

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

AUDIT REPORT  
OF

PERRY COUNTY MEMORIAL HOSPITAL  
A COMPONENT UNIT OF  
PERRY COUNTY, INDIANA

January 1, 2006 to December 31, 2006



**FILED**  
05/02/2007



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HOSPITAL OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Executive Director	Joseph Stuber	01-01-06 to 12-31-07
Treasurer	Kathy Clayton	01-01-06 to 12-31-07
Chairman of the Hospital Board	John B. Land	01-01-06 to 12-31-07
President of the Board of County Commissioners	Terry Lock Louis Fortwendel	01-01-06 to 12-31-06 01-01-07 to 12-31-07



**STATE OF INDIANA**  
AN EQUAL OPPORTUNITY EMPLOYER

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INDEPENDENT AUDITOR'S REPORT

TO: THE OFFICIALS OF THE PERRY COUNTY MEMORIAL HOSPITAL, PERRY COUNTY, INDIANA

We have audited the accompanying basic financial statements of Perry County Memorial Hospital (Hospital), as of and for the year ended December 31, 2006, 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 financial position of the Hospital as of December 31, 2006, and the changes in financial position and cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States.

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

STATE BOARD OF ACCOUNTS

April 9, 2007

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## Management's Discussion and Analysis Perry County Memorial Hospital

Our discussion and analysis of Perry County Memorial Hospital's (PCMH) financial performance provides an overview of PCMH's financial activities for the fiscal year ended December 31, 2006. Please read it in conjunction with PCMH's financial statements and accompanying notes to the financial statements.

### Using This Annual Report

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

In the "Management Discussion and Analysis" section of this report the management of the hospital discuss various components of the annual report and provide an analysis of the current financial statement information.

The "Basic Financial Statement" section of this report includes a series of financial statements that provide information about the activities of PCMH as a whole. The Statement of Net Assets reveals the assets and liabilities of PCMH on December 31, 2006 while the Statement of Revenues, Expenses, and Changes in Net Assets summarizes the changes in the assets and liabilities for the year then ended. The Statement of Cash Flows summarizes 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

With increased volumes and improved Net Patient Revenues, fiscal year 2006 was a good year for Perry County Memorial Hospital (PCMH). The following report represents improvements in hospital operations as follows:

- Acute Care Discharges increased slightly
- Net Patient Revenue increased 4.4%
- Total Margin was 6.09%
- PCMH invested \$2,909,531 for Capital Equipment and Improvements in 2006
- Maximum Annual Debt Service coverage remains strong 4.54.
- Cash Not Restricted for Debt Service of \$11,762,191 is strong at 211 days cash on hand.
- During the year, PCMH made the following significant Capital Expenditures:

Conveniently located in the center of your life.

- Troy Clinic (\$221,195)
- Perry County Clinic (\$871,000)
- PACS System (\$114,545)
- Fuji Computed Radiography System (\$131,544)
- Land Purchase Hwy 37 (\$600,000)
- Vitek 2 Com-Analyzer (\$56,592)
- Park Avenue House (\$44,264)
- Sleep Lab Renovation (\$91,656)
- OB Renovation (\$92,293)
- Video Gastroscope (\$22,413)
- Mobile C-Arm Surgery (\$72,030)
- Blood Culture Analyzer (\$25,598)

Utilization

Total Inpatient Services had slightly decreased volumes with Swing Bed volumes decreasing by 28%. Acute Care Discharges were equivalent to 2005 with an equivalent Average Length of Stay at 3.2 days and Acute Care census was equivalent to 2005.

Imaging Procedures increased 6%; Lab tests increased 15%; Emergency Room increased 3% and EMS volumes increased 7%. PCMH's Home Health Agency saw a 12% increase in visits during the year. Other services such as Surgery, Respiratory Therapy, and Outpatient Visits had slight decreases during the year.

Sources of Revenue

PCMH receives a significant portion of its revenues from government health programs, principally Medicare and Medicaid, which are highly regulated and subject to frequent and substantial changes. Revenues from the Medicare and Medicaid programs decreased to 60.0% of gross revenues in 2006 from 62.3% in 2005.

