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January 23, 2013

Board of Directors  
Hancock Regional Hospital  
801 N. State Street  
Greenfield, IN 46140

We have reviewed the audit report prepared by Blue & Company, LLC, Independent Public Accountants, for the period January 1, 2011 to December 31, 2011. In our opinion, the audit report was prepared in accordance with the guidelines established by the State Board of Accounts. Per the Independent Public Accountants' opinion, the financial statements included in the report present fairly the financial condition of the Hancock Regional Hospital, as of December 31, 2011 and the results of its operations for the period then ended, on the basis of accounting described in the report.

The Independent Public Accountants' report is filed with this letter in our office as a matter of public record.

STATE BOARD OF ACCOUNTS



**COMBINED FINANCIAL STATEMENTS**

**DECEMBER 31, 2011 AND 2010**

*CPAs / ADVISORS*



# HANCOCK REGIONAL HOSPITAL

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## REPORT OF INDEPENDENT AUDITORS

Board of Trustees  
Hancock Regional Hospital  
Greenfield, Indiana

We have audited the accompanying combined balance sheets of Hancock Regional Hospital (Hospital) and component units as of December 31, 2011 and 2010, and the related combined statements of operations and changes in net assets, and cash flows for the years then ended. These combined financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

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

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of the Hospital as of December 31, 2011 and 2010, and its combined results of operations, changes in net assets, and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Board of Trustees  
Hancock Regional Hospital  
Greenfield, Indiana

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Blue & Co., LLC*

April 24, 2012

**REQUIRED SUPPLEMENTARY INFORMATION**

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

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This section of Hancock Regional Hospital's (Hospital) annual combined financial statements presents background information and management's discussion and analysis of the Hospital's financial performance during the years ended December 31, 2011 and 2010. Please read it in conjunction with the Hospital's combined financial statements, which begin on page 3. Unless otherwise indicated, amounts are in thousands.

### FINANCIAL HIGHLIGHTS

- The Hospital reported a decrease in net assets of approximately \$119 or 0.1% for the year ended 2011.
- Operating income in 2011 compared to 2010 decreased by \$1,233 or 28.3%.
- Nonoperating income decreased from 2011 to 2010 by \$4,961 or 202.2%.

### USING THIS ANNUAL REPORT

The Hospital's financial statements consist of three statements—a Balance Sheet; a Statement of Operations and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by contributors, grantors, or enabling legislation.

### THE BALANCE SHEET AND STATEMENT OF OPERATIONS CHANGES IN NET ASSETS

Our analysis of the Hospital finances begins on page ii. One of the most important questions asked about the Hospital's finances is, "Is the Hospital as a whole better or worse off as a result of the year's activities?" The Balance Sheet and the Statement of Operations, and Changes in Net Assets report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These statements report the Hospital's net assets and changes in them. You can think of the Hospital's net assets—the difference between assets and liabilities—as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the Hospital's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the Hospital.

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

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### THE STATEMENT OF CASH FLOWS

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It provides answers to such questions as “Where did cash come from?” “What was cash used for?” and “What was the change in cash balance during the reporting period?”

### THE HOSPITAL’S NET ASSETS

The Hospital’s net assets are the difference between its assets and liabilities reported in the Balance Sheet on page 3. The Hospital’s net assets decreased in 2011 by \$119 (0.1%) as you can see from Table 1.

**Table 1: Assets, Liabilities, and Net Assets**

	<u>2011</u>	<u>2010</u>	<u>2011 - 2010</u> <u>\$ Change</u>	<u>2009</u>
<b>Assets</b>				
Current assets	\$ 32,057	\$ 28,541	\$ 3,516	\$ 30,657
Capital assets, net	64,536	67,041	(2,505)	64,338
Restricted and limited use assets	43,730	45,780	(2,050)	41,382
Other noncurrent assets	4,176	3,128	1,048	3,603
Total assets	<u>144,499</u>	<u>144,490</u>	<u>9</u>	<u>139,980</u>
<b>Liabilities</b>				
Current liabilities	16,956	15,868	1,088	16,286
Long - term debt outstanding	29,245	30,205	(960)	31,230
Total liabilities	<u>46,201</u>	<u>46,073</u>	<u>128</u>	<u>47,516</u>
<b>Net Assets</b>				
Unrestricted	56,494	53,928	2,566	52,091
Invested in capital assets, net of related debt	34,331	35,916	(1,585)	32,193
Restricted by trustee for debt service	3,798	5,030	(1,232)	4,199
Donor restricted - expendable	805	694	111	666
Net assets - controlling interest	95,428	95,568	(140)	89,149
Non-controlling interest	2,870	2,849	21	3,315
Total net assets	<u>98,298</u>	<u>98,417</u>	<u>(119)</u>	<u>92,464</u>
Total liabilities and net assets	<u>\$ 144,499</u>	<u>\$ 144,490</u>	<u>\$ 9</u>	<u>\$ 139,980</u>

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

A significant component in the Hospital's assets is the increase in current assets. Current assets increased by \$3,516 or 12.3% due to the increase in patient accounts receivable as well as the addition of an OB/GYN practice. Capital assets, net decreased as depreciation exceeded the additions/retirements, net activity. The reduction in restricted and limited use assets is attributable to the market conditions in investments.

