated in the ordinance or resolution.
- (4) When the purpose for which the credit card has been issued has been accomplished, the card should be returned to the custody of the responsible person.
- (5) The designated responsible official or employee should maintain an accounting system or log which would include the names of individuals requesting usage of the cards, their position, estimated amounts to be charged, fund and account numbers to be charged, date the card is issued and returned, etc.
- (6) Credit cards should not be used to bypass the accounting system. One reason that purchase orders are issued is to provide the fiscal officer with the means to encumber and track appropriations to provide the governing board and other officials with timely and accurate accounting information and monitoring of the accounting system.
- (7) Payment should not be made on the basis of a statement or a credit card slip only. Procedures for payments should be no different than for any other claim. Supporting documents such as paid bills and receipts must be available. Additionally, any interest or penalty incurred due to late filing or furnishing of documentation by an officer or employee should be the responsibility of that officer or employee.
- (8) If properly authorized, an annual fee may be paid.

(Accounting and Uniform Compliance Guidelines Manual for County and City Hospitals, Chapter 1)

ACCOUNTS PAYABLE

During the testing of accounts payable, it was noted that there were multiple open purchase orders, some of which dated back to 1996. Upon reviewing the payable report, batch #5, it was discovered that the Laboratory Manager creates a purchase order to generate an account payable at the end of the month. However, when the actual order is placed in the next month for the inventory or supply, a new purchase order is created by the Manager. This resulted in open purchase orders in the amount of \$58,920, as well as \$53,926 in credits, to one vendor, which had not been cleared off of the accounts payable system as of December 31, 2008.

DAVIESS COMMUNITY HOSPITAL
AUDIT RESULTS AND COMMENTS
(Continued)

According to the Daviess Community Hospital personnel, the vendor in question for Batch #5 has not been used since 2001. This is a concern considering that the credits were created in 2004 by the Laboratory Department.

The Field Examiner tested December 31, 2008, Payables #3 batch report; this batch also contained old, open purchase orders, some that date back to 1998, and multiple instances where the purchase orders were either closed or completed.

There is no reconciliation of open purchase orders to an outstanding accounts payable listing at year end. The unit does not appear to analyze the accounts payable with the individual open invoice totals.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objectives, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets and all forms of information processing are necessary for proper internal control. (Accounting and Uniform Compliance Guidelines Manual for County and City Hospitals, Chapter 1)

DEPOSITORY RECONCILEMENTS

The Hospital did not prepare monthly reconcilements of the account balances recorded in the accounting records to the balance in bank accounts on a timely basis. At December 31, 2007, there was an unidentified discrepancy between the bank balance and the ledger balance of \$231.44. This discrepancy increased monthly during 2008 leading to an unidentified discrepancy of \$3,870.04 at December 31, 2008.

To provide for adequate safeguarding of cash and to enable the hospital to identify and correct errors on a timely basis, a reconciliation of the account balances recorded in the accounting records to the balances of the depository accounts should be performed by the hospital at least monthly. (Accounting and Uniform Compliance Guidelines Manual for County and City Hospitals, Chapter 9)

INTERNAL CONTROLS

Controls over the receipting, disbursing, recording, and accounting for financial activities were insufficient.

The account, Deferred Loss on Bond Refund, had three entries posted, for a total of \$159,617.35, that were incorrect. The 2008 amortization expense was posted with the 2007 calculation which resulted in an understatement of \$26,253.67. The unit received an unidentified charge from the bond bank in the amount of \$136,547.08 which was charged to the deferral loss on Bond refund which resulted in an overstatement. There was an additional amount of \$3,183.40 credited to the fund.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objectives, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets and all forms of information processing are necessary for proper internal control. (Accounting and Uniform Compliance Guidelines Manual for County and City Hospitals, Chapter 1)

DAVIESS COMMUNITY HOSPITAL
AUDIT RESULTS AND COMMENTS
(Continued)

INTERNAL CONTROLS OVER FINANCIAL TRANSACTIONS AND REPORTING

We noted several deficiencies in the internal control system of the Daviess Community Hospital (Hospital) related to financial transactions and reporting. We believe the following deficiencies constitute material weaknesses:

1. **Preparing Financial Statements:** Effective internal control over financial reporting involves the identification and analysis of the risks of material misstatement to the Daviess Community Hospital's audited financial statements and then determining how those identified risks should be managed. The Hospital has not identified risks to the preparation of reliable financial statements and as a result has failed to design effective controls over the preparation of the financial statements to prevent or detect material misstatements, including Notes to the Financial Statements.
2. **Monitoring of Controls:** Effective internal control over financial reporting requires the Hospital Board to monitor and assess the quality of the Daviess Community Hospital's system of internal control. The Hospital Board has not performed either an ongoing or separate evaluation of their system of internal controls. The failure to exercise their oversight responsibility place the Hospital at risk that controls may not be designed or operating effectively to provide reasonable assurance that controls will prevent or detect material misstatements in a timely manner. Additionally, the Hospital has no process to identify or communicate corrective actions to improve controls.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objections, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets and all forms of information processing are necessary for proper internal control. (Accounting and Uniform Compliance Guidelines Manual for County and City Hospitals, Chapter 1)

DAVISS COMMUNITY HOSPITAL
EXIT CONFERENCE

The contents of this report were discussed on August 13, 2009, with Gary Kendrick, Executive Director; Brad Hardcastle, Chief Financial Officer; Anthony R. Showalter, Vice President of the Hospital Board; and Kenneth Parsons, Chairman of the Hospital Board.