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

AUDIT REPORT  
OF

SCOTT MEMORIAL HOSPITAL  
A COMPONENT UNIT OF  
SCOTT COUNTY, INDIANA

January 1, 2006 to December 31, 2006



**FILED**

06/28/2007



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HOSPITAL OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
President/Executive Director	Clifford D. Nay	01-01-06 to 12-31-07
Chief Financial Officer/Treasurer	Angela G. Doan	01-01-06 to 12-31-07
Chairman of the Hospital Board	Randy Hancock Ivan R. Wells	01-01-06 to 12-31-06 01-01-07 to 12-31-07
President of the Board of County Commissioners	Mark Hays Robert Tobias	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 SCOTT MEMORIAL HOSPITAL, SCOTT COUNTY, INDIANA

We have audited the accompanying basic financial statements of Scott 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 did not audit the financial statements of the Jewish Hospital & St. Mary's HealthCare Network Regional Service Center, LLC, an affiliated company. Those financial statements were audited by other auditors whose report has been furnished to us. Our opinion, insofar as it relates to the investment in affiliated companies (other assets) in the amount of \$161,473, is based solely on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States. 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, based on our audit and report of the other auditors, 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 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

June 5, 2007

# SCOTT MEMORIAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS

This section of Scott Memorial Hospital's (Hospital) annual financial statements presents background information and management's discussion and analysis (MD&A) of the Hospital's financial performance during this fiscal year ended December 31, 2006. This MD&A should be read together with the financial statements included in this report. While there are comparisons made in this report to December 31, 2005 we realize that they are not presented in the audited financial statements but have listed them in this report for comparative discussion. Figures shown are rounded to the thousands.

## OPERATING RESULTS AND FINANCIAL PERFORMANCE

During 2006, the Hospital derived substantially all of its revenue from patient services and other related activities. The Hospital's revenues depend upon inpatient occupancy levels, related ancillary services, and outpatient procedures as ordered by physicians. The Hospital's gross charges typically do not reflect what is actually paid. The Hospital has 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 according to the patient's diagnosis or on a discount 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 anticipated payment.

The Hospital 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. In 2006, inpatient revenues from the Medicare and Medicaid programs increased to 79.6% of total gross inpatient revenues up from 70.3% in 2005. Outpatient revenues from the Medicare and Medicaid programs showed an increase from 2005 to 2006, going from 46.0% to 47.6%.

The table below presents the percentages of gross revenues for patient services, by payer, for the years ended December 31, 2006 and 2005, respectively:

	2006			2005		
	Inpatient	Outpatient	Combined	Inpatient	Outpatient	Combined
Medicare	55.1%	29.5%	38.8%	53.5%	29.1%	36.4%
Medicaid	24.5%	18.1%	17.3%	16.8%	16.9%	16.9%
Blue Cross	4.6%	17.0%	15.0%	5.4%	17.0%	13.5%
Other	11.3%	25.7%	21.5%	16.0%	29.7%	25.6%
Self Pay	4.5%	9.7%	7.4%	8.3%	7.3%	7.6%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

## FINANCIAL STATEMENTS

The financial statements of the Hospital present information about the Hospital using financial reporting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information. The Balance Sheet includes all of the Hospital's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to Hospital creditors (liabilities). All of the current year's revenues and expenses are accounted for in the Statement of Revenue and Expenses and Changes in Net Assets. These statements measure the financial results of the Hospital's operations and presents revenues earned and expenses incurred. The final statement is the Statement of Cash Flows. The primary purpose of the statement is to provide information about the Hospital's cash flow from operating activities, capital and related financing activities and investing activities, and provides information on the sources and uses of cash during the year.

## FINANCIAL ANALYSIS

The Balance Sheet and the Statement of Revenues and Expenses and Changes in Net Assets report information about the Hospital's activities. These three 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 it's financial health is improving or deteriorating. However, other non-financial factors such as changes in economic conditions, population growth (including uninsured and medically indigent individuals and families) and new or changed government legislation need to also be considered.