### OPERATING RESULTS AND CHANGES IN THE HOSPITAL'S NET ASSETS

In 2011, the Hospital's change in net assets decreased by \$6,072 compared to 2010 as shown in Table 2.

**Table 2: Operating Results and Changes in Net Assets**

	<u>2011</u>	<u>2010</u>	<u>2011 - 2010 \$ Change</u>	<u>2009</u>
<b>Operating Revenue</b>				
Net patient service revenue	\$ 89,363	\$ 87,626	\$ 1,737	\$ 90,374
Other	7,498	6,449	1,049	6,018
Total operating revenue	<u>96,861</u>	<u>94,075</u>	<u>2,786</u>	<u>96,392</u>
<b>Operating expenses</b>				
Salaries and benefits	50,930	48,712	2,218	49,100
Medical supplies and drugs	11,308	10,775	533	10,436
Purchased services and medical fees	16,105	14,764	1,341	12,989
Depreciation and amortization	8,205	8,175	30	8,658
Other operating expense	7,189	7,292	(103)	7,280
Total operating expense	<u>93,737</u>	<u>89,718</u>	<u>4,019</u>	<u>88,463</u>
Operating income	3,124	4,357	(1,233)	7,929
<b>Nonoperating income (expense)</b>				
Noncapital contributions	989	913	76	1,016
Other nonoperating income	(992)	(610)	(382)	(683)
Interest expense	(1,663)	(1,663)	-0-	(1,724)
Investment income	(842)	3,813	(4,655)	7,730
Total nonoperating income (expense)	<u>(2,508)</u>	<u>2,453</u>	<u>(4,961)</u>	<u>6,339</u>
Change in net assets before capital distributions	616	6,810	(6,194)	14,268
<b>Capital distributions</b>	<u>(735)</u>	<u>(857)</u>	<u>122</u>	<u>(503)</u>
Change in net assets	(119)	5,953	(6,072)	13,765
<b>Net assets</b>				
Beginning of year	98,417	92,464	5,953	78,699
End of year	<u>\$ 98,298</u>	<u>\$ 98,417</u>	<u>\$ (119)</u>	<u>\$ 92,464</u>

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

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### SOURCES OF REVENUE

During 2011, the Hospital derived substantially all of its revenue from patient service and other related activities. Revenue includes, among other items, revenue from the Medicare and Medicaid programs, patients, insurance carriers, preferred provider organizations, and managed care programs.

The table below presents the percentages of gross revenue for patient services by payor, for the years ended December 31, 2011 and 2010, respectively.

### PAYOR MIX

	2011	2010	2009
Medicare	49%	47%	46%
Medicaid	8%	8%	8%
Commercial	34%	35%	37%
Self-Pay	7%	7%	7%
Other	2%	3%	2%
	<u>100%</u>	<u>100%</u>	<u>100%</u>

The Hospital provides care to patients under payment arrangement with Medicare, Medicaid, and various managed care programs. Services provided under those arrangements are paid at predetermined rates and/or reimbursable costs as defined. Provisions have been made in the financial statements for contractual adjustments, which represent the difference between the standard charges for services and the actual or estimated payment. It was noted that the payor mix in 2011 shifted from Commercial to Medicare. Disproportionate Share Hospital Payment for years 2011 and 2010 were \$2,060 and \$2,215, respectively.

### OPERATING GAINS

The first component of the overall change in the Hospital's net assets is its operating income, generally the difference between net patient service and the expenses incurred to perform those services. In each of the past two years, the Hospital has reported an operating gain. This is consistent with the Hospital's entire operating history. The Hospital's operations were begun in 1951 as a county owned and operated hospital under Indiana Code 16-22.

The decrease in the Hospital's total operating income in 2011 of \$1,233 or 28.3% from 2010 is the result of a rate and statistical decreases as well as payor mix shifts. During 2011, the Hospital increased gross charge rates 5% compared to 2010 which was increased by 7%.

