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

AUDIT REPORT
OF

DAVIESS COMMUNITY HOSPITAL
A COMPONENT UNIT OF
DAVIESS COUNTY, INDIANA

January 1, 2007 to December 31, 2007

FILED
08/26/2008

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HOSPITAL OFFICIALS

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

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), as of and for the year ended December 31, 2007, 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 as of December 31, 2007, 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 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 5, 2008

Daviess Community Hospital

Management's Discussion and Analysis

Our discussion and analysis of Daviess Community Hospital's (the Hospital) financial performance provides an overview of the Hospital's financial statements for the fiscal year ended December 31, 2007. 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, 2007 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 increased by $0.4 million or 1% as a result of this year's operations.
- The Hospital's net operating revenues of $44.6 million decreased by $2.7 million or 6% from prior year. The discontinuation of ER professional fee billing, due to an ER physician contract change, resulted in a $1.1 million reduction in net operating revenue. Higher contractual adjustments led to a $1.6 million decline in net operating revenue.
- The Hospital's operating expenses of $45.2 million decreased by $1.2 million or 3% from the prior year. This decrease was primarily related to a new ER physician group contract. The hospital had previously paid an hourly rate and billed all professional fees. This change reduced professional fees by approximately $1.1 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 2007 and Prior Year 2006. Related notes follow the financial reports.

NET ASSETS		
	2007	2006
Current Assets	$14.6	$16.8
Noncurrent Assets	11.4	10.5
Capital Assets	33.6	34.1
Total Assets	59.6	61.4
Current Liabilities	4.5	4.4
Long-Term Debt	19.6	21.9
Total Liabilities	24.1	26.3
Net Assets		
Invested in Capital Assets	12.5	10.8
Restricted	2.0	2.4
Unrestricted	21.0	21.9
Total Net Assets	$35.5	$35.1

Current Assets of $14.6 million decreased $2.2 million or 13% from the prior year. Gross patient receivables declined $1.1 million and $2.0 million of capital equipment was purchased.

Long-Term Debt of $19.6 million decreased $2.3 million or 11% from the prior year.

CHANGES IN NET ASSETS		
	2007	2006
Revenue		
Net Patient Service Revenue	$43.9	$46.5
Other Revenues	0.7	0.8
Total Revenues	44.6	47.3
Expenses		
Salaries and Benefits	24.0	23.7
Medical Supplies and Drugs	3.9	4.4
Insurance	0.6	0.6
Other Supplies	1.2	1.2
Depreciation and Amortization	2.9	3.2
Other Expenses	12.6	13.3
Total Expenses	45.2	46.4
Operating Income (Loss)	-0.6	0.9
Nonoperating Revenues (Expenses)	1.0	0.8
Increase (Decrease) In Net Assets	0.4	1.7
Net Assets Beginning of the Year	35.1	33.4
Net Assets End of the Year	$35.5	$35.1

The Hospital reported a $0.4 million increase in net assets for Calendar Year 2007. 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 2007 are:

- The Hospital's net operating revenues of $44.6 million decreased by $2.7 million or 6% from prior year. Inpatient service revenue increased 1%, outpatient revenue decreased 6%, and physician clinic revenue increased 8%. The change in outpatient revenue was most affected by the discontinuation of billing for ER professional fees, which led to a $1.1 million decline in net operating revenue. Under a new contractual agreement the ER physician group bills for the professional fees instead of the hospital billing for them. Revenue deductions increased from 42.0% in 2006 to 44.0% in 2007 resulting in $1.6 million less net operating revenue.
- The Hospital's operating expenses of $45.2 million decreased by $1.2 million or 3% from prior year. Expense for ER physician fees declined by $1.1 million.

Capital Assets and Debt Administration

Capital Assets

At the end of 2007, the Hospital had $33.6 million invested in capital assets. The Hospital had a net decrease of $0.5 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, 2007.

Capital Assets at Year-End Net of Depreciation		
	2007	2006
Land	$1.2	$1.2
Land Improvements/Leasehold Improvements	0.7	0.7
Building	36.2	35.6
Equipment	21.6	20.5
Total	59.7	58.0
Less Accumulated Depreciation	26.7	24.2
Subtotal	33.0	33.8
Construction In Progress	0.6	0.3
Capital Assets (Net)	$33.6	$34.1

Debt

At year-end, the Hospital had approximately $22.5 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		
	2007	2006
Variable Rate Hospital Revenue Bonds		
2001 Revenue Bonds	$3.0	$3.8
Indiana Health Facility Financing Authority (IHFFA)		
1998/1999 Revenue Bonds	0.2	0.0
2006 Revenue Bond (Refunded 1998 and 1999 series)	18.4	19.2
PACS Capital Lease	0.9	1.1
Total Debt	$22.5	$24.1

Economic Factors

Although bad debt expense declined $0.5 million in 2007 it is expected to increase in future years due to higher deductible insurance plans.