A summary of the Hospital's Combined Balance Sheets as of December 31, 2006 and 2005 is presented below (in thousands):

	2006	2005	\$ Change	% Change
<b>Assets:</b>				
Cash and equivalents	\$ 4,703	\$ 3,210	\$1,493	47%
Other assets	2,512	2,349	163	7%
Net property and equipment	12,350	12,676	(326)	(3%)
Accounts Receivable	4,312	3,305	1,007	30%
Short Term Investments	4,830	4,173	657	16%
<b>Total Assets</b>	<b>\$28,707</b>	<b>\$25,713</b>	<b>\$2,994</b>	<b>12%</b>
<b>Liabilities and Fund Balance:</b>				
Current and other liabilities	\$1,100	\$1,130	(\$30)	(3%)
Long-term obligations	0	0	0	0
Total liabilities	1,100	1,130	(30)	(3%)

Total Unrestricted Net Assets	27,607	24,583	3,024	12%
<b>Total Liabilities &amp; Fund Balance</b>	<u>\$28,707</u>	<u>\$25,713</u>	<u>\$2,994</u>	<u>12%</u>

*Notes on the Balance Sheet*

- The Hospital's fund balance increased by \$3 million, derived from operating income of \$2 million and \$1 million from DSH payment to offset amount of indigent care.
- The Hospital investment policy allows it to invest in mutual funds. Short & long term investments increased 16% due to this change.
- Cash increased 47% due to increase in revenue of 5% and capital expenditures were less than anticipated.
- Receivables, net increased 31% due to increase in revenue of 5% and in some billing issues that caused a delay in payment. Coding was behind due to change in management position but also was resolved at the first of 2007.
- Estimated third party settlements increased 173%, this was due to our change in CAH and the receiving 100% of Medicare allowable bad debt.
- Capital Assets, net decreased 3%. This was caused due to depreciation expense exceeding capital purchases.
- Accounts payable and accrued expenses decreased 23% in 2006. Vendor accruals decreased by \$18,000 and general accruals decreased by \$10,000 and the biggest change was in management fee, which decreased \$36,000.
- Other current liabilities increased 19%. This change occurred in accrued wages of \$53,000 and accrued vacation of \$8,000.

**CAPITAL ASSETS**

- During the year, the Hospital made the following significant capital acquisitions and improvements:
  - \$441,000 was expended on a new office building to house Physical Therapy and Dr. McEldowney.
  - The Hospital invested \$622,000 in other areas within the hospital in 2006.

A summary of the Hospital's capital asset balances as of December 31, 2006 and 2005 is presented below (in thousands):

<b>As of</b>	<b>Disposals/</b>	<b>As of</b>
--------------	-------------------	--------------

	<b>12/31/2005</b>	<b>Additions</b>	<b>Retirements</b>	<b>12/31/2006</b>
Land and improvements	\$ 762	\$ 19	\$9	\$ 772
Buildings	11,967	445	24	12,388
Equipment	10,081	449	210	10,320
Construction in progress	0	150	0	150
	<hr/>	<hr/>	<hr/>	<hr/>
Total capital assets	22,810	1,063	243	23,480
Less accumulated				
Depreciation	(10,134)	1,147	3	(11,278)
	<hr/>	<hr/>	<hr/>	<hr/>
Capital assets – net	\$12,676	\$ 84	\$ 240	\$12,350
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

A summary of the Hospital's Statements of Revenue and Expenses and Changes in Fund Balances for the years ended December 31, 2006 and 2005 is presented below (in thousands):