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

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More importantly, the Hospital experienced statistical changes in the following areas:

<b>Statistical Growth</b>	<b>2011</b>	<b>2010</b>	<b>2011-2010 % Increase / &lt;Decrease&gt;</b>	<b>2009</b>
Patient Days	16,210	19,096	-15.11%	19,814
Diagnostic Imaging Procedures	60,272	62,275	-3.22%	62,069
Laboratory Procedures	310,832	291,089	6.78%	302,965
Pharmaceutical Medication Units	494,915	545,403	-9.26%	1,620,507
Rehab Procedures	75,195	77,815	-3.37%	81,159
Home Health Units of Service	42,496	53,073	-19.93%	55,958
Outpatient Clinic Procedures	14,944	14,482	3.19%	15,373

Excluded from net patient service revenue are charges for patient service waived under the Hospital's uncompensated care policy. Uncompensated care represents unreimbursed charges, both charity care and bad debt, incurred by the Hospital in providing uncompensated care to patients. Based on established rates, gross charges of \$14,726 were waived during 2011. This is an increase of \$460 from the previous year. Management's commitment to provide emergency care for all patients without regard to their ability to pay contributed to this increase.

The Hospital sometimes provides care for patients who have little or no health insurance or other means of repayment. As discussed, this service to the community is consistent with the goals established for the Hospital when it was established in 1951. Because there is no expectation of repayment, charity care is not reported as patient service revenues of the Hospital.

### NON-OPERATING INCOME AND EXPENSES

Non-operating income and expenses are the result of changes in the Hospital's investment income and other non-capital grants and contributions. The Hospital's investment income decreased due to market improvements during 2010 that were not duplicated in 2011. The Hospital's non-operating income and expenses decreased in 2011 by \$4,961 or 202.2% from 2010.

### GRANTS, CONTRIBUTIONS, AND ENDOWMENTS

The Hospital receives operating grants from various state and federal agencies for specific programs. Operating grants received in 2011 totaled \$989 compared to \$913 in 2010. Some of the significant grants received by the Hospital are:

- Tobacco Cessation – From Indiana State Department of Health for prevention of tobacco use

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

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- Rural Health Clinic – Knightstown from Indiana State Department of Health – for rural health clinic operations in Knightstown
- Disaster Preparedness & Bioterrorism– From the State Department of Health – for Hospital disaster preparation and bioterrorism.
- Lifeline patient monitoring - Central Indiana Power – for remote monitoring of home-bound elderly patients
- Education Department – Substance Abuse Prevention
- Critical Needs Expansion – from Hancock Regional Hospital Foundation
- Women’s Health Center
- In Patient Hospice Program – from Hancock Regional Hospital Foundation

### THE HOSPITAL’S CASH FLOWS

Changes in the Hospital’s cash flows are consistent with changes in operating income and non-operating income and expenses as discussed earlier.

### CAPITAL ASSETS AND DEBT ADMINISTRATION

#### CAPITAL ASSETS

During 2011, the Hospital’s net capital assets decreased by approximately \$2,505. This compares to an increase of approximately \$2,703 for 2010 compared to 2009. The change in capital assets is outlined in the following table:

	2011	2010	Change	2009
Land	\$ 270	\$ 270	\$ -0-	\$ 270
Land improvements	5,490	5,489	1	5,217
Buildings and fixed equipment	100,059	105,165	(5,106)	101,060
Major movable equipment	53,042	46,271	6,771	41,290
Construction in progress	1	1,963	(1,962)	2,973
Total capital assets	<u>158,862</u>	<u>159,158</u>	<u>(296)</u>	<u>150,810</u>
Less accumulated depreciation	<u>94,326</u>	<u>92,117</u>	<u>2,209</u>	<u>86,472</u>
Capital assets, net	<u>\$ 64,536</u>	<u>\$ 67,041</u>	<u>\$ (2,505)</u>	<u>\$ 64,338</u>

Capital assets, net decreased as depreciation exceeded the additions/retirements, net activity.

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (MD&A) (UNAUDITED) DECEMBER 31, 2011 AND 2010

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### DEBT

At year-end, the Hospital had \$30.2 million in revenue notes, mortgage loans, and capital lease obligations outstanding. The Indiana Bond Bank issued new debt in June 2004 totaling \$35 million pursuant to a Trust Indenture with the Trustee – the Bank of New York Trust Company. The Hancock County Association was created in 2004 under Indiana Code and is authorized to enter into leases with a county to provide funds to the Hospital. The Association issued the Series 2004 C Qualified Obligations pursuant to a Trust Indenture dated June 1, 2004 between the Association and Trustee. This debt was issued for a new 122,000 square foot hospital expansion with the expanded services in Emergency Medicine, Cardiology and Critical Care and an expansion of space for future health needs of the community. The Board of Trustees of the Hospital and Hancock County, Indiana, acting through its Board of Commissioners are lessees with the Association for the Hospital additions and improvements. The Lessee has agreed to make payments directly to the Trustee in amounts and times sufficient to pay in full, when due, the principal and interest of the Series 2004 C Obligations.

The County and Hospital anticipate that the full lease rental payments will be paid from Hospital Revenues. This debt consists of Revenue Bonds maturing in January 2031. This transaction is further detailed in Note 8.

### CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Hospital Chief Financial Officer's Office, 801 N State Street, Greenfield, IN 46140.

# HANCOCK REGIONAL HOSPITAL

## COMBINED BALANCE SHEETS DECEMBER 31, 2011 AND 2010

### ASSETS

	<u>2011</u>	<u>2010</u>
<b>Current assets</b>		
Cash and cash equivalents	\$ 12,989,596	\$ 14,033,704
Investments	2,010,425	1,727,208
Patient accounts receivable, net	12,796,764	10,085,185
Inventories and other current assets	3,766,032	2,694,620
Total current assets	<u>31,562,817</u>	<u>28,540,717</u>
<b>Assets whose use is limited</b>		
Board designated funds	39,126,852	40,056,110
Trustee held funds for debt service	3,798,191	5,030,178
Donor restricted funds	804,788	693,619
Total assets whose use is limited	<u>43,729,831</u>	<u>45,779,907</u>
<b>Capital assets</b>		
Land and land improvements	5,760,136	5,759,492
Buildings and fixed equipment	100,058,414	105,200,517
Major movable equipment	53,041,760	46,235,397
Construction in progress	915	1,962,525
Total capital assets	<u>158,861,225</u>	<u>159,157,931</u>
Less accumulated depreciation	<u>94,325,652</u>	<u>92,116,529</u>
Capital assets, net	64,535,573	67,041,402
<b>Other assets</b>		
Bond issuance costs, net of accumulated amortization of \$379,834 in 2011 and \$374,703 in 2010	102,611	107,742
Other assets	4,568,347	3,020,185
Total other assets	<u>4,670,958</u>	<u>3,127,927</u>
Total assets	<u>\$ 144,499,179</u>	<u>\$ 144,489,953</u>

# HANCOCK REGIONAL HOSPITAL

## COMBINED BALANCE SHEETS DECEMBER 31, 2011 AND 2010

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### LIABILITIES AND NET ASSETS

	<u>2011</u>	<u>2010</u>
<b>Current liabilities</b>		
Current portion of long-term debt	\$ 960,000	\$ 920,000
Accounts payable and other liabilities	5,117,273	4,463,627
Accrued salaries and related liabilities	6,431,488	5,679,242
Estimated third-party settlements	4,447,679	4,805,456
Total current liabilities	<u>16,956,440</u>	<u>15,868,325</u>
<b>Long-term debt, less current portion</b>	<u>29,245,000</u>	<u>30,205,000</u>
Total liabilities	46,201,440	46,073,325
<b>Net assets</b>		
Unrestricted	56,493,914	53,927,905
Invested in capital assets, net of related debt	34,330,573	35,916,402
Restricted by trustee for debt service	3,798,191	5,030,178
Donor restricted-expendable	804,788	693,619
Net assets before non-controlling interest	<u>95,427,466</u>	<u>95,568,104</u>
Unrestricted - non-controlling interest	<u>2,870,273</u>	<u>2,848,524</u>
Total net assets	<u>98,297,739</u>	<u>98,416,628</u>
Total liabilities and net assets	<u>\$ 144,499,179</u>	<u>\$ 144,489,953</u>

# HANCOCK REGIONAL HOSPITAL

## COMBINED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
<b>Operating revenue</b>		
Net patient service revenue	\$ 89,362,939	\$ 87,626,284
Other operating revenue	7,497,786	6,448,871
Total operating revenue	96,860,725	94,075,155
<b>Operating expenses</b>		
Salaries and wages	39,577,347	38,010,911
Employee benefits	11,353,124	10,701,028
Professional medical fees	1,618,758	1,976,474
Supplies and drugs	11,308,008	10,775,400
Purchased services	14,486,706	12,787,181
Utilities and insurance	2,463,970	2,468,727
Depreciation and amortization	8,204,792	8,175,497
Other	4,724,014	4,823,285
Total operating expenses	93,736,719	89,718,503
Operating income	3,124,006	4,356,652
<b>Nonoperating income (expense), net</b>		
Noncapital contributions	989,259	913,089
Other nonoperating expense	(992,558)	(609,501)
Interest expense	(1,663,357)	(1,663,222)
Investment income (loss)	(841,529)	3,813,037
Total nonoperating income (expense), net	(2,508,185)	2,453,403
Change in net assets before capital distributions	615,821	6,810,055
<b>Capital distributions</b>	(734,710)	(857,345)
Change in net assets	(118,889)	5,952,710
<b>Net assets</b>		
Beginning of year	98,416,628	92,463,918
End of year	\$ 98,297,739	\$ 98,416,628

