

APR 06 2009

JOHNSON MEMORIAL HOSPITAL

COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2008 AND 2007

CPAs / ADVISORS



JOHNSON MEMORIAL HOSPITAL

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REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Johnson Memorial Hospital
Franklin, Indiana

We have audited the accompanying combined balance sheets of Johnson Memorial Hospital (Hospital) as of December 31, 2008 and 2007 and the related combined statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These combined financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, issued by the Comptroller General of the United States, Guidelines for Examination of Entities Receiving Financial Assistance From Governmental Sources and Guidelines for Audits of County and City Hospitals by Independent Certified Public Accountants issued by the Indiana State Board of Accounts. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above, present fairly, in all material respects, the combined financial position of the Hospital as of December 31, 2008 and 2007, and the results of its operations, changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis on pages i through vii is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. 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.

Board of Trustees
Johnson Memorial Hospital
Franklin, Indiana

In accordance with *Government Auditing Standards*, we have issued, under separate cover, our report dated March 19, 2009, on our consideration of the Hospital's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audits.

Blue & Co., LLC

March 19, 2009

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

This section of Johnson Memorial Hospital's (Hospital) annual combined financial statements presents background information and management's discussion and analysis of the Hospital's financial performance during the year ended December 31, 2008. This MD&A also includes an analysis of the activities and results of the Johnson County Health Foundation (blended component unit).

This MD&A should be read together with the combined financial statements included in this report.

FINANCIAL HIGHLIGHTS

- The Hospital's net assets increased by \$500,000, and include operating income of \$2.3 million in 2008.
- The Hospital's total operating revenue increased by 10.8% to \$82.8 million while expenses increased by 8.8% to \$80.5 million. The resulting income from operations of \$2.2 million represents an increase of 220% from 2007 operations.
- The Hospital's total non-operating revenue decreased from a gain of \$1.59 million in 2007 to a loss of \$1.12 million in 2008 due mainly to investment losses in a declining stock market.
- During the year, the Hospital prepaid its 2007 85A Pool Loan Program debt due to the uncertainties in the market for insured bond issues. The amount prepaid was \$4.1 million (out of a total approved loan amount of \$6 million which was not entirely drawn upon). In turn, a commercial loan was taken out in the amount of \$4.5 million. The purpose of this funding was to finance a major portion of the private room bed renovation project that began in 2007.

FINANCIAL STATEMENTS

The Hospital's combined financial statements consist of three statements - a Balance Sheet; a Statement of Revenues, Expenses and Changes in Net Assets; and a Statement of Cash Flows. The Balance Sheet includes all of the Hospital's assets and liabilities, including assets held by the Hospital but restricted for specific purposes by contributors, grantors, or enabling legislation. The Balance Sheet provides a basis for computing rate of return, evaluating the capital structure of the Hospital, and assessing the liquidity and financial flexibility of the Hospital. The Statement of Revenues, Expenses and Changes in Net Assets includes all revenues and expenses of the Hospital. This statement measures the financial results of the Hospital's operations and presents revenue earned and expenses incurred. The Statement of Cash Flows provides information about the Hospital's cash flows from operating activities, capital and related financing activities, and investing activities, and provides information on the sources and uses of cash during the year.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

FINANCIAL ANALYSIS

The Balance Sheet and the Statement of Revenues, Expenses and Changes in Net Assets report information about the Hospital's activities. These two statements report the net assets of the Hospital and its changes. Increases or decreases in the Hospital's net assets are one indicator of whether its financial position is improving or deteriorating. However, other non-financial factors such as changes in economic conditions, population growth (including uninsured or medically indigent individuals and families), and new or changed governmental legislation should also be considered.

A summary of the Hospital's Balance Sheets as of December 31, 2008 and 2007 is presented below (in thousands):

	2008	2007	\$ Change	% Change
Cash and investments	\$ 36,206	\$ 34,731	\$ 1,475	4.2%
Capital assets	41,272	41,639	(367)	-0.9%
Other assets	20,424	17,687	2,737	15.5%
Total assets	\$ 97,902	\$ 94,057	\$ 3,845	4.1%
Current and other liabilities	\$ 12,559	\$ 9,372	\$ 3,187	34.0%
Long term debt	4,451	4,293	158	3.7%
Total liabilities	17,010	13,665	3,345	24.5%
Net assets				
Invested in capital assets, net of related debt	35,477	36,237	(760)	-2.1%
Restricted	7,703	8,918	(1,215)	-13.6%
Unrestricted	37,712	35,237	2,475	7.0%
Total net assets	80,892	80,392	500	0.6%
Total liabilities and net assets	\$ 97,902	\$ 94,057	\$ 3,845	4.1%

As displayed above, total net assets increased to \$80.9 million in 2008, up from \$80.4 million in 2007. The change in net assets resulted primarily from operating gains. Investment income had a negative impact on total excess revenues during 2008, which was the experience for nearly all industries throughout the state and nation.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

A summary of the Hospital's Statement of Revenues, Expenses and Changes in Net Assets for 2008 and 2007 is presented below (in thousands):

	2008	2007	\$ Change	% Change
Revenue				
Net patient service revenue	\$ 72,598	\$ 66,462	\$ 6,135	9.2%
Other	10,181	8,271	1,910	23.1%
Total revenue	82,780	74,733	8,047	10.8%
Expenses				
Salary and benefits	43,068	40,748	2,320	5.7%
Supplies and other	32,663	28,546	4,117	14.4%
Depreciation and amortization	4,801	4,736	65	1.4%
Total operating expenses	80,532	74,031	6,501	8.8%
Operating income	2,247	702	1,544	219.9%
Non-operating income	(1,122)	1,586	(2,707)	170.6%
Excess of revenues over expenses	1,127	2,289	(1,163)	-50.8%
Other changes in net assets	(627)	58	(684)	-1184.6%
Change in net assets	\$ 500	\$ 2,347	\$ (1,846)	-78.7%

SOURCES OF REVENUE

During 2008, the Hospital derived substantially all of its revenue from patient services and other related activities. Revenue includes, among other items, revenue from the Medicare and Medicaid programs, patients, insurance carriers, preferred provider organizations, and managed care programs.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

The table below presents the percentages of gross revenue for patient services, by payor, for 2008 and 2007.