	<b>2006</b>	<b>2005</b>	<b>\$ Change</b>	<b>% Change</b>
<b>Revenues:</b>				
Net patient service revenue	\$19,430	\$18,371	\$1,059	6.0
Other	386	396	10	(3.0%)
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Total Revenues</b>	\$19,816	\$18,767	(\$1,802)	(9.0%)
<b>Operating Expenses:</b>				
Salaries and benefits	\$10,003	\$9,189	\$814	9.0%
Medical Professional Fees	139	240	(102)	(42.0%)
Other Professional Fees	2,385	2,409	(23)	(1.0%)
Supplies	2,457	2,455	2	1.0%
Other	1,141	1,138	3	.0%
Management Fees	263	512	(249)	(49.0%)
Depreciation	1,373	1,406	(34)	(3.0%)
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Total Operating Expenses</b>	\$17,762	\$17,349	\$455	3.0%
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Operating Income</b>	2,054	1,417	637	45.0%
Investment Income	797	256	540	211.0%
Non-capital grants and contributions	148	99	49	49.0%
Other non-operating income	0	137	(137)	(100%)

Gain (loss) on invest in affiliated companies & gain/loss on equip	26	34	8	(24.0%)
Total non operating revenues	971	526	444	84.0%
Excess (deficiency) before capital grants and contributions	3,024	1,943	1,082	56.0%
Capital grants and contributions	0	0	0	0
<b>Increase (decrease) in net assets</b>	<b>\$3,024</b>	<b>\$1,943</b>	<b>\$1,082</b>	<b>56.0%</b>

*Notes on the Hospital's Combined Statements of Operations and Changes in Net Assets:*

- The Hospital's fund balance increased by \$3 million, derived from operating income of \$2 million and \$1 thousand from DSH payment to offset amount of indigent care.
- Management fees decreased \$249,000 from 2005 to 2006. These fees are based on the hospital's net assets before contributions, however, there was a contract correction made in the calculation to exclude investment income from this calculation. There was a contract period revision back to the start of the contract in 1991. This is the main reason for the decrease; normal calculation would have caused us to be higher than 2005.
- We implemented an investment policy, which allowed us to invest more aggressively which contributed to the significant increase in investment income due to market conditions.

Future Events

- The hospital will be moving forward with the construction and renovation of new surgery suite. We currently have 4,000 square feet and there will be an addition to bring it to a total of 24,000 square feet. The budget for this project with FFE is anticipated on being \$7 million dollars. The old Physical Therapy space will be renovated to house Dr. Janet Buhse, and our employed OBGYN Dr. Charles Buhse at a cost of approximately \$80,000. It is anticipated that they will move in May 2007.

SCOTT MEMORIAL HOSPITAL  
STATEMENT OF NET ASSETS  
December 31, 2006

Assets

Current assets:	
Cash and cash equivalents	\$ 4,703,288
Short-term investments	4,829,593
Patient accounts receivable, net of estimated uncollectibles of \$5,437,416	4,312,288
Estimated third-party settlements	500,215
Supplies and other current assets	1,840,963
Capital assets:	
Land and construction in progress	425,201
Depreciable capital assets, net of accumulated depreciation	11,925,356
Other assets	<u>170,342</u>
Total assets	<u>\$ 28,707,246</u>

Liabilities and Net Assets

Current liabilities:	
Accounts payable and accrued expenses	\$ 445,122
Other current liabilities	<u>654,967</u>
Total liabilities	<u>1,100,089</u>
Net assets:	
Invested in capital assets, net of related debt	12,350,557
Unrestricted	<u>15,256,600</u>
Total net assets	<u>27,607,157</u>
Total liabilities and net assets	<u>\$ 28,707,246</u>

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

SCOTT 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)	\$ 19,430,048
Other	<u>385,902</u>
Total operating revenues	<u>19,815,950</u>
Operating expenses:	
Salaries and benefits	10,003,383
Supplies	2,457,806
Purchased services	2,385,227
Professional services	138,669
Other	1,141,148
Management fee (see note disclosure)	262,992
Depreciation and amortization	<u>1,372,564</u>
Total operating expenses	<u>17,761,789</u>
Operating income	<u>2,054,161</u>
Nonoperating revenues (expenses):	
Investment income	796,551
Noncapital grants and contributions	147,623
Loss on sale of equipment	(5,549)
Gain on investment in affiliated companies	<u>32,000</u>
Total nonoperating revenues (expenses)	<u>970,625</u>
Increase in net assets	3,024,786
Net assets beginning of the year	<u>24,582,371</u>
Net assets end of the year	<u>\$ 27,607,157</u>