# HANCOCK REGIONAL HOSPITAL

## COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
<b>Operating activities</b>		
Cash received from patients and third party payors	\$ 86,293,583	\$ 87,609,939
Cash paid to employees for wages and benefits	(50,178,225)	(49,524,680)
Cash paid to vendors for goods and services	(35,019,222)	(32,734,314)
Other operating receipts, net	7,353,616	6,282,488
Net cash from operating activities	<u>8,449,752</u>	<u>11,633,433</u>
<b>Noncapital financing activities</b>		
Noncapital contributions	989,259	913,089
Other nonoperating	(992,558)	(609,501)
Net cash from noncapital financing activities	<u>(3,299)</u>	<u>303,588</u>
<b>Capital and related financing activities</b>		
Acquisition and construction of capital assets	(5,915,575)	(10,959,639)
Loss on disposal of capital assets	410,922	84,535
Capital distributions	(734,710)	(857,345)
Interest paid on long-term debt	(1,663,357)	(1,663,222)
Principal payments on long-term debt	(920,000)	(1,020,000)
Net cash from capital and related financing activities	<u>(8,822,720)</u>	<u>(14,415,671)</u>
<b>Investing activities</b>		
Other assets	(1,548,162)	1,940,922
Investment income	(841,529)	3,813,037
Other changes in assets whose use is limited, net	(2,105,095)	(7,228,523)
Net cash from investing activities	<u>(4,494,786)</u>	<u>(1,474,564)</u>
Net change in cash and cash equivalents	(4,871,053)	(3,953,214)
<b>Cash and cash equivalents</b>		
Beginning of year	21,160,074	25,113,288
End of year	<u>\$ 16,289,021</u>	<u>\$ 21,160,074</u>

# HANCOCK REGIONAL HOSPITAL

## COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2011 AND 2010

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	<u>2011</u>	<u>2010</u>
<b>Reconciliation of operating income to net cash from operating activities</b>		
Operating income	\$ 3,124,006	\$ 4,356,652
Adjustment to reconcile operating income to net cash from operating activities		
Depreciation and amortization	8,204,792	8,175,497
Bad debts	10,157,492	10,155,216
Realized and unrealized gain (loss) on investments	(144,170)	97,486
Changes in assets and liabilities		
Patient accounts receivable	(12,869,071)	(11,004,824)
Other current assets	(1,071,412)	276,291
Accounts payable and other liabilities	653,646	(448,007)
Accrued salaries and related liabilities	752,246	(808,141)
Estimated third-party settlements	(357,777)	833,263
Net cash from operating activities	<u>\$ 8,449,752</u>	<u>\$ 11,633,433</u>
 <b>Reconciliation of cash and cash equivalents to the balance sheets</b>		
Cash and cash equivalents:		
In current assets	\$ 12,989,596	\$ 14,033,704
In investments and assets whose use is limited	<u>3,299,425</u>	<u>7,126,370</u>
Total cash and cash equivalents	<u>\$ 16,289,021</u>	<u>\$ 21,160,074</u>

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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### 1. SIGNIFICANT ACCOUNTING POLICIES

#### Organization and Reporting Entity

Hancock Regional Hospital (HRH) is an acute-care hospital located in Greenfield, Indiana, organized for the purpose of providing healthcare services to the residents of Hancock County and the surrounding communities. Hancock Regional Hospital is a county owned facility operated under the Indiana County Hospital Law, Indiana Code 16-22. The Board of County Commissioners of Hancock County appoints the Governing Board of the Hospital and a financial benefit/burden relationship exists between the County and HRH. For these reasons, HRH is considered a component unit of Hancock County.

In 2004, the Board of County Commissioners of Hancock County, upon written request of the Hancock County Hospital Board of Trustees created the Hancock County Hospital Association. The Association was created pursuant to the provisions of Indiana Code 16-22-6 for the exclusive purpose to provide funds to finance, acquire, renovate, equip and lease land and buildings for HRH.

Accounting principles generally accepted in the United States of America require that these combined financial statements present HRH and its blended component units, collectively referred to as the "Hospital". The component units discussed below are included in HRH's reporting entity because of the significance of their operation or financial relationship with HRH. A blended component unit although a legally separate entity is in substance part of the primary government unit's operations and exists solely or primarily to provide services to or for HRH.

#### Blended Component Units

The accompanying combined financial statements include the accounts of Hancock Regional Hospital Foundation, Inc. (Foundation), a separate not-for-profit entity organized to support the operations of HRH. The accompanying combined financial statements also include the accounts of the Hancock Wellness Center, LLC (Wellness), a separate for-profit entity organized to support the operations of HRH. During 2011, Wellness was dissolved and became a department of HRH. The accompanying combined financial statements also include the accounts of the Blended Component Unit – Hancock Regional Surgery Center, LLC (HRSC), a separate limited liability company. All significant intercompany transactions have been eliminated for financial reporting purposes.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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HRSC was formed for the purpose of owning and operating a multi-specialty ambulatory surgery facility that provides the medical, management and administrative support necessary for licensed physicians to perform non-emergency surgical procedures on an outpatient basis. HRH's membership interest in HRSC is 51%. HRH maintains substantial participation in the operations of HRSC in addition to an economic interest in HRSC's financial position.