<u>Payor Mix</u>	<u>2008</u>	<u>2007</u>
Medicare	46%	46%
Medicaid	9%	9%
Commercial insurance	18%	21%
Blue Cross/Anthem	16%	15%
Self-pay	9%	7%
Other	2%	2%
Total	<u>100%</u>	<u>100%</u>

The Hospital entered into agreements with third party payers, including government programs and managed care health plans, under which payments for healthcare services provided to patients are based upon predetermined rates or discounts from gross charges. Provisions have been made in the financial statements for contractual adjustments, which represent the difference between the standard charges for services and the actual or estimated payment.

OPERATING AND FINANCIAL PERFORMANCE

Overall, the Hospital's financial performance in 2008 was considerably stronger than that experienced in 2007. This section discusses highlights of 2008 operations and changes in activities.

(a) Revenue

- Net patient revenues increased in 2008 compared to 2007 primarily as a result of an increase in both inpatient and outpatient volumes associated with the temporary closure of Columbus Regional Hospital from June – October 2008.
 - Acute inpatient volume, as measured in terms of admissions, increased to 3,862 in 2008 from 3,464 in 2007, or 11.5%.
 - Acute rehabilitation volume, as measured in terms of admissions, decreased to 200 in 2008 from 228 in 2007, or 12.3%.
 - The Hospital discontinued its skilled nursing services in October, which by year end resulted in a reduction in patient volumes over the previous year, of 2,017 patient days.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

- There was also growth experienced in outpatient volumes. Gross outpatient charges increased by 10.2% over 2007, which also factors in a 7% rate increase.
- Excluded from net patient revenue are charges for patient services waived under the Hospital's charity policy. Charity care represents unreimbursed charges incurred by the Hospital in providing uncompensated care to indigent patients. Based on established rates, gross charges of \$2.6 million were waived in 2008, compared to \$1.8 million in 2007.

(b) Expenses

- Total operating expenses increased \$6.5 million or 8.8% in 2008 primarily due to the increase in general inflationary pressures, the addition of new employed physicians, and the increased volumes experienced during the year. Further discussion follows:
 - Employee labor and benefit expenses increased \$2.3 million or 5.7% over 2007. With the closure of the Hospital's Skilled Nursing Facility unit in October 2008, labor expenses were not as high as would have been experienced otherwise. Supplies and other expenses increased \$4.1 million or 14.4% over 2007. The increase is mostly attributable to higher volumes and utilization.
 - Provision for bad debt expenses increased \$1.2 million or 21.5% over 2007, primarily related to the increased volume and significant amount of self-pay patients from Bartholomew County who utilized the Hospital while Columbus Regional was out of business. The combined charity care/bad debt write-offs as a percent of hospital gross patient revenues increased from 5.2% in FY 2007 to 5.9% in FY 2008.
 - Depreciation and amortization expenses increased slightly over 2007 due to new capital assets being placed in service in 2008.

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MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

CAPITAL ASSETS

During 2008, the Hospital's capital assets decreased by \$367,000 due to depreciation outpacing capital additions and construction in progress. The below table summarizes the broad categories (in thousands):

	2008	2007	\$ Change	% Change
Land and improvements	\$ 4,353	\$ 4,338	\$ 15	0.4%
Buildings and improvements	50,842	49,919	924	1.9%
Equipment	37,465	37,278	187	0.5%
Total capital assets	92,661	91,534	1,127	1.2%
Less accumulated depreciation	57,727	56,002	1,725	3.1%
Construction in progress	6,338	6,107	231	3.8%
Capital assets - net	\$ 41,272	\$ 41,639	\$ (367)	-0.9%

The increase in capital assets and corresponding accumulated depreciation is attributable to the Hospital's commitment to replace equipment as it becomes obsolete as well as upgrade its facilities and the capabilities of its information systems.

LONG TERM DEBT

As of December 31, 2008, the Hospital had \$5.8 million in short term and long term notes and bonds, an increase of \$400,000 from the \$5.4 million as of December 31, 2007. More detailed information about the Hospital's debt position is presented in the Notes to the Combined Financial Statements.

ECONOMIC FACTORS AND 2009 BUDGET

The Hospital's Board and management considered many factors when establishing the 2009 Budget. Included was the status of the economy, which takes into account market factors and other environmental factors such as the following items:

- Population growth of Johnson County, Indiana and the Hospital's current market share of county residents
- Advances in medical equipment and information systems technology and the need to replace obsolete equipment

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MANAGEMENT DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2008 AND 2007

- Decreasing reimbursement from governmental and commercial insurance payers as well as the increasingly unfavorable governmental payer mix the Hospital is experiencing
- Increasing number of uninsured, underinsured and/or indigent patients
- Increasing costs of technology, medical supplies, pharmaceuticals, and medical malpractice insurance
- The increasing need to partner with a tertiary-level Indianapolis hospital(s) for services the Hospital is not capable of implementing on its own
- Increasing awareness and expectations from the public on the quality of services
- Increased competition from niche and physician providers as well as the continued expansion of the major Indianapolis providers of healthcare into the Johnson County market (i.e., St. Francis, Community Health Network and Clarian)

CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

This report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Hospital's Chief Financial Officer, Elizabeth A. Hedden, at Johnson Memorial Hospital, P.O. Box 549, Franklin, Indiana 46131.