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

SCOTT MEMORIAL HOSPITAL  
STATEMENT OF CASH FLOWS - RESTRICTED AND UNRESTRICTED FUNDS  
Year Ended December 31, 2006

Cash flows from operating activities:	
Receipts from and on behalf of patients	\$ 18,422,295
Payments to suppliers and contractors	(6,314,431)
Payments to employees	(9,947,075)
Other receipts and payments, net	<u>68,551</u>
Net cash provided by operating activities	<u>2,229,340</u>
Cash flows from noncapital financing activities:	
Noncapital grants and contributions	<u>147,623</u>
Cash flows from capital and related financing activities:	
Proceeds from sale of capital assets	9,526
Purchase of capital assets	<u>(1,062,075)</u>
Net cash used by capital and related financing activities	<u>(1,052,549)</u>
Cash flows from investing activities:	
Interest and dividends on investments	438,450
Increase in investment in affiliated company	28,969
Purchase of investments	(1,298,472)
Proceeds from sale of investments	<u>1,000,000</u>
Net cash provided by investing activities	<u>168,947</u>
Net increase in cash and cash equivalents	1,493,361
Cash and cash equivalents at beginning of year	<u>3,209,927</u>
Cash and cash equivalents at end of year	<u><u>\$ 4,703,288</u></u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 2,054,161
Adjustments to reconcile operating income to net cash flows provided by operating activities:	
Depreciation and amortization	1,372,564
Provision for bad debts	3,876,203
(Increase) decrease in current assets:	
Patient accounts receivable	(4,883,956)
Supplies and other current assets	157,999
Estimated third-party payor settlements	(317,351)
Increase (decrease) in current liabilities:	
Accounts payable and accrued expenses	(133,367)
Other current liabilities	<u>103,087</u>
Net cash provided by operating activities	<u><u>\$ 2,229,340</u></u>

Noncash investing, capital, and financing activities:

The Hospital held investments at December 31, 2006 with a fair value of \$4,829,593. During 2006, the net increase in the fair value of these investments was \$358,101.

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

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS

I. Summary of Significant Accounting Policies

A. Reporting Entity

Scott 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 Scott 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 Scott County.

The accompanying financial statements present the activities of the Hospital (primary government). There are no significant component units which require inclusion.

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.

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.

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.

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Investments in affiliated companies are reported using the equity method of accounting, or at cost, as applicable.

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	\$ 1,000	Straight-line	5 to 25 years
Buildings and improvements	1,000	Straight-line	5 to 50 years
Equipment	1,000	Straight-line	2 to 25 years

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. There was no interest expense incurred by the Hospital during the current year.

4. Net Assets

Net assets of the Hospital are classified in two components.

Net assets invested in capital assets consist of capital assets net of accumulated depreciation.

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

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

D. Grants and Contributions

From time to time, the Hospital receives grants from Scott 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

1. Sick Leave

Hospital employees earn sick leave at the rate of 12 days per year. Unused sick leave may be accumulated to a maximum of 54 to 60 days depending upon job classification. Accumulated sick leave is not paid to employees.

2. Vacation Leave

Hospital employees earn vacation leave at rates from 10 to 20 days per year based upon the number of years of service. Vacation leave may be carried over from one year to the next; however, the amount carried over cannot exceed the employee's annual accrual amount.

3. Personal Leave

Hospital employees earn personal leave at the rate of 1 to 3 days per year based upon meeting certain conditions. Personal leave is not cumulative and must be taken within 6 months after being accrued.

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

No liability is reported for sick and personal leave.

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

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 16-22-3-15 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 bank balance held at Edward Jones in the amount of \$88 was uncollateralized. 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

Authorization for investment activity is stated in Indiana Code 16-22-3-20. As of December 31, 2006, the Hospital had mutual funds with a market value of \$4,829,593.