The separate financial statements for each of the entities discussed above may be obtained through contacting management of HRH.

### Use of Estimates

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

### Proprietary Fund Accounting

The Hospital utilizes the proprietary fund method of accounting whereby revenue and expenses are recognized on the accrual basis of accounting. Substantially all revenues and expenses are subject to accrual.

### Accounting Standards

Pursuant to Governmental Accounting Standards Board (GASB) Statement Number 20, *Accounting and Financial Reporting For Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

### Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid assets with maturity dates of 90 days or less when purchased with the exception of those included in assets whose use is limited. The Hospital maintains its cash in accounts, which at times, may exceed federally insured limits. The Hospital has not experienced any losses in such accounts. The Hospital believes that it is not exposed to any significant credit risk on cash and cash equivalents.

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# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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### Patient Accounts Receivable and Net Patient Service Revenue

Patient revenues and the related accounts receivable are recorded at the time services to patients are performed. Management estimates an allowance for doubtful accounts receivable based on an evaluation of historical losses, current economic conditions, and other factors unique to the Hospital's customer base.

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

A summary of the payment arrangements with major third-party payors follows.

The Hospital is a provider of services to patients entitled to coverage under Titles XVIII and XIX of the Health Insurance Act (Medicare and Medicaid). The Hospital is reimbursed for Medicare and Medicaid inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG). The Hospital is reimbursed for Medicare and Medicaid outpatient services based on a fixed price per clinical unit of service. Differences between the total program billed charges and the payments received are reflected as deductions from revenue.

Net revenue from the Medicare and Medicaid programs accounted for approximately 44 percent and 12 percent, respectively, of the Hospital's net patient revenue for the year ended 2011, and 42 percent and 12 percent, respectively, of the Hospital's net patient revenue, for the year ended 2010. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

The Hospital recognized revenue related to the Medicaid Disproportionate Share Hospital and the Upper Payment Limitation programs of \$2,060,422 and \$2,214,561 for the years ended December 31, 2011 and 2010, respectively. These amounts are reimbursements for providing care to the uninsured and underinsured.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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

### Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy on a sliding scale on the basis of financial need. Because the Hospital does not pursue collection of approved charity care balances, the charges are not reflected in net revenue. Rather, charges approved for charity are posted to gross revenue and subsequently written off as a charity adjustment before the resulting net patient service revenue.

Of the Hospital's total expenses reported (approximately \$93,700,000 and \$89,700,000 during 2011 and 2010, respectively), an estimated \$2,200,000 and \$2,000,000 arose from providing services to charity patients during 2011 and 2010, respectively. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the Hospital's total expenses (less bad debt expense) divided by gross patient service revenue.

### Combined Statements of Cash Flows

For purposes of the combined statements of cash flows, cash consists of unrestricted cash and cash equivalents that is readily available for use in operations.

### Inventories

Inventories are valued at the lower of cost (first-in, first-out method) or market. Inventory at year-end consists mainly of pharmaceuticals and medical supplies.

### Assets Whose Use is Limited and Investments

Assets whose use is limited include investments designated by HRH's Board for internal purposes, investments and other assets restricted by donors for a specific purpose and investments held by trustees for debt service and continued construction projects.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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Assets whose use is limited and investments consist of U.S. Government securities and mutual funds that are reported at fair value. assets whose use is limited and investments also consist of money market funds and certificates of deposit which are recorded at contract value. Interest, dividends, and gains and losses, both realized and unrealized, are included in nonoperating income when earned.

### Capital Assets and Depreciation

Capital assets such as property and equipment are stated at cost and include expenditures for new additions and other costs added to existing facilities, which exceed \$1,000 and meet certain useful life thresholds. Maintenance, repairs and minor renewals are expensed as incurred. The Hospital provides for depreciation of property and equipment using annual rates, which are sufficient to depreciate the cost of depreciable assets over their estimated useful lives using the straight-line method.

The ranges of useful lives in computing depreciation include the following:

<u>Description</u>	<u>Range of Useful Lives</u>
Land improvements	8-15 years
Buildings and fixed equipment	5-40 years
Major movable equipment	3-20 years

### Costs of Borrowing

Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. No amounts were capitalized as of December 31, 2011 and 2010.

### Bond Issuance Costs

The Hospital provides for the amortization of costs incurred for the issuance of bonds over the life of the debt.