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, 2007

Assets	
Current assets:	
Cash and cash equivalents	$ 2,642,067
Patient accounts receivable, net of estimated uncollectibles of $4,428,300	7,363,359
Supplies and other current assets	3,694,839
Noncurrent cash and investments:	
Internally designated	9,324,178
Held by trustee for debt service	2,029,019
Capital assets:	
Land and construction in progress	1,748,704
Depreciable capital assets, net of accumulated depreciation	31,823,246
Other assets	948,374
Total assets	$ 59,573,786
Liabilities and Net Assets	
Current liabilities:	
Current maturities of long-term debt	$ 1,547,536
Accounts payable and accrued expenses	2,026,823
Other current liabilities	929,088
Long-term debt, net of current maturities	19,575,728
Total liabilities	24,079,175
Net assets:	
Invested in capital assets, net of related debt	12,448,686
Restricted:	
For debt service	2,029,019
Unrestricted	21,016,906
Total net assets	35,494,611
Total liabilities and net assets	$ 59,573,786

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, 2007

Operating revenues:	
Net patient service revenue (net of provision for bad debt)	$ 43,936,092
Other	637,665
Total operating revenues	44,573,757
Operating expenses:	
Salaries and benefits	23,966,102
Medical supplies and drugs	3,944,372
Insurance	552,250
Other supplies	1,160,578
Other expenses	12,647,451
Depreciation and amortization	2,892,151
Total operating expenses	45,162,904
Operating loss	(589,147)
Nonoperating revenues:	
Investment income	753,544
Gain on sale of equipment	16,292
Other	229,232
Total nonoperating revenues	999,068
Increase in net assets	409,921
Net assets beginning of the year	35,084,690
Net assets end of the year	$ 35,494,611

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, 2007

	2007
Cash flows from operating activities:	
Receipts from and on behalf of patients	$ 44,434,380
Payments to suppliers and contractors	(5,330,726)
Payments to employees	(23,966,102)
Other receipts and payments, net	(10,687,635)
Net cash provided by operating activities	4,449,917
Cash flows from capital and related financing activities:	
Principal paid on long-term debt	(1,832,584)
Interest paid on long-term debt	(1,361,884)
Purchase of capital assets	(2,312,354)
Net cash used by capital and related financing activities	(5,506,822)
Cash flows from investing activities:	
Interest and dividends on investments	753,544
Purchase of investments	(2,393,000)
Net cash used by investing activities	(1,639,456)
Net decrease in cash and cash equivalents	(2,696,361)
Cash and cash equivalents at beginning of year	9,498,625
Cash and cash equivalents at end of year	$ 6,802,264
Reconciliation of cash and cash equivalents to the Statement of Net Assets:	
Cash and cash equivalents in current assets	$ 2,642,067
Restricted cash and cash equivalents	4,160,197
Total cash and cash equivalents	$ 6,802,264
Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	$ (589,147)
Adjustments to reconcile operating loss to net cash flows used in operating activities:	
Depreciation and amortization	2,892,151
Provision for bad debts	2,794,918
Nonoperating revenue	229,232
Gain on sale of equipment	16,292
(Increase) decrease in current assets:	
Patient accounts receivable	(2,296,630)
Estimated third-party payor settlements	232,105
Supplies and other current assets	260,683
Other assets	(17,313)
Increase in current liabilities:	
Accounts payable and accrued expenses	65,791
Other current liabilities	861,835
Net cash provided in operating activities	$ 4,449,917

The accompanying notes are an integral part of the 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 outpatient 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.

Blended Component Units

The Health Services Development 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.

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 nonoperating 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.

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 520 hours.

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

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	$ 6,751,404
Receivable from Medicare	3,701,311
Receivable from Medicaid	1,338,944
Total patient accounts receivable	11,791,659
Less allowance for uncollectible amounts	4,428,300
Patient accounts receivable, net	$ 7,363,359

Accounts Payable and Accrued Expenses	
Payable to employees (including payroll taxes)	$ 1,156,510
Payable to suppliers	870,313
Total accounts payable and accrued expenses	$ 2,026,823

C. Capital Assets

Capital asset activity for the year ended December 31, 2007, was as follows:

Primary Government	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	$ 1,170,484	$ -	$ -	$ 1,170,484
Construction in progress	265,993	805,631	493,404	578,220
Total capital assets, not being depreciated	1,436,477	805,631	493,404	1,748,704

Primary Government	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, being depreciated:				
Land improvements	729,739	7,106	-	736,845
Buildings and improvements	35,612,014	626,162	87,505	36,150,671
Equipment	20,516,560	1,430,493	317,841	21,629,212
Totals	56,858,313	2,063,761	405,346	58,516,728
Less accumulated depreciation for:				
Land improvements	353,395	12,847	-	366,242
Buildings and improvements	9,420,265	982,744	54,146	10,348,863
Equipment	14,446,056	1,819,887	287,566	15,978,377
Totals	24,219,716	2,815,478	341,712	26,693,482
Total capital assets, being depreciated, net	32,638,597	(751,717)	63,634	31,823,246
Total primary government capital assets, net	$34,075,074	$ 53,914	$ 557,038	$33,571,950