Investment Policies

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.

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	\$ 6,451,532
Receivable from Medicare	1,948,349
Receivable from Medicaid	<u>1,349,823</u>
Total patient accounts receivable	9,749,704
Less allowance for uncollectible amounts	<u>5,437,416</u>
Patient accounts receivable, net	<u><u>\$ 4,312,288</u></u>

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Accounts Payable and Accrued Expenses

Payable to employees (including payroll taxes)	\$ 657,089
Payable to suppliers	441,522
Other	<u>1,478</u>
Total accounts payable and accrued expenses	<u>\$ 1,100,089</u>

C. Capital Assets

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

<u>Primary Government</u>	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 285,708	\$ -	\$ 9,475	\$ 276,233
Construction in progress	<u>-</u>	<u>659,271</u>	<u>510,303</u>	<u>148,968</u>
Total capital assets, not being depreciated	<u>285,708</u>	<u>659,271</u>	<u>519,778</u>	<u>425,201</u>
Capital assets, being depreciated:				
Land improvements	476,383	19,179	-	495,562
Buildings	11,966,807	445,363	23,945	12,388,225
Fixed equipment	2,109,776	9,766	87,746	2,031,796
Major movable equipment	<u>7,971,692</u>	<u>438,798</u>	<u>122,402</u>	<u>8,288,088</u>
Totals	<u>22,524,658</u>	<u>913,106</u>	<u>234,093</u>	<u>23,203,671</u>
Less accumulated depreciation for:				
Land improvements	289,010	30,924	-	319,934
Buildings	3,452,970	511,992	19,070	3,945,892
Fixed equipment	1,715,824	58,071	87,022	1,686,873
Major movable equipment	<u>4,676,441</u>	<u>771,577</u>	<u>122,402</u>	<u>5,325,616</u>
Totals	<u>10,134,245</u>	<u>1,372,564</u>	<u>228,494</u>	<u>11,278,315</u>
Total capital assets, being depreciated, net	<u>12,390,413</u>	<u>(459,458)</u>	<u>5,599</u>	<u>11,925,356</u>
Total primary government capital assets, net	<u>\$ 12,676,121</u>	<u>\$ 199,813</u>	<u>\$ 525,377</u>	<u>\$ 12,350,557</u>

D. Construction Commitments

Construction work in progress is composed of the following:

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
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<u>Project</u>	<u>Total Project Authorized</u>	<u>Expended to December 31, 2006</u>	<u>Required Future Funding</u>
MED 3/ICU	\$ 90,000	\$ 53,932	\$ 36,068
Sleep Lab	20,000	6,872	13,128
Surgery	<u>7,000,000</u>	<u>88,164</u>	<u>6,911,836</u>
Totals	<u>\$ 7,110,000</u>	<u>\$ 148,968</u>	<u>\$ 6,961,032</u>

E. Charity Care

Charges excluded from revenue under the Hospital's charity care policy were \$121,543 for 2006.

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; 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.

B. Management Agreement Related Party Transactions

In 1991, the Hospital entered into an agreement with MedGroup Management, Inc. (MedGroup), an affiliate of Jewish Hospital HealthCare Services, Inc., whereby MedGroup would supervise, manage and operate the Hospital. According to the agreement, MedGroup will provide the Chief Executive Officer, who will be appointed by the Hospital's Board of Directors, and the Chief Financial Officer.

Expenses related to the management contract with MedGroup for 2006 were \$624,028. In addition, expenses in the amount of \$1,840,331 were incurred during 2006 for services performed by Jewish Hospital HealthCare Services, Inc., and its related entities. As of the statement of net assets date, the amount of \$179,925 was due to MedGroup Management and its affiliates.

The management fee expense shown on the statement of revenues, expenses, and changes in net assets for the year ended December 31, 2006, of \$262,992 is net of overpayments from prior years totaling \$247,345. The agreement excludes investment income from the net operating income amount on which the management fee is calculated. In prior years this income was inadvertently included in the amount on which the management fee was based. The management fee for 2006 before deducting the prior year overpayments was \$510,338.