	<u>2006</u>	<u>2005</u>
Medicare	46.5%	48.6%
Medicaid	13.5%	13.7%
Commercial	34.2%	33.1%
Private	5.8%	4.6%

Legislative changes continue to limit or reduce the levels of payments from these programs. The Hospital elected to be designated as a Critical Access Hospital effective July 1, 2004. Under this designation Medicare Services have been reimbursed at 101% of reasonable costs. The new Indiana Medicaid Managed Care program has also had an impact on reimbursement and contractual allowance.

### Operating Results

PCMH's Financial Operations resulted in a 3.11% Operating Margin of \$821,687. This was \$788,393 decrease from prior year of \$1,610,080. This was related to a continued effort to remain competitive in the market and a change to a three tiered charity policy. PCMH's Total Margin was \$1,607,814 or 6.09% and Investment Earnings of \$866,249 were \$406,451 over prior year of \$459,798. This includes the Foundation Endowment and Memorial Fund Earnings.

Operating Expenses of \$25.6 million increased \$2.5 million or 10.8% from prior year. Salaries and Benefits increased \$1,406,675, which was related to adjustments to compensation levels resulting from a Mercer wage survey performed in 2005 and annual merit increases. Medical Fees increased \$268,588 for an increase in Physician services provided under arrangement. A new Cardiologist began seeing patients on a seven day a week schedule. Supply costs increased \$317,011 and Other Expenses increased \$407,788.

### Balance Sheet

Hospital Operating Cash and Investments increased \$466,658 during the year. This was due to a continued increase in our collection efforts. Non-current Cash and Investments increased \$1,056,723 with the addition of PCMH's Foundation and improved earnings in the Equity Markets.

Accounts Receivable Days increased 63.5 days compared to prior year of 53.3.

Long Term Debt to Capitalization Ratio is extremely favorable at 12.21% compared to the S&P-BBB of 40.70%. This reflects PCMH's strong Balance Sheet.

Cash Flows to Liabilities percentage experience a slight change in 2006 to 47.32% compared to prior year of 47.90%. This is very favorable when compared to the S&P-BBB of 14.10%.

Unrestricted Cash to Long Term Debt Ratio remains extremely favorable as Cash and Investments exceed Long-Term Debt Ratio is 298.35% (S&P-BBB 80.40%).

### Capital Assets

At the end of 2006 PCMH had approximately \$11,310,492 invested in Capital Assets. This represents a net increase of \$380,961 that consists of \$2,909,531 in new Capital Purchases; Less: Assets retired for disposal or trade -in, \$62,620, an increase in Depreciation Expense to \$1,335,700, and the reduction of CIP in the amount of \$1,053,112. Capital Assets consist of:

	<u>2006</u>	<u>2005</u>
Land	\$1,828,347	\$1,030,592
Land Improvements	\$1,328,965	\$1,187,046
Buildings	\$10,005,450	\$8,679,434
Equipment	\$12,278,368	\$11,832,775
<b>Total</b>	<b>\$25,441,130</b>	<b>\$22,729,847</b>
Less: Accumulated		
Depreciation	(\$14,207,778)	(\$12,930,568)
<b>Subtotal</b>	<b>\$11,233,352</b>	<b>\$9,799,279</b>
Construction-In-Progress	\$77,140	\$1,130,252
<b>Capital Assets</b>	<b>\$11,310,492</b>	<b>\$10,929,531</b>

Debt: PCMH acquired one additional loan financing in 2006. Loans and Capital Leases outstanding consisted of:

	<u>2006</u>	<u>2005</u>
Capital Leases	\$208,613	\$328,234
Mortgages Payable	\$347,569	\$387,945
Loan Payable	\$3,823,393	\$3,852,081
<b>Total Debt</b>	<u>\$4,379,575</u>	<u>\$4,568,260</u>