### Income Taxes

HRH is a governmental instrumentality organized under Title 16, Article 12, of the Indiana statutes. HRH is exempt from federal income tax as a unit of local government.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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The Foundation is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (Code) and is exempt from federal and state income taxes on related income pursuant to Section 501(a) of the Code. However, the Foundation is required to file Federal Form 990 – Return of Organization Exempt from Income Tax which is an informational return only.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Hospital and recognize a tax liability if the Hospital has taken an uncertain position that more likely than not would not be sustained upon examination by various federal and state taxing authorities. Management has analyzed the tax positions taken by the Hospital and has concluded that as of December 31, 2011 and 2010, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying combined financial statements. The Hospital is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

Wellness (prior to dissolution) and HRSC are organized as limited liability companies, whereby net taxable income is taxed directly to the members of the limited liability companies. Thus, the combined financial statements do not include any provision for Federal or State income taxes related to these entities.

These entities have filed their federal and state income tax returns for periods through their most recent fiscal year ends. These income tax returns are generally open to examination by the relevant taxing authorities for a period of three years from the later of the date the return was filed or its due date (including approved extensions).

### Advertising and Community Relations

The Hospital records advertising and promotion expense in the period incurred. Total expense for advertising and promotion was \$546,261 and \$371,074 for 2011 and 2010, respectively.

### Compensated Absences

The Hospital's employees earn time off at varying rates depending on years of service. The estimated amount of unused earned time off is reported as a liability in combined financial statements.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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### Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted net assets are expendable noncapital net assets that must be used for a particular purpose, as specified by creditors or donors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

### Donor Restricted Net Assets

Restricted funds include donations to the Foundation that have been restricted by donors for a specific purpose. Generally, these donations are for additions to Hospital property and equipment. Transfers are made to unrestricted funds as expenditures are made in accordance with the donor restrictions.

### Operating Revenues and Expenses

The Hospital's statement of operations 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 which is the Hospital's principal activity. Contributions, investment income, fund development costs and certain other non-healthcare activities are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

### Contributions

From time to time, the Hospital receives contributions from individuals and private organizations. Revenues from contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Contributions may be restricted either for 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.

### 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.

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# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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### Litigation

The Hospital is involved in litigation 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, results from operations, and cash flows.

### Risk Management

The Hospital is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

### Accounting for Non-Controlling Interest

The Hospital has classified the non-controlling interest as a component of net assets in the combined balance sheets. Non-controlling interests represent the portion of the net assets that is attributable to investors that are external to and not included in the Hospital's combined financial statements.

### Reclassification

Certain amounts in the prior year combined financial statements have been reclassified for comparative purposes to conform to the current year presentation. The reclassifications had no effect on the previously reported net assets and change in net assets.

### Subsequent Events

The Hospital evaluated events or transactions occurring subsequent to the combined balance sheet date for recognition and disclosure in the accompanying combined financial statements through the date the combined financial statements are issued which is April 24, 2012.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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### 2. INVESTMENTS AND ASSETS WHOSE USE IS LIMITED

#### Board Designated Funds

The Hospital funds depreciation expense to meet the capital equipment needs of the facility. Depreciation is funded totally, with expenditures for capital equipment and debt principal payments reducing the funded depreciation balance. The Hospital designates other investments to fund specific projects. All interest earned by the funded depreciation and other board designated investment accounts are left to accumulate as an addition to the funds.

#### Donor Restricted Funds

The Hospital has assets, which have been donated for a specific purpose.

#### Trustee Held Assets

The Hospital deposited investments with a trustee, which will be utilized to provide for debt service, and continued construction projects.

The following represents assets whose use is limited and investments as of December 31, 2011 and 2010:

	2011	2010
Board designated funds	\$ 39,126,852	\$ 40,056,110
Donor restricted funds	804,788	693,619
Trustee held assets for debt service	3,798,191	5,030,178
Total assets whose use is limited	43,729,831	45,779,907
Investments	2,010,425	1,727,208
	<u>\$ 45,740,256</u>	<u>\$ 47,507,115</u>
	2011	2010
Mutual funds - equities	\$ 29,185,092	\$ 30,234,303
Mutual funds - fixed income	10,617,046	7,511,929
Certificates of deposit	126,654	122,474
Money market funds	3,299,425	7,126,370
U.S. Government securities	2,512,039	2,512,039
	<u>\$ 45,740,256</u>	<u>\$ 47,507,115</u>

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# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

### 3. DEPOSITS AND INVESTMENTS

Deposits with financial institutions in the State of Indiana at year-end were entirely insured by the Federal Depository Insurance Corporation or by the Indiana Public Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

Investments are carried at fair market value. Net realized gains and losses on security transactions are determined on the specific identification cost basis. Assets whose use is limited investments consist of cash equivalents, mutual funds and U.S. Government securities.

The Hospital's investments generally are reported at fair value, as discussed in Note 1. As of December 31, 2011 and 2010, the Hospital had the following investments and maturities, all of which were held in the Hospital's name by custodial financial institutions that are agents of the Hospital.