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
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C. 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.

D. Fair Value of Financial Instruments

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

Cash and Cash Equivalents

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

Short-Term Investments

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

Investments

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

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.

E. Investment in Affiliated Companies

Regional Service Center

In 1999, the Hospital entered into an agreement with seven related hospitals to establish and operate a purchasing and supply distribution center. In accordance with this agreement, the Hospital invested \$103,183 for 1.6% equity interest in the distribution center. The investment was made in the years 1999 and 2000. The distribution center began operation in 1999. During 2004, the agreement was amended to allow for annual ownership adjustments based on the aggregate purchases of all members during the fiscal year most recently ended. Accordingly, at December 31, 2006, Scott Memorial Hospital's equity interest was 1.3%. The investment is recorded on the equity method. The Hospital's investment in affiliated companies is included in the Other Assets category of the statement of net assets.

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Summarized financial information as of December 31, 2006, and for the year then ended from the audited financial statements of the Affiliated Company follows:

Current assets	\$ 21,419,053
Noncurrent assets	664,469
Current liabilities	9,388,314
Stockholders' equity	12,695,208
Revenue	114,406,921
Net income	3,409,567

In 2006, services and supplies in the amount of \$968,161 were provided by the distribution center to the Hospital. At December 31, 2006, \$75,240 was reported in accounts payable as owed to the service center. During 2006, the Hospital received distributions from the service center in the amount of \$38,400 and made an additional investment of \$9,431.

Health Care Staffing Agency

In 2002, the Hospital entered into an agreement with two related hospitals to establish and operate a health care staffing agency and cost share support services. In accordance with this agreement, the Hospital invested \$8,869 for 7% equity interest in the health care staffing agency. The investment was made in the year 2002. The health care staffing agency began operation in 2002. The investment is recorded on the cost method. The Hospital's investment in affiliated companies is included in the Other Assets category of the statement of net assets.

Summarized financial information as of December 31, 2006, and for the year then ended from the unaudited financial statements of the Affiliated Company follows:

Current assets	\$ 199,000
Noncurrent assets	11,000
Current liabilities	245,000
Stockholders equity	(35,000)
Revenue	1,910,000
Net income	95,000

In 2006, services in the amount of \$77,052 were provided by the health care staffing agency to the Hospital. At December 31, 2006, \$20,973 was recognized in accounts payable as amounts owed by the Hospital to the Health Care Staffing Agency.

F. Estimated Third-Party Settlements

Regulations in effect require annual retroactive settlements for third-party settlements based upon cost reports filed by the Hospital. These retroactive settlements are estimated and recorded in the accompanying financial statements. Changes in these estimates are reflected in the year in which they occur. During 2006, net patient service revenues in the accompanying statements of operations were decreased by \$143,664, to reflect changes in the estimated settlements for certain prior years.

SCOTT MEMORIAL HOSPITAL  
NOTES TO FINANCIAL STATEMENTS  
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G. Pension Plan

Defined Contribution Pension Plan

Plan Description

The Hospital has a defined contribution pension plan administered by Diversified Investment Advisors 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 does not issue a publicly available financial report that includes financial statements and required supplementary information of the plan.

Funding Policy

The contribution requirements of plan members are established by the written agreement between the Hospital Board of Trustees and the Plan Administrator. Plan members may, but are not required to, contribute to the fund. The Hospital is required to contribute 4% of each eligible individual's annual covered payroll. After five years of service the employee is vested in the plan. Statements of employer and employee contributions to the plan are sent to individual plan members. The Hospital does not receive a statement.

SCOTT MEMORIAL HOSPITAL  
EXIT CONFERENCE

The contents of this report were discussed on June 5, 2007, with Clifford D. Nay, President/Executive Director; Ivan R. Wells, Chairman of the Hospital Board; and Angela G. Doan, Chief Financial Officer/Treasurer. Our audit disclosed no material items that warrant comment at this time.