JOHNSON MEMORIAL HOSPITAL

COMBINED BALANCE SHEETS DECEMBER 31, 2008 AND 2007

ASSETS

	<u>2008</u>	<u>2007</u>
Current assets		
Cash and cash equivalents	\$ 2,849,804	\$ 3,117,883
Investments	11,482,168	11,091,894
Assets whose use is limited, current portion	1,344,260	1,108,448
Patient accounts receivable, net of allowance for uncollectible accounts of \$3,908,000 in 2008 and \$2,524,000 in 2007	13,806,722	11,514,298
Other accounts receivable	2,380,619	1,245,425
Inventory and other current assets	2,438,708	2,440,046
Current portion of notes receivable	97,692	96,000
Total current assets	<u>34,399,973</u>	<u>30,613,994</u>
Assets whose use is limited		
Internally designated	21,200,747	19,650,893
Held by trustee for debt service	673,643	870,630
Total assets whose use is limited	<u>21,874,390</u>	<u>20,521,523</u>
Less current portion	<u>1,344,260</u>	<u>1,108,448</u>
Noncurrent assets whose use is limited	20,530,130	19,413,075
Capital assets		
Land	3,141,963	3,141,963
Depreciable capital assets, net	<u>38,130,188</u>	<u>38,496,546</u>
Total capital assets, net	41,272,151	41,638,509
Other assets		
Foundation assets	1,170,089	1,795,873
Notes receivable, net of current portion	118,137	212,971
Investment in affiliated companies	394,042	345,887
Other assets	17,755	36,986
Total other assets	<u>1,700,023</u>	<u>2,391,717</u>
Total assets	<u><u>\$ 97,902,277</u></u>	<u><u>\$ 94,057,295</u></u>

See accompanying notes to combined financial statements.

JOHNSON MEMORIAL HOSPITAL

COMBINED BALANCE SHEETS DECEMBER 31, 2008 AND 2007

LIABILITIES AND NET ASSETS

	<u>2008</u>	<u>2007</u>
Current liabilities		
Accounts payable and accrued expenses	\$ 2,249,976	\$ 2,125,095
Accrued wages and related liabilities	7,861,919	5,801,827
Estimated third-party settlements	731,749	336,778
Current portion of long term debt	1,344,260	1,108,448
Other current liabilities	371,484	-0-
Total current liabilities	<u>12,559,388</u>	<u>9,372,148</u>
Long term debt, net of current portion		
Capital lease obligations	149,577	197,950
Other long term debt	<u>4,301,876</u>	<u>4,095,499</u>
Total long term debt	<u>4,451,453</u>	<u>4,293,449</u>
Total liabilities	17,010,841	13,665,597
Net assets		
Invested in capital assets, net of related debt	35,476,438	36,236,612
Restricted		
For debt service	673,643	870,630
Expendable - funded depreciation	4,936,219	4,736,111
Expendable - other specific purpose	924,297	1,515,768
Held by Foundation	<u>1,168,710</u>	<u>1,795,570</u>
Total restricted net assets	<u>7,702,869</u>	<u>8,918,079</u>
Unrestricted	<u>37,712,129</u>	<u>35,237,007</u>
Total net assets	<u>80,891,436</u>	<u>80,391,698</u>
Total liabilities and net assets	<u>\$ 97,902,277</u>	<u>\$ 94,057,295</u>

See accompanying notes to combined financial statements.

JOHNSON MEMORIAL HOSPITAL

COMBINED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
Revenues		
Net patient service revenue	\$ 72,598,213	\$ 66,461,966
Other revenue	10,181,416	8,271,070
Total revenues	82,779,629	74,733,036
Expenses		
Salaries and wages	34,131,582	32,386,853
Employee benefits	8,936,091	8,361,186
Medical professional fees	916,151	623,050
Other professional fees	8,312,748	6,461,539
Medical supplies and drugs	10,304,615	9,868,588
Other supplies	954,877	901,514
Depreciation and amortization	4,800,552	4,735,572
Insurance	1,094,651	920,996
Other expenses	11,080,173	9,770,662
Total expenses	80,531,440	74,029,960
Operating income	2,248,189	703,076
Nonoperating revenues (expenses)		
Investment income (loss)	(1,046,950)	1,441,922
Interest expense	(68,096)	(97,599)
Gain (loss) on sale of equipment	24,284	(45,514)
Other nonoperating income (expense)	(30,829)	287,455
Nonoperating revenues (expenses), net	(1,121,591)	1,586,264
Excess revenues over expenses	1,126,598	2,289,340
Other changes in net assets		
Change in Foundation net assets	(626,860)	57,706
Change in net assets	499,738	2,347,046
Net assets		
Beginning of year	80,391,698	78,044,652
End of year	\$ 80,891,436	\$ 80,391,698

See accompanying notes to combined financial statements.

JOHNSON MEMORIAL HOSPITAL

COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
Operating activities		
Cash received from patient services	\$ 70,700,760	\$ 70,626,801
Cash paid for salaries, wages and benefits	(41,007,581)	(39,043,406)
Cash paid to vendors and suppliers	(33,629,751)	(29,630,665)
Other receipts, net	11,155,476	8,258,878
Net cash flows from operating activities	7,218,904	10,211,608
Capital and related financing activities		
Receipts on notes receivable, net	93,142	95,630
Proceeds from long term debt	4,500,000	2,744,249
Payments on long term debt, net	(4,138,147)	(1,029,638)
Interest on long term debt	(68,096)	(97,599)
Gain (loss) on sale of property and equipment	24,284	(45,514)
Purchases of capital assets	(4,466,429)	(6,584,053)
Proceeds from sale of capital assets	67,606	42,829
Net cash flows from capital and related financing activities	(3,987,640)	(4,874,096)
Investing activities		
Other nonoperating income (expense)	(30,829)	287,455
Investment income (loss)	(1,046,950)	1,441,922
Change in Foundation net assets	(626,860)	57,706
Other changes in investments	(441,837)	(3,707,017)
Other changes in assets whose use is limited	215,678	(1,626,313)
Net cash flows from investing activities	(1,930,798)	(3,546,247)
Net change in cash and cash equivalents	1,300,466	1,791,265
Cash and cash equivalents		
Beginning of year	5,135,885	3,344,620
End of year	\$ 6,436,351	\$ 5,135,885
Reconciliation of cash and cash equivalents to the balance sheets		
Cash and cash equivalents		
In current assets	\$ 2,849,804	\$ 3,117,883
In assets whose use is limited	3,586,547	2,018,002
Total cash and cash equivalents	\$ 6,436,351	\$ 5,135,885

See accompanying notes to combined financial statements.