**PERRY COUNTY MEMORIAL HOSPITAL**

**Management Discussion and Analysis**

**Summarized Financial Statement Information related to the hospital activities for the last 2 years**

**STATEMENT OF NET ASSETS**

	2006	2005	Increase Decrease
<b><u>CURRENT ASSETS:</u></b>			
<i>Cash and cash equivalents</i>	\$7,959,580	\$8,675,358	(\$715,778)
<i>Investments</i>	2,140,705	1,891,585	249,120
<i>Patient accounts receivable net of allowance</i>	4,526,754	3,363,629	1,163,125
<i>Accounts receivable</i>	475,588	560,916	(85,328)
<i>Supplies and other current assets</i>	1,036,880	945,347	91,533
<i>Noncurrent cash and investments</i>	3,085,925	2,029,202	1,056,723
<i>Capital assets:</i>			
<i>Land and Construction in progress</i>	1,905,487	2,160,844	(255,357)
<i>Depreciable capital assets, net of accumulated depreciation</i>	9,405,005	8,768,687	636,318
<i>Other Assets</i>	25,000	25,000	0
<b>TOTAL ASSETS</b>	<b>\$30,560,924</b>	<b>\$28,420,568</b>	<b>\$2,140,356</b>
<b><u>LIABILITIES &amp; NET ASSETS</u></b>			
<i>Current Portion - LTD</i>	994,178	667,879	326,299
<i>Accounts payable and accrued expenses</i>	871,191	986,842	(115,651)
<i>Estimated third-party payor settlements</i>	405,999	301,040	104,959
<i>Other Current Liabilities</i>	563,945	569,119	(5,174)
<i>Long-term debt, net of current maturities</i>	3,385,397	3,900,381	(514,984)
<b>TOTAL LIABILITIES</b>	<b>6,220,710</b>	<b>6,425,261</b>	<b>(204,551)</b>
<i>Invested in capital assets, net of related debt</i>	6,955,917	6,386,272	569,645
<i>Unrestricted</i>	17,384,297	15,609,035	1,775,262
<b>TOTAL NET ASSETS</b>	<b>24,340,214</b>	<b>21,995,307</b>	<b>2,344,907</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$30,560,924</b>	<b>\$28,420,568</b>	<b>\$2,140,356</b>

**CHANGES IN NET ASSETS**

	2006	2005	<i>Increase Decrease</i>
<b>PATIENT REVENUES:</b>			
<i>Inpatient Services</i>	\$15,146,103	\$14,576,968	\$569,135
<i>Outpatient Services</i>	32,615,656	28,411,670	4,203,986
<i>Total Patient Revenue</i>	47,761,759	42,988,638	4,773,121
<b>DEDUCTIONS FROM REVENUE:</b>			
<i>Contractual Provision</i>	21,946,715	18,816,593	3,130,122
<i>Charity and Uncompensated Care</i>	2,997,317	2,308,665	688,652
<i>Net Patient Revenue</i>	22,817,727	21,863,380	954,347
<i>Other Operating Revenue</i>	3,587,152	2,844,262	742,890
<i>Net Operating Revenue</i>	26,404,879	24,707,642	1,697,237
<b>OPERATING EXPENSES:</b>			
<i>Salaries &amp; benefits</i>	12,852,534	11,445,859	1,406,675
<i>Medical professional Fees</i>	1,257,524	988,936	268,588
<i>Supplies, food, and drugs</i>	3,202,558	2,885,547	317,011
<i>Depreciation and amortization</i>	1,335,700	1,160,715	174,985
<i>Contracted services</i>	2,553,825	2,643,242	(89,417)
<i>Other expenses</i>	4,381,051	3,973,263	407,788
<i>Total Expenses</i>	25,583,192	23,097,562	2,485,630
<b>Operating Income</b>	821,687	1,610,080	(788,393)
<b>Nonoperating Income ( Expenses)</b>			
<i>Investment income</i>	866,249	459,798	406,451
<i>Interest expense</i>	(206,478)	(152,960)	(53,518)
<i>Noncapital grants and contributions</i>	212,006	0	212,006
<i>Other</i>	(85,650)	0	(85,650)
<i>Net Nonoperating Income</i>	786,127	306,838	479,289
<b>Net Income/(Loss) After Investments</b>	\$1,607,814	\$1,916,918	(\$309,104)