D. Construction Commitments

Construction work in progress is composed of the following:

Project	Total Project Authorized	Expended to December 31, 2007	Required Future Funding
General constuction	$ 87,661	$ 87,661	$ -
Behavorial health remodling	322,774	94,162	228,612
Urgent care center	1,500,000	396,397	1,103,603
Totals	$ 1,910,435	$ 578,220	$ 1,332,215

E. Capital Lease

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, 2007, are as follows:

2008	$ 258,409
2009	258,409
2010	258,409
2011	193,807
Total minimum lease payments	969,034
Less amount representing interest	80,368
Present value of net minimum lease payments	$ 888,666

Assets acquired through the capital lease still in effect are as follows:

Equipment	$ 1,152,251
Accumulated depreciation	326,471
Total	$ 825,780

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	$ 195,000
2001 Variable rate revenue bonds for hospital constuction	Variable	3,021,120.00
2006 Refunding revenue bonds for hospital improvements	Variable	18,350,000
Total		$ 21,566,120

Revenue bonds debt service requirements to maturity are as follows:

Year Ended December 31	Principal	Interest
2008	$ 1,325,280	$ 957,134
2009	1,460,280	897,800
2010	1,385,280	834,699
2011	1,410,280	770,449
2012	680,000	720,973
2013-2017	3,815,000	3,102,077
2018-2022	4,625,000	2,136,250
2023-2027	5,610,000	964,563
2028-2032	1,255,000	31,270
Totals	$ 21,566,120	$ 10,415,215

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, 2007, were considered defeased:

	Amount
Hospital	$ 16,095,000

3. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2007, was as follows:

Primary Government	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable:					
Revenue:					
Hospital association	$ 3,776,400	$ -	$ 755,280	$ 3,021,120	$ 755,280
Indiana health facility financing authority	-	195,000	-	195,000	95,000
Other revenue bonds	19,215,000		865,000	18,350,000	475,000
Less deferred amount on refunding	788,211	581,000	37,689	1,331,522	-
Total bonds payable	22,203,189	(386,000)	1,582,591	20,234,598	1,325,280
Capital leases	1,100,970	-	212,304	888,666	222,256
Total long-term liabilities	$ 23,304,159	$ (386,000)	$ 1,794,895	$ 21,123,264	$ 1,547,536

4. Net Revenue Available for Debt Service

The following disclosures concerning net revenue available for debt service applicable to the years ended December 31, 2007, are required by terms of the financing agreement between the Hospital and IHFFA:

Revenue from operations	$ 44,573,757
Investment income	753,544
Less:	
Expenses (excluding depreciation, amortization and interest on funded debt)	41,287,923
Total net revenue available for debt service	$ 4,039,378
Funded debt service for year	$ 2,547,939
Historical debt service coverage ratio	2:1

G. Charity Care

Charges excluded from revenue under the Hospital's charity care policy were $443,404 for 2007.

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 Indiana Code 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.

Internally designated:	
Funded depreciation:	
Cash and cash equivalents	$ 1,934,532
Investments	6,543,000
Total funded depreciation	8,477,532

Internally designated (continued):	
Capital improvement:	
Cash and cash equivalents	37,513
Investments	100,000
Total capital improvement	137,513
Board designation:	
Cash and cash equivalents	159,133
Investments	550,000
Total board designation	709,133
Total internally designated	$ 9,324,178

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.

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

	2007	2006
Unpaid claims, beginning of fiscal year	$ 156,831	$ 254,147
Incurred claims and changes in estimates	2,209,672	2,122,129
Claim payments	(2,226,258)	(2,219,445)
Unpaid claims, end of fiscal year	$ 140,245	$ 156,831

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-F the Hospital provides postemployment health insurance benefits, as authorized by Indiana Code 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, three 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, 2007, expenditures of $4,340 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.

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.

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. 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 2007, net patient service revenues in the accompanying statements of operations were decreased by $232,105, to reflect changes in the estimated settlements for certain prior years.

F. Pension Plan

Daviess Community Hospital Money Purchase Plan

Plan Description

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

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.

G. Internal Investigation of Ghost Employment

Three employees, including a manager, were found to have falsified payroll records dating back to April 2006. Approximately 886 hours were falsely recorded as worked. This amounted to approximately $25,000 paid to these individuals for work not performed. The employees were terminated in November 2007, and the three were reported to the State Licensing Board. The investigation was turned over to the Daviess County Prosecutor and charges were filed against the three in March 2008.

DAVIESS COMMUNITY HOSPITAL
EXIT CONFERENCE

The contents of this report were discussed on August 5, 2008, with Brad Hardcastle, Chief Financial Officer; Kenneth Parsons, Chairman of the Hospital Board; Ann Perkins, Controller; and Anthony R. Showalter, Chairman of the Finance Committee. Our audit disclosed no material items that warrant comment at this time.