JOHNSON MEMORIAL HOSPITAL

COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
Reconciliation of operating income to net cash from operating activities		
Operating income	\$ 2,248,189	\$ 703,076
Adjustments to reconcile operating income to net cash flows from operating activities		
Depreciation and amortization	4,800,552	4,735,572
Bad debts	6,659,886	5,482,788
Changes in operating assets and liabilities		
Patient accounts receivable	(8,952,310)	(2,384,538)
Other accounts receivable	(1,135,194)	(385,694)
Inventory and other current assets	1,338	(191,602)
Other assets	19,231	24,535
Change in foundation assets	625,784	(58,009)
Accounts payable and accrued expenses	123,805	(486,041)
Accrued wages and related liabilities	2,060,092	1,704,633
Estimated third-party settlements	394,971	1,066,585
Change in foundation liabilities	1,076	303
Net cash from operating activities	<u>\$ 7,218,904</u>	<u>\$ 10,211,608</u>
Supplemental disclosure of cash flows		
Cash paid for interest	\$ 68,096	\$ 97,599
Assets acquired through capital lease	\$ 31,963	\$ 263,122

See accompanying notes to combined financial statements.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Johnson Memorial Hospital (Hospital) is an acute-care hospital located in Franklin, Indiana, organized for the purpose of providing healthcare services to the residents of Johnson County and the surrounding communities. The 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 outpatient health care, skilled nursing and intermediate care and emergency care.

The Board of County Commissioners of Johnson County appoints the Governing Board of the Hospital. The Hospital is considered a component unit of Johnson County.

Accounting principles generally accepted in the United States require that these combined financial statements present the Hospital and its significant component units, collectively referred to as the "primary government." The blended component unit discussed below is 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 primary government's operations and exist solely to provide services for the primary government; data from these units is combined with data of the primary government.

Blended Component Unit

The accompanying combined financial statements include the accounts of Johnson County Health Foundation, Inc. (Foundation), a separate not-for-profit entity organized to support the operations of the Hospital. The separate financial statements of the Foundation may be obtained through contacting their office as follows:

Johnson County Health Foundation, Inc.
1101 W. Jefferson St., Ste. V
Franklin, IN 46131

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Use of Estimates

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

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.

Cash and Cash Equivalents

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

Investments

Nonparticipating certificates of deposit, demand deposits and similar negotiable instruments that are not reported as cash and cash equivalents are reported as investments at fair value.

Debt securities are reported at fair value. Debt securities are defined as securities backed by the full faith and credit of the United States Treasury or fully insured or guaranteed by the United States or any United States government agency.

Mutual funds are reported at fair value based on the fund's market price. Money market investments that mature within one year or less at the date of their acquisition are reported at fair value. Other money market investments are reported at fair value.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Other investments are generally reported at fair value.

The Hospital holds Level 1 investments, in which fair market values are readily determinable using quoted prices in active markets for identical assets as determined by FAS 157: *Fair Value Measurements*. Level 2 investments fair market values are determined by significant other observable inputs.

Investment income, including changes in the fair value of investments, is reported as nonoperating revenue in the combined statements of revenues, expenses and changes in net assets.

Patient Accounts Receivable and Patient Service Revenues

Patient revenues and the related accounts receivable are recorded at the time services to patients are performed. The Hospital is a provider of services to patients entitled to coverage under Titles XVIII and XIX of the Health Insurance Act (Medicare and Medicaid). The Hospital is reimbursed for Medicare and Medicaid inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG). The Hospital is reimbursed for Medicare and Medicaid outpatient services based on a fixed price per clinical unit of service. Differences between the total program billed charges and the payments received are reflected as deductions from revenue. At the Hospital's year-end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients. The difference between computed reimbursement and interim reimbursement is reflected as a receivable from or payable to the third-party program. These programs have audited the year-end cost report filed with the Medicare program through December 31, 2006 with differences reflected as deductions from revenue in 2008. Amounts from unresolved cost reports for 2007 through 2008 are reflected in estimated third-party settlements on the combined balance sheets. The Hospital recognized a reduction to income of approximately \$201,818 in 2008 and an increase to income of \$96,383 in 2007 due to the differences between original estimates and subsequent revisions for the final settlement of cost reports.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Inventory

Inventory is valued at the lower of cost or market with cost being determined on the first-in, first-out (FIFO) method. Inventories at year-end consist of the following:

	<u>2008</u>	<u>2007</u>
Medical supplies and other	\$ 995,166	\$ 1,004,763
Pharmaceutical	380,882	459,352
	<u>\$ 1,376,048</u>	<u>\$ 1,464,115</u>

Assets Whose Use is Limited

Assets whose use is limited are stated at fair market value in the combined financial statements. These assets include investments designated by the Hospital Board for internal purposes, investments restricted by donors for a specific purpose and investments held by trustees for debt service. These investments consist primarily of cash and cash equivalents, certificates of deposit, US government securities, mutual funds and corporate stock. Investment interest, dividends, gains and losses, both realized and unrealized are included in nonoperating revenue (expense) in the combined statements of revenues, expenses and changes in net assets.

Capital Assets and Depreciation

Capital assets such as property and equipment are stated at cost and include expenditures for new additions and other costs added to existing facilities which exceed \$500 and meet certain useful life thresholds. Maintenance, repairs and minor renewals are expensed as incurred. The Hospital provides for depreciation of property and equipment using annual rates, which are sufficient to depreciate the cost of depreciable assets over their estimated useful lives using the straight-line method. The range of useful lives in computing depreciation is as follows:

<u>Description</u>	<u>Range of Useful Lives</u>
Land improvements	15 years
Buildings and improvements	4-50 years
Equipment	5-15 years

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

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 net assets are noncapital net assets that must be used for a particular purpose, as specified by creditors or donors outside the Hospital, including amounts deposited with trustees as required by revenue bond indentures and net assets held by the Foundation. Unrestricted net assets are the remaining net assets that do not meet the definition of net assets invested in capital assets net of related debt or restricted net assets.

Combined Statements of Revenues, Expenses and Changes in Net Assets

The Hospital's combined statement of revenues, expenses and changes in net assets distinguishes between operating and nonoperating revenues and expenses. 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 or incidental transactions such as investment activities are reported as nonoperating gains or losses.

Combined Statements of Cash Flows

For the purposes of the combined statement of cash flows, cash and cash equivalents include demand deposits and investments in highly liquid debt instruments with an original maturity date of three months or less. Cash paid for interest in 2008 and 2007 was \$68,096 and \$97,599, respectively. Capitalized interest for 2008 and 2007 was approximately \$347,000 and \$37,000, respectively.

Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not collect amounts deemed to be charity care, they are not reported as revenue.

Management estimates an allowance for uncollectible patient accounts receivable based on an evaluation of historical losses, current economic conditions, and other factors unique to the Hospital's customer base.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Costs of Borrowing

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Bond Issuance Costs

The Hospital provides for the amortization of costs incurred for the issuance of bonds over the life of the debt. Bond issuance costs are amortized utilizing the straight-line method. Bond issue costs, net of accumulated amortization as of December 31, 2008 and 2007 were \$17,755 and \$36,986, respectively.

Federal or State Income Taxes

The Hospital is a governmental instrumentality organized under Title 16, Article 12, of the Indiana statutes. The Hospital is exempt from federal income tax under Section 115 of the Internal Revenue Code of 1986 as a not-for-profit organization under Section 501(c)(3). Johnson County Health Foundation, Inc. is a 501(c)(3) not-for-profit organization.

Accounting for Uncertainty in Income Taxes

The Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), which clarifies generally acceptable accounting principles for recognition, measurement, presentation and disclosure relating to uncertain tax positions. FIN 48 applies to business enterprises, not-for-profit entities, and pass-through entities, such as S corporations and limited liability companies. As permitted by FIN 48 (as amended), the Hospital elected to defer the application of FIN 48 until issuance of its December 31, 2009 financial statements. For financial statements covering periods prior to calendar 2009, the Hospital evaluates uncertain tax positions in accordance with existing generally accepted accounting principles and makes such accruals and disclosures as might be required there under.

Investments in Affiliates

The Hospital owns 50% of Johnson County Health Network, Inc, a Physician Hospital Organization. The Hospital also owns 47% of JMH Surgical Management Company, which operates and manages the surgery department. During 2007, the Hospital purchased a 20% interest in St. Francis Imaging Center, LLC, which provides multiple diagnostic imaging services on an outpatient basis. The investments are recorded on the equity method of accounting in the Hospital's combined financial statements. The Hospital's investment in affiliated companies is included in the other assets category in the combined balance sheets.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Compensated Absences

Hospital exempt employees earn Paid Time Off (PTO) at the rate of twenty-three days to thirty-two days per year based upon the number of years of service. Hospital non-exempt employees earn PTO at the rate of fourteen days to thirty-two days per year based upon the number of years of service. PTO is awarded and becomes earned on the first day of the pay period following the first six months of employment and then annually thereafter on the first day of the pay period following the employee's anniversary date for PTO accrual. The maximum PTO balance allowed at any given time will be four hundred twenty (420) hours. Unused PTO time, up to forty (40) hours total, in excess of the four hundred and twenty (420) hour maximum may be sold back to the Hospital at the employee's anniversary for PTO renewal. An employee will not be able to sell back more than forty (40) hours, nor will they be allowed to bring their PTO maximum below four hundred twenty hours (420) when selling back PTO hours. PTO hours in excess of four hundred twenty (420) hours that are not sold back to the Hospital will be lost.

During 2008, the Hospital modified the PTO policy. Under the modified policy, any earned PTO hours not taken will be paid to terminated employees with the employee's final paycheck at 50% of earned PTO with a maximum of three hundred (300) hours. A terminated employee loses all rights to PTO hours accrued since the last anniversary date. PTO is accrued and reported as a liability in the combined balance sheets.

Reclassifications

Certain amounts from the 2007 financial statements have been reclassified to conform to the current year presentation.

Litigation

The Hospital is involved in litigation arising in the normal course of business. After consultation with the Hospital's 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.

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 and natural disasters. 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.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

2. EDINBURGH/TRAFALGAR FAMILY HEALTH CENTER, INC.

The Hospital has a note receivable due from Edinburgh/Trafalgar Family Health Center. The note is noninterest bearing, unsecured and due in monthly installments of \$8,000 through 2010. The outstanding amount due on the note as of December 31, 2008 and 2007 was \$215,829 and \$308,971, respectively.

3. NET PATIENT SERVICE REVENUE

The Hospital has agreements with third-party payors that provide for reimbursement to the Hospital at amounts different from its established rates. Estimated contractual adjustments under third-party reimbursement programs represent the difference between the Hospital's billings at standard rates and amounts reimbursed by third-party payors. They also include any differences between estimated third-party reimbursement settlements for prior years and subsequent final settlements. A summary of the reimbursement arrangements with major third-party payors is as follows:

Medicare

Medicare inpatient services are reimbursed based on a predetermined amount for each case based on the diagnosis associated with the patient (Prospective Payment Hospital). These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The prospectively determined rates are not subject to retroactive adjustment.

The Hospital's classification of patients under the Prospective Payment Hospital and the appropriateness of patient admissions are subject to validation reviews by the Medicare peer review organization which is under contract with the Hospital to perform such reviews. Medicare outpatient services are primarily reimbursed on predetermined rates based on the services provided.

Medicaid

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.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

The Hospital is eligible for the Indiana Medicaid Supplemental programs including Medicaid Disproportionate Share Hospital and Municipal Upper Payment Limit programs. The Hospital recognized reimbursement from these programs within net patient revenue of approximately \$4,712,262 and \$2,263,000 during the years ended December 31, 2008 and 2007, respectively. These programs are administered by the State of Indiana, but rely on Federal funding.

Other Payors

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

The following is a summary of net patient service revenue for 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Patient service revenue		
Inpatient	\$ 66,711,279	\$ 57,047,454
Outpatient	92,372,994	83,828,296
Gross patient service revenue	<u>159,084,273</u>	<u>140,875,750</u>
Deductions from revenue		
Contractual allowances	77,171,631	67,091,140
Charity care	2,654,543	1,839,856
Bad debts	6,659,886	5,482,788
Total deductions from revenue	<u>86,486,060</u>	<u>74,413,784</u>
Net patient service revenue	<u>\$ 72,598,213</u>	<u>\$ 66,461,966</u>

4. CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy. The charity care provided during 2008 and 2007 was \$2,654,623 and \$1,839,856, respectively.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

5. ASSETS WHOSE USE IS LIMITED

The classification "Assets whose use is limited" includes:

Internally Designated:

Funded Depreciation – Amounts transferred 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.