**PERRY COUNTY MEMORIAL HOSPITAL**  
**Management Discussion and Analysis**  
**Summary of key Operating Statistics and Ratio Analysis**

	OPERATING STATISTICS		Percentage Change
	2006	2005	
<b><u>DISCHARGES</u></b>			
Acute Care	1,271	1,268	0%
Swing Bed	102	141	-28%
New Born	94	104	-10%
<b>TOTAL DISCHARGES</b>	<b>1,467</b>	<b>1,513</b>	<b>-3%</b>
<b><u>PATIENT DAYS:</u></b>			
Acute Care	4,080	4,091	-0%
Swing Bed	831	1,141	-27%
New Born	223	252	-12%
<b>TOTAL PATIENT DAYS</b>	<b>5,134</b>	<b>5,484</b>	<b>-6%</b>
<b><u>% UTILIZATION:</u></b>			
Medicare	64.2%	66.1%	-1.9%
Medicaid	13.6%	14.2%	-0.6%
Commercial	19.2%	19.7%	-0.5%
Private Pay	4.3%	2.6%	1.7%
	1		
<b><u>AVERAGE LENGTH OF STAY:</u></b>			
Acute Care	3.2	3.2	
Swing Bed	8.1	8.1	
Newborn	2.4	2.4	
<b><u>OTHER OPERATING STATISTICS</u></b>			
Surgical Operations	1,291	1,332	-3%
Laboratory Tests	107,668	93,259	15%
Physical Therapy/Occ Therapy Tr	20,927	22,343	-6%
Imaging Procedures	17,304	16,343	6%
Respiratory Therapy Treatments	65,040	67,408	-4%
Emergency Room Visits	9,414	9,190	2%
Outpatient Visits	61,468	63,355	-3%
Home Health Visits	3,142	2,808	12%
EMS Trips	1,353	1,266	7%

**PERRY COUNTY MEMORIAL HOSPITAL**  
**Management Discussion and Analysis**  
**Summary of key Operating Statistics and Ratio Analysis**

	S & P BBB	2006	2005
Operating Margin % (Operating Income/Net Operating Revenue)	1.40%	3.11%	6.50%
Total Margin % (Net Income/Net Operating Revenue)	2.70%	6.09%	7.76%
Total EBIDA Margin % (Net Income + Interest + Depreciation / Net Revenue)	10.10%	11.85%	13.08%
Days of Cash on Hand (Unrestricted cash / (Operating Expense-Depreciation)/365)	111	211	232
Days in Accounts Receivable (Net AVR / Net Average Daily Revenue)	51.50	63.50	53.30
Labor Costs to Net Revenue % (Salaries + Benefits) / Net Operating Revenue	53.20%	48.67%	46.33%
Supply Costs to Net Revenue % (Supplies / Net Operating Revenue)	N/A	12.13%	11.68%
Long Term Debt to Capitalization % (Long Term Debt / (Fund Balance + Long Term Debt))	40.70%	12.21%	15.06%
Maxium Annual Debt Service Cove (Net Income + Interest + Depreciation + Amortization) / Debt Service	2.80	4.54	4.84
Cash Flows to Liabilities % (Net Income + Depreciation + Amortization) / Total Liabilities	14.10%	47.32%	47.90%
Cash to Debt (Cash / Long Term Debt)	80.40%	298.35%	270.92%
Average Age of Plant (Years) (Accumulated Depreciation / Depreciation)	10.10	10.64	11.14

PERRY COUNTY MEMORIAL HOSPITAL  
STATEMENT OF NET ASSETS  
December 31, 2006

Assets

Current assets:	
Cash and cash equivalents	\$ 7,959,580
Short-term investments	2,140,705
Patient accounts receivable, net of estimated uncollectibles	4,526,754
Accounts receivable	475,588
Supplies and other current assets	1,036,880
Noncurrent cash and investments:	
Internally designated	2,257,509
Other long-term investments	828,416
Capital assets:	
Land and construction work in progress	1,905,487
Depreciable capital assets, net of accumulated depreciation	9,405,005
Other assets	<u>25,000</u>
Total assets	<u>\$ 30,560,924</u>