Capital Improvement – Amounts designated by the Board of Trustees for capital purchases and improvements.

Board Designated – Amounts designated by the Board of Trustees for other specific purposes.

Funds Held by Trustee for Debt Service – Hospital Association funds deposited with a trustee and limited to use in accordance with the requirements of a trust indenture.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Assets whose use is limited that are required for obligations classified as current liabilities are reported in current assets. The composition of assets whose use is limited includes the following as of December 31:

	2008	2007
Internally designated		
Funded depreciation		
Cash and cash equivalents	\$ 6,739,368	\$ 1,991,197
Investments	1,475,738	2,514,781
Accrued interest receivable	10,496	7,180
Total funded depreciation	8,225,602	4,513,158
Capital improvement		
Cash and cash equivalents	-0-	17,733
Investments	7,007,948	8,707,370
Accrued interest receivable	106,681	160,755
Total capital improvements	7,114,629	8,885,858
Board designation		
Cash and cash equivalents	173,536	538,442
Investments	5,642,715	5,659,316
Accrued interest receivable	44,265	54,119
Total board designated funds	5,860,516	6,251,877
Total internally designated	21,200,747	19,650,893
Held by trustee for debt service		
Cash and cash equivalents	673,643	870,630
Total assets limited as to use	\$ 21,874,390	\$ 20,521,523

Investments include certificates of deposit, mutual funds, marketable equity securities and U.S. government obligations.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

6. DEPOSITS AND INVESTMENTS

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 Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

Investments are carried at fair market value. Net realized gains and losses on security transactions are determined on the specific identification cost basis. Funded depreciation investments consist of cash equivalents and U.S. Government securities. Market value approximated cost as of December 31, 2008 and 2007.

The Hospital's investments generally are reported at fair value, as discussed in Note 1. As of December 31, 2008 and 2007, the Hospital had the following investments and maturities, all of which were held in the Hospital's name by custodial banks that are agents of the Hospital:

December 31, 2008					
Carrying Amount	Investment Maturities (in years)				
	Less than 1	1-5	6-10	More than 10	
US Government Securities	\$ 4,878,156	\$ 3,941,793	\$ 936,363	\$ -0-	\$ -0-
Certificates of deposit	25,267,823	25,267,823	-0-	-0-	-0-
Mutual funds - equities	2,656,460	2,656,460	-0-	-0-	-0-
Donated corporate stock	554,119	554,119	-0-	-0-	-0-
	\$ 33,356,558	\$ 32,420,195	\$ 936,363	\$ -0-	\$ -0-

December 31, 2007					
Carrying Amount	Investment Maturities (in years)				
	Less than 1	1-5	6-10	More than 10	
US Government Securities	\$ 4,647,877	\$ 3,112,947	\$ 1,534,930	\$ -0-	\$ -0-
Certificates of deposit	21,615,679	21,615,679	-0-	-0-	-0-
Mutual funds - equities	4,528,151	4,528,151	-0-	-0-	-0-
Donated corporate stock	821,710	821,710	-0-	-0-	-0-
	\$ 31,613,417	\$ 30,078,487	\$ 1,534,930	\$ -0-	\$ -0-

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Interest rate risk - The Hospital does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates.

Credit risk - Statutes authorize the Hospital to invest in interest bearing deposit accounts, passbook savings accounts, certificates of deposit, money market 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.

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.

Deposits and investments consist of the following as of December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Carrying amount		
Deposits	\$ 2,849,804	\$ 3,117,883
Investments	33,356,558	31,613,417
	<u>\$ 36,206,362</u>	<u>\$ 34,731,300</u>
Included in the balance sheet captions		
Cash and cash equivalents	\$ 2,849,804	\$ 3,117,883
Investments	11,482,168	11,091,894
Internally designated	21,200,747	19,650,893
Held by trustee for debt service	673,643	870,630
	<u>\$ 36,206,362</u>	<u>\$ 34,731,300</u>

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

7. 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 other observable inputs.

The Hospital partially adopted the provisions of FAS 157 for 2008, but will delay adoption of non-financial assets and non-financial 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 non-financial assets and non-financial 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 non-financial 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 and corporate equity securities.

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 corporate and municipal bonds that trade infrequently and privately held securities and certificates of deposit.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

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. These investments could be certain private equity investments.

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

	Total	Fair value measurements at reporting date using		
		Quoted market prices for identical assets Level 1	Significant other observable inputs Level 2	Significant unobservable inputs Level 3
Investments				
US Government Securities	\$ 4,878,156	\$ -0-	\$ 4,878,156	\$ -0-
Certificates of deposit	25,267,823	-0-	25,267,823	-0-
Mutual funds - equities	2,656,460	2,656,460	-0-	-0-
Corporate stock	554,119	554,119	-0-	-0-
Totals	<u>\$ 33,356,558</u>	<u>\$ 3,210,579</u>	<u>\$ 30,145,979</u>	<u>\$ -0-</u>

8. RESTRICTED NET ASSETS

Restricted net assets are categorized as follows as of December 31, 2008 and 2007:

	2008	2007
Held by trustee for debt service	\$ 673,643	\$ 870,630
Cumulative building fund - funded depreciation	4,936,219	4,736,111
Other specific purpose - gift fund	924,297	1,515,768
Primary government	6,534,159	7,122,509
Johnson County Health Foundation	1,168,710	1,795,570
Total restricted funds	<u>\$ 7,702,869</u>	<u>\$ 8,918,079</u>

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

9. CAPITAL ASSETS

Capital Assets

A summary of capital assets, including assets under capital leases, as of December 31, 2008 and 2007, follows:

	December 31, 2007	Additions	Retirements	Transfers	December 31, 2008
Land	\$ 3,141,963	\$ -0-	\$ -0-	\$ -0-	\$ 3,141,963
Land improvements	1,195,952	7,283	-0-	8,199	1,211,434
Buildings and improvements	49,917,555	17,911	-0-	906,837	50,842,303
Equipment	37,277,886	1,223,749	(3,139,712)	2,103,309	37,465,232
Construction in progress	6,106,691	3,249,449	-0-	(3,018,345)	6,337,795
Total capital assets	<u>97,640,047</u>	<u>4,498,392</u>	<u>(3,139,712)</u>	<u>-0-</u>	<u>98,998,727</u>
Less accumulated depreciation:					
Land improvements	(926,015)	(44,864)	-0-	-0-	(970,879)
Buildings and improvements	(26,567,406)	(1,665,852)	-0-	-0-	(28,233,258)
Equipment	(28,508,117)	(3,070,600)	3,056,278	-0-	(28,522,439)
Total accumulated depreciation	<u>(56,001,538)</u>	<u>(4,781,316)</u>	<u>3,056,278</u>	<u>-0-</u>	<u>(57,726,576)</u>
Capital assets, net	<u>\$ 41,638,509</u>	<u>\$ (282,924)</u>	<u>\$ (83,434)</u>	<u>\$ -0-</u>	<u>\$ 41,272,151</u>

	December 31, 2006	Additions	Retirements	Transfers	December 31, 2007
Land	\$ 3,141,963	\$ -0-	\$ -0-	\$ -0-	\$ 3,141,963
Land improvements	1,193,752	-0-	-0-	2,200	1,195,952
Buildings and improvements	49,788,627	77,823	-0-	51,105	49,917,555
Equipment	36,827,227	861,559	(1,272,662)	861,762	37,277,886
Construction in progress	1,113,965	5,907,793	-0-	(915,067)	6,106,691
Total capital assets	<u>90,220,537</u>	<u>6,847,175</u>	<u>(1,272,662)</u>	<u>-0-</u>	<u>97,640,047</u>
Less accumulated depreciation:					
Land improvements	(879,691)	(46,324)	-0-	-0-	(926,015)
Buildings and improvements	(24,849,795)	(1,717,611)	-0-	-0-	(26,567,406)
Equipment	(26,745,209)	(2,947,227)	1,184,319	-0-	(28,508,117)
Total accumulated depreciation	<u>(49,016,597)</u>	<u>(4,711,162)</u>	<u>1,184,319</u>	<u>-0-</u>	<u>(56,001,538)</u>
Capital assets, net	<u>\$ 41,203,940</u>	<u>\$ 2,136,013</u>	<u>\$ (2,456,981)</u>	<u>\$ -0-</u>	<u>\$ 41,638,509</u>

Depreciation expense for 2008 and 2007 amounted to \$4,781,316 and \$4,711,162, respectively.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Assets Under Capital Lease

The assets acquired through capital leases still in effect are as follows:

	<u>2008</u>	<u>2007</u>
Equipment	\$ 252,971	\$ 213,889
Less accumulated depreciation	<u>90,850</u>	<u>7,309</u>
	<u>\$ 162,121</u>	<u>\$ 206,580</u>

10. INVESTMENT IN AFFILIATED COMPANIES

The Hospital owns 50% of Johnson County Health Network, Inc., a Physician Hospital Organization. Additionally, the Hospital owns 47% of JMH Surgical Management Company, which operates and manages the surgery department. The investments are recorded on the equity method of accounting in the Hospital's combined financial statements.

The Hospital owns a 20% interest (20 units) in St. Francis Imaging Center, LLC, which provides multiple diagnostic imaging services on an outpatient basis. This investment is recorded on the cost method.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Summarized financial information as of December 31, 2008 and 2007 and the years then ended from the unaudited financial statements of Johnson County Health Network and JMH Surgical Management Company follows:

	Johnson County Health Network		JMH Surgical Management Company	
	2008	2007	2008	2007
Cash and cash equivalents	\$ 72,152	\$ 84,775	\$ 381,511	\$ 395,772
Due from Hospital	87,046	79,071	210,307	92,685
Other assets	-0-	-0-	-0-	-0-
Total assets	<u>\$ 159,198</u>	<u>\$ 163,846</u>	<u>\$ 591,818</u>	<u>\$ 488,457</u>
Liabilities	\$ 49,381	\$ 50,249	\$ 208,818	\$ 102,957
Equity	<u>109,818</u>	<u>113,597</u>	<u>383,000</u>	<u>385,500</u>
Total liabilities and equity	<u>\$ 159,199</u>	<u>\$ 163,846</u>	<u>\$ 591,818</u>	<u>\$ 488,457</u>
Operating revenue	\$ 26,471	\$ 28,420	\$ 389,000	\$ 266,000
Nonoperating revenue	-0-	-0-	7,522	10,396
Other expenses	(30,250)	(32,829)	(151,585)	(134,888)
Net income	<u>\$ (3,779)</u>	<u>\$ (4,409)</u>	<u>\$ 244,937</u>	<u>\$ 141,508</u>
Dividends Paid	\$ -0-	\$ -0-	\$ 247,437	\$ 141,508

11. LONG TERM DEBT

A summary of long term debt as of December 31, 2008 and 2007 is as follows:

- The \$2,200,000, 1998 Variable Rate Demand Revenue Bonds were paid off during 2008.
- The \$6,000,000, 2000 Variable Rate Demand Revenue Bonds are due in installments of \$600,000 to \$700,000, plus variable interest (3.6% at December 31, 2008) through January 1, 2010. Secured by a letter of credit of approximately \$2,139,000 expiring January 16, 2010.
- During the year, the Hospital prepaid its 2007 85A Pool Loan Program debt due to the uncertainties in the market for insured bond issues. In turn, a commercial bank loan was taken out in the amount of \$4,500,000. The purpose of this funding was to finance a major portion of the private room bed renovation project that began in 2007. Interest on the commercial bank loan is fixed at 4.75% and is payable in monthly principal and interest payments of \$63,225 due on May 28, 2015 and is collateralized by patient accounts receivable 90 days or less.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

- The Hospital has two capital lease obligations. The first has imputed interest of 6.5% and is payable in monthly principal and interest payments of \$9,224. The second has imputed interest of 9.44% and is payable in monthly principal and interest payments of \$1,023.

The bonds require the Hospital to maintain certain financial debt coverage ratios. As of December 31, 2008 and 2007, the Hospital believes it was in compliance with the debt coverage ratios.