Liabilities and Net Assets

Current liabilities:	
Current maturities of long-term debt	\$ 994,178
Accounts payable and accrued expenses	871,191
Estimated third-party payor settlements	405,999
Other current liabilities	563,945
Long-term debt, net of current maturities	<u>3,385,397</u>
Total liabilities	<u>6,220,710</u>
Net assets:	
Invested in capital assets, net of related debt	6,955,917
Unrestricted	<u>17,384,297</u>
Total net assets	<u>24,340,214</u>
Total liabilities and net assets	<u>\$ 30,560,924</u>

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

PERRY COUNTY MEMORIAL HOSPITAL  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
Year Ended December 31, 2006

Operating revenues:	
Net patient service revenue (net of provision for bad debt)	\$ 22,817,727
Other	<u>3,587,152</u>
Total operating revenues	<u>26,404,879</u>
Operating expenses:	
Salaries and benefits	12,852,534
Medical professional fees	1,257,524
Medical supplies and drugs	2,116,832
Insurance	382,946
Other supplies	952,764
Food	132,962
Utilities	498,019
Depreciation and amortization	1,335,700
Contracted services	2,553,825
Service agreements	478,811
Repair and maintenance	104,111
Other expenses	<u>2,917,164</u>
Total operating expenses	<u>25,583,192</u>
Operating income	<u>821,687</u>
Nonoperating revenues (expenses):	
Investment income	866,249
Investment expense	(206,478)
Noncapital grants and contributions	212,006
Other	<u>(85,650)</u>
Total nonoperating revenues	<u>786,127</u>
Increase in net assets	1,607,814
Net assets beginning of the year	<u>22,732,400</u>
Net assets end of the year	<u><u>\$ 24,340,214</u></u>

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

PERRY COUNTY MEMORIAL HOSPITAL  
STATEMENT OF CASH FLOWS  
Year Ended December 31, 2006

Cash flows from operating activities:	
Receipts from and on behalf of patients	\$ 21,654,602
Payments to suppliers and contractors	(8,494,691)
Payments to employees	(12,852,534)
Other receipts and payments, net	<u>664,814</u>
Net cash provided by operating activities	<u>972,191</u>
Cash flows from noncapital financing activities:	
Other	<u>(85,651)</u>
Cash flows from capital and related financing activities:	
Capital grants and contributions	212,006
Principal paid on long-term debt	(688,685)
Interest paid on long-term debt	(206,478)
Purchase of capital assets	<u>(1,216,661)</u>
Net cash used by capital and related financing activities	<u>(1,899,818)</u>
Cash flows from investing activities:	
Interest and dividends on investments	866,249
Net proceeds from investing activities	<u>(610,096)</u>
Net cash provided by investing activities	<u>256,153</u>
Net decrease in cash and cash equivalents	(757,125)
Cash and cash equivalents at beginning of year	<u>9,302,776</u>
Cash and cash equivalents at end of year	<u>\$ 8,545,651</u>
Reconciliation of cash and cash equivalents to the Statement of Net Assets:	
Cash and cash equivalents in current assets	\$ 7,959,580
Restricted cash and cash equivalents	<u>586,071</u>
Total cash and cash equivalents	<u>\$ 8,545,651</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 821,687
Adjustments to reconcile operating income to net cash flows used in operating activities:	
Depreciation and amortization	1,335,700
Provision for bad debts	2,273,441
(Increase) decrease in current assets:	
Patient accounts receivable	(3,436,566)
Accounts receivable	85,328
Supplies and other current assets	(91,533)
Increase (decrease) in current liabilities:	
Accounts payable and accrued expenses	(115,651)
Other current liabilities	(5,174)
Estimated third-party payor settlements	<u>104,959</u>
Net cash provided in operating activities	<u>\$ 972,191</u>
Noncash investing, capital, and financing activities:	
The Hospital entered into a loan agreement of \$500,000 for new equipment in 2006.	

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

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS

I. Summary of Significant Accounting Policies

A. Reporting Entity

Perry County Memorial 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 Perry 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 Perry County.

On September 7, 1971, the Board of County Commissioners of Perry County, upon written request of the Hospital Board of Trustees created the Perry County Memorial Hospital Association. The Association was created pursuant to the provisions of Indiana Code 16-22-6 for the exclusive purpose of financing and constructing hospital facilities for the Hospital.

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

Blended Component Units

The Perry County Memorial Hospital Foundation is a significant blended component unit of the Hospital. The primary government appoints a voting majority of the Foundation's board. 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.

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

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.

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

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.

Open-end mutual funds are reported at fair value.

Money market investments that mature within one year or less at the date of their acquisition are reported at amortized cost. Other money market investments are reported at fair value.

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	\$ 5,000	Straight-line	2 to 20 years
Buildings and improvements	5,000	Straight-line	25 to 45 years
Equipment	5,000	Straight-line	5 to 20 years

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

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 two 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.

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 Perry 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. 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.

F. Compensated Absences

1. Sick Leave

Hospital employees earn sick leave at the rate of twelve days per year. Unused sick leave may be accumulated to a maximum of thirty days. Accumulated sick leave is not paid to employees upon retirement or termination.

2. Vacation Leave

Hospital employees earn vacation leave at rates from five days to twenty-five days per year based upon the number of years of service. One year of employment must be completed before taking vacation leave and it is generally required the vacation leave be taken during each year. Unused vacation leave is paid to employees through cash payment upon termination.

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Vacation leave is accrued when incurred and reported as a liability.

No liability is reported for sick leave.

II. Detailed Notes

A. Deposits and Investments

1. Deposits

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 16-22-3-16 requires only that money in the hospital funds be deposited in the manner determined by the governing board. The Hospital does not have a formal policy regarding custodial credit risk for deposits. At December 31, 2006, the Hospital had deposit balances in the amount of \$8,545,651. Of this amount, \$32,640 was uninsured and un-collateralized. The remaining bank balances were insured by the Federal Deposit Insurance Corporation or the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

2. Investments

As of December 31, 2006, the Hospital had the following investments:

Investment Type	Primary	Investment Maturities (in Years)		
	Government Market Value	Less Than 1	1-2	More Than 2
Corporate bonds	\$ 301,679	\$ 200,147	\$ 101,532	\$ -
Mutual funds	3,831,643	-	-	-
Stocks	282,390	-	-	-
Totals	<u>\$ 4,415,712</u>	<u>\$ 200,147</u>	<u>\$ 101,532</u>	<u>\$ -</u>

Statutory Authorization for Investments

Indiana Code 16-22-3-20 authorizes the Hospital to invest in: 1) any interest bearing account that is authorized to be set up and offered by a financial institution or brokerage firm registered and authorized to do business in Indiana; 2) repurchase or resale agreements involving the purchase and guaranteed resale of any interest bearing obligations issued or fully insured or guaranteed by the United States or any United States government agency in which type of agreement the amount of money must be fully collateralized by interest bearing obligations as determined by the current market value computed on the day the agreement is effective; 3) mutual funds offered by a financial institution or brokerage firm registered and authorized to do business in Indiana; 4) 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; or 5) pooled fund investments for participating hospitals offered, managed, and administered by a financial institution or brokerage firm registered or authorized to do business in Indiana.

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Investment Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Hospital does not have a formal policy for custodial credit risk for investments. At December 31, 2006, the Hospital held investments in stocks and corporation bonds in the amount of \$584,069. Of these investments \$584,069 were held by the counterparty's trust department or agent but not in the Hospital's name.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The distribution of securities with credit ratings is summarized below.

Standard and Poor's Rating	Hospital's Investments Corporate Bonds
AAA	\$ -
AA	101,532
A	-
BBB	-
BB	100,130
B	-
CCC	-
Unrated	100,017
Total	\$ 301,679

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a Hospital's investment in a single issuer. The Hospital does not have a policy in regards to concentration of credit risk. United States of America government and United States of America governmental agency securities are exempt from this policy requirement.