The following represents a progression for long term debt for 2008 and 2007:

	December 31, 2007	Additional Borrowings	Payments	December 31, 2008	Current Portion
Other long term debt					
Indiana Health Facility Financing Authority (IHFFA):					
\$2,200,000 1998 Demand Bonds	\$ 300,000	\$ -0-	\$ (300,000)	\$ -0-	\$ -0-
\$6,000,000 2000 Demand Bonds	2,100,000	-0-	(700,000)	1,400,000	700,000
\$6,000,000 1985A Pool Borrowing	2,744,249	-0-	(2,744,249)	-0-	-0-
Commercial bank loan	-0-	4,500,000	(327,854)	4,172,146	570,270
Capital lease obligations	<u>257,648</u>	<u>31,963</u>	<u>(66,044)</u>	<u>223,567</u>	<u>73,990</u>
Total long term debt	<u>\$ 5,401,897</u>	<u>\$ 4,531,963</u>	<u>\$ (4,138,147)</u>	<u>\$ 5,795,713</u>	<u>\$ 1,344,260</u>

	December 31, 2006	Additional Borrowings	Payments	December 31, 2007	Current Portion
Other long term debt					
Indiana Health Facility Financing Authority (IHFFA):					
\$2,200,000 1998 Demand Bonds	\$ 600,000	\$ -0-	\$ (300,000)	\$ 300,000	\$ 300,000
\$6,000,000 2000 Demand Bonds	2,700,000	-0-	(600,000)	2,100,000	700,000
\$6,000,000 1985A Pool Borrowing	-0-	2,744,249	-0-	2,744,249	48,750
Capital lease obligations	<u>124,164</u>	<u>257,648</u>	<u>(124,164)</u>	<u>257,648</u>	<u>59,698</u>
Total long term debt	<u>\$ 3,424,164</u>	<u>\$ 3,001,897</u>	<u>\$ (1,024,164)</u>	<u>\$ 5,401,897</u>	<u>\$ 1,108,448</u>

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Scheduled principal and interest repayments on long term debt and payments on capital lease obligations for the years ending after December 31, 2008 are as follows:

<u>Years Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	\$ 1,344,260	\$ 251,806	\$ 1,596,066
2010	1,377,624	193,242	1,570,866
2011	698,110	133,148	831,258
2012	658,721	99,979	758,700
2013	691,154	67,546	758,700
Thereafter	1,025,844	37,041	1,062,885
	<u>\$ 5,795,713</u>	<u>\$ 782,762</u>	<u>\$ 6,578,475</u>

12. PENSION PLAN

Plan Termination

During 2007, the Hospital elected to terminate the defined benefit plan effective December 31, 2007 and replace it with a defined contribution plan effective January 1, 2008. The estimated plan assets were transferred to a trust account at Allegiant Asset Management Company to protect the assets from the economic downturn. At December 31, 2008, the defined benefit plan assets consisted of mainly cash and had a value of approximately \$25,000,000. The plan will distribute the assets to the participants based on participant elections of lump sum payouts or annuities. The Hospital will be required to fund any shortage between plan assets and expected liquidation distributions and has recorded an estimated liability of approximately \$700,000 as of December 31, 2008.

During 2008, the Hospital established a defined contribution plan. Eligibility rules for the defined contribution include 1,000 hours worked in a service year, completion of two service years and no minimum age requirement. The Hospital may elect to make a discretionary contribution on behalf of eligible employees. The plan does allow employee deferral contributions. The Hospital matches 50% of the employee deferrals up to 3% of eligible compensation. Hospital discretionary and matching contributions to the plan are vested at 20% after 2 vesting years of service and increasing 20% every vesting year up until reaching 100% after completing 6 vesting years. For 2008, the Hospital recognized approximately \$990,000 in pension expense into the defined contribution plan.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

13. RENTAL EXPENSE

Leases that do not meet the criteria for capitalization are classified as operating leases with related rentals charged to operating as incurred. Total rent expense for 2008 and 2007 was \$1,817,669 and \$1,635,239, respectively.

14. CONCENTRATIONS OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third party payors at December 31, 2008 and 2007 was as follows:

	<u>2008</u>	<u>2007</u>
Medicare	35%	36%
Medicaid	11%	8%
Blue Cross	9%	9%
Other third party payors	13%	18%
Self-pay	32%	29%
	<u>100%</u>	<u>100%</u>

15. BLENDED COMPONENT UNIT

The accompanying combined financial statements of the primary government include the blended component unit accounts of Johnson County Health Foundation, Inc. (Foundation), a separate not-for-profit entity organized to support the operations of the Hospital.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

The following is a financial summary of the Foundation as of and for the years ended December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Total assets - primarily investments	\$ 1,170,089	\$ 1,795,873
Liabilities	\$ 1,379	\$ 303
Unrestricted net assets	653,705	1,149,168
Restricted net assets	515,005	646,402
Total net assets	<u>1,168,710</u>	<u>1,795,570</u>
Total liabilities and net assets	<u>\$ 1,170,089</u>	<u>\$ 1,795,873</u>
Operating revenue	\$ 3,629	\$ 3,529
Nonoperating revenue (expense)	(382,970)	124,219
Other expenses	(247,519)	(70,042)
Change in net assets	<u>(626,860)</u>	<u>57,706</u>
Beginning net assets	1,795,570	1,737,864
Ending net assets	<u>\$ 1,168,710</u>	<u>\$ 1,795,570</u>

16. RISK MANAGEMENT

Medical Benefits to Employees and Dependents

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 General Fund, where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of \$300,000 per year. Settled claims resulting from this risk did not exceed commercial insurance coverage in the past three years. Provisions are also made for unexpected and unusual claims.

JOHNSON MEMORIAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

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. These amounts are reported in accounts payable and accrued expense under current liabilities on the combined balance sheets.

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

	<u>2008</u>	<u>2007</u>
Unpaid claims, beginning of year	\$ 624,000	\$ 568,000
Incurred claims and changes in estimates	3,994,560	3,726,334
Claim payments	<u>(3,753,560)</u>	<u>(3,670,334)</u>
Unpaid claims, end of year	<u>\$ 865,000</u>	<u>\$ 624,000</u>