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

The Hospital held the following investments that were exposed to concentration of credit risk:

Issuer	December 31, 2006
Spdr Tr Unit Ser 1	\$ 282,390
T. Rowe Price Funds	244,346
Mutual Funds held at Edward Jones	1,796,994
Mutual Funds held at Fifth Third Securities	1,790,303
Total	\$ 4,114,033

Foreign Currency Risk

The Hospital does not have a formal policy in regards to foreign currency risk.

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	\$ 3,948,966
Receivable from Medicare	2,288,677
Receivable from Medicaid	1,137,813
Total patient accounts receivable	7,375,456
Less allowance for uncollectible amounts	2,848,702
Patient accounts receivable, net	\$ 4,526,754

Accounts Payable and Accrued Expenses

Payable to employees (including payroll taxes)	\$ 563,945
Payable to suppliers	871,191
Other	405,999
Total accounts payable and accrued expenses	\$ 1,841,135

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

C. Capital Assets

Capital asset activity for the year ended December 31, 2006, was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 1,030,592	\$ 842,019	\$ 44,264	\$ 1,828,347
Construction in progress	<u>1,130,252</u>	<u>1,333,453</u>	<u>2,386,565</u>	<u>77,140</u>
 Total capital assets, not being depreciated	 <u>2,160,844</u>	 <u>2,175,472</u>	 <u>2,430,829</u>	 <u>1,905,487</u>
Capital assets, being depreciated:				
Land improvements	1,187,046	141,919	-	1,328,965
Buildings and improvements	8,679,434	1,342,016	16,000	10,005,450
Equipment	<u>11,832,775</u>	<u>506,438</u>	<u>60,845</u>	<u>12,278,368</u>
 Totals	 <u>21,699,255</u>	 <u>1,990,373</u>	 <u>76,845</u>	 <u>23,612,783</u>
Less accumulated depreciation for:				
Land improvements	1,000,160	31,555	-	1,031,715
Buildings and improvements	3,993,379	318,660	-	4,312,039
Equipment	<u>7,937,029</u>	<u>985,485</u>	<u>58,490</u>	<u>8,864,024</u>
 Totals	 <u>12,930,568</u>	 <u>1,335,700</u>	 <u>58,490</u>	 <u>14,207,778</u>
 Total capital assets, being depreciated, net	 <u>8,768,687</u>	 <u>654,673</u>	 <u>18,355</u>	 <u>9,405,005</u>
 Total capital assets, net	 <u>\$ 10,929,531</u>	 <u>\$ 2,830,145</u>	 <u>\$ 2,449,184</u>	 <u>\$ 11,310,492</u>

D. Construction Commitments

Construction work in progress is composed of the following:

<u>Project</u>	<u>Total Project Authorized</u>	<u>Expended to December 31, 2006</u>	<u>Committed</u>	<u>Required Future Funding</u>
Master planning	\$ 68,052	\$ 68,052	\$ -	\$ -
Workbench	5,725	5,725	-	-
PC Clinic	<u>3,363</u>	<u>3,363</u>	<u>-</u>	<u>-</u>
 Totals	 <u>\$ 77,140</u>	 <u>\$ 77,140</u>	 <u>\$ -</u>	 <u>\$ -</u>

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

E. Capital Leases

The Hospital has entered into various capital leases for equipment. Future minimum lease payments and present values of the net minimum lease payments under these capital leases as of year end, are as follows:

2007	\$	126,959
2008		49,551
2009		39,918
2010		<u>3,326</u>
Total minimum lease payments		219,754
Less amount representing interest		<u>11,141</u>
Present value of net minimum lease payments		<u><u>\$ 208,613</u></u>

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

Equipment	\$	606,084
Accumulated depreciation		<u>374,426</u>
Total	\$	<u><u>231,658</u></u>

F. Long-Term Liabilities

1. Mortgages and Loans Payable

The Hospital has entered into various mortgages and loans. Annual debt service requirements to maturity including interest of \$713,237, are as follows:

2007	\$	1,057,655
2008		639,640
2009		621,069
2010		621,069
2011		621,068
2012-2016		<u>1,323,698</u>
Total	\$	<u><u>4,884,199</u></u>

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

2. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2006, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Capital leases	\$ 328,234	\$ -	\$ 119,621	\$ 208,613	\$ 120,128
Mortgage payable	387,945	-	40,376	347,569	347,569
Loans payable	<u>3,852,081</u>	<u>500,000</u>	<u>528,688</u>	<u>3,823,393</u>	<u>526,481</u>
Total long-term liabilities	<u>\$ 4,568,260</u>	<u>\$ 500,000</u>	<u>\$ 688,685</u>	<u>\$ 4,379,575</u>	<u>\$ 994,178</u>

G. Charity Care

Charges excluded from revenue under the Hospital's charity care policy were \$723,876 for 2006.

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. 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	\$ 280,499
Investments	<u>1,516,438</u>
Total funded depreciation	<u>1,796,937</u>
Board designation:	
Cash and cash equivalents	305,572
Scholarship Fund	55,000
Endowment Fund	<u>100,000</u>
Total board designation	<u>460,572</u>
Total internally designated	<u>\$ 2,257,509</u>

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

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, Retirees and Dependents (Excluding Postemployment Benefits)

The Hospital has contracted with a Third Party to administer the Perry County Memorial Hospital Employee Benefit Trust, an account created to service employee health benefit claims and administrative costs of the program. This is a pay as you go system and claims are expensed as incurred. An excess policy through commercial insurance covers individual claims in excess of \$35,000 per year. Settled claims resulting from this risk did not exceed commercial insurance coverage in the past three years. A premium is charged to each fund that accounts for employee payroll. This total charge is calculated using trends in actual claims experience.

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. Fair Value of Financial Instruments

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

Cash and Cash Equivalents

The carrying amount reported in the statement of net assets for cash and cash equivalents approximates its fair value.

Short-Term Investments

The carrying amount reported in the statement of net assets is the investment's fair value on the day it becomes a short-term investment.

Investments

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

PERRY COUNTY MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Accounts Payable and Accrued Expenses

The carrying amount reported in the statement of net assets for accounts payable and accrued expenses approximates its fair value.

Estimated Third-Party Payor Settlements

The carrying amount reported in the statement of net assets for estimated third-party payor settlements approximates its fair value.

D. Pension Plan

Defined Contribution Pension Plan

Plan Description

The Hospital has a defined contribution pension plan administered by Plan Administrators 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:

Plan Administrators, Inc.  
115 S. Wisconsin Street  
Depere, WI 54775-2765  
Ph. (920)337-9906

Funding Policy and Annual Pension Cost

The contribution requirements of plan members are established by the written agreement between the Hospital Board of Trustees and the Plan Administrator. Plan members are required to contribute 3% of the annual covered salary plus an optional 3% matching contribution. Employer and employee contributions to the plan were \$367,169 and \$311,149, respectively.

E. Ambulance Service Subsidy

Perry County Memorial Hospital provides ambulance service for Perry County residents, including the cities of Cannelton and Tell City, through an agreement dated July 1986. The agreement provides that Perry County is to reimburse the Hospital, on monthly basis, for the amount that expenses exceeded revenues for the period. During 2006, the County reimbursed the Hospital \$102,759 for ambulance services.

In addition, the County leases the EMS Building from the Hospital. During 2006, the final lease payment of \$9,750 was received.

These amounts are included in the financial statements in other operating revenue.

PERRY COUNTY MEMORIAL HOSPITAL  
EXIT CONFERENCE

The contents of this report were discussed on April 9, 2007, with Joseph Stuber, Executive Director; and Kathy Clayton, Treasurer. Our audit disclosed no material items that warrant comment at this time.

Separate phone exits were held with Board members: Dr. Joe LeClere, Grant Taylor, Don Etienne, John B. Land, Tim Harding and Rita Mahoney.