December 31, 2011					
	Carrying Amount	Investment Maturities (in years)			
		Less than 1	1-5	6-10	More than 10
Money market funds	\$ 3,299,425	\$ 3,299,425	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit	126,654	97,004	29,650	-0-	-0-
Mutual funds - equities	29,185,092	29,185,092	-0-	-0-	-0-
Mutual funds - fixed income	10,617,046	10,617,046	-0-	-0-	-0-
U.S. Government securities	2,512,039	-0-	-0-	-0-	2,512,039
	<u>\$ 45,740,256</u>	<u>\$ 43,198,567</u>	<u>\$ 29,650</u>	<u>\$ -0-</u>	<u>\$ 2,512,039</u>

December 31, 2010					
	Carrying Amount	Investment Maturities (in years)			
		Less than 1	1-5	6-10	More than 10
Money market funds	\$ 7,126,370	\$ 7,126,370	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit	122,474	63,268	59,206	-0-	-0-
Mutual funds - equities	30,234,303	30,234,303	-0-	-0-	-0-
Mutual funds - fixed income	7,511,929	7,511,929	-0-	-0-	-0-
U.S. Government securities	2,512,039	-0-	-0-	-0-	2,512,039
	<u>\$ 47,507,115</u>	<u>\$ 44,935,870</u>	<u>\$ 59,206</u>	<u>\$ -0-</u>	<u>\$ 2,512,039</u>

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

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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*Credit risk* - Statutes authorize the Hospital to invest in interest bearing deposit accounts, passbook savings accounts, certificates of deposit, money market accounts, mutual funds, pooled fund investments, securities backed by the full faith and credit of the United States Treasury and repurchase agreements. The statutes require that repurchase agreements be fully collateralized by U.S. Government or U.S. Government Agency obligations.

*Concentration of credit risk* - The Hospital places no limit on the amount it may invest in any one issuer. The Hospital maintains its investments, which at times may exceed federally insured limits. The Hospital has not experienced any losses in such accounts. The Hospital believes that it is not exposed to any significant credit risk on investments.

Deposits and investments consist of the following as of December 31, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Carrying amount		
Deposits	\$ 12,989,596	\$ 14,033,704
Investments	45,740,256	47,507,115
	<u>\$ 58,729,852</u>	<u>\$ 61,540,819</u>
Included in the balance sheet captions		
Cash and cash equivalents	\$ 12,989,596	\$ 14,033,704
Investments	2,010,425	1,727,208
Board designated funds	39,126,852	40,056,110
Trustee held funds, less current portion	3,798,191	5,030,178
Donor restricted funds	804,788	693,619
	<u>\$ 58,729,852</u>	<u>\$ 61,540,819</u>

#### 4. FAIR VALUE MEASUREMENTS

During 2011, the Hospital changed its accounting policies to expand the level of detail provided on investments by disaggregating mutual funds by investment objective. The change was made to adopt Financial Accounting Standards Board's Accounting Standards Update No. 2010-06, Fair Value Measurements and Disclosures (Topic 820) - Improving Disclosures about Fair Value Measurements. Accordingly, the accounting change has been retrospectively applied to prior periods presented as if the policy had always been used. The Hospital's investments are reported at fair value in the accompanying combined balance sheets.

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# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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Fair value is defined as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction value hierarchy, which requires an entity to maximize the use of observable inputs when measuring fair value.

The following provides a description of the three levels of inputs that may be used to measure fair value under the standard, the types of the Hospital's investments that fall under each category and the valuation methodologies used to measure these investments at fair value.

### Level 1 Fair Value Measurements

Inputs to the valuation methodology are quoted prices available in the active markets for identical investments as of the reporting date.

The fair value of mutual funds is based on quoted net asset values of the shares held by the Hospital at year-end. The net asset value is based on the value of the underlying assets owned by the fund, minus its liabilities and then divided by the number of shares outstanding. The net asset value is quoted in an active market.

The fair value of U.S. Government securities is based on the closing price reported in the active market in which the individual security is traded.

### Level 2 Fair Value Measurements

Inputs to the valuation methodology are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date and fair value can be determined through the use of models or other valuation methodologies.

### Level 3 Fair Value Measurements

Inputs to the valuation methodology are unobservable inputs in situations where there is little or no market activity for the asset or liability and the reporting entity makes estimates and assumptions related to the pricing of the asset or liability including assumptions regarding risk.

The preceding methods used to measure fair value may produce an amount that may not be indicative of net realizable value or reflective of future fair values.

Furthermore, although the Hospital believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2011 and 2010 are as follows:

	December 31, 2011			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Investments and assets whose use is limited				
Mutual funds - equities				
Large blend	\$ 9,783,125	\$ 9,783,125	\$ -0-	\$ -0-
Large growth	2,435,490	2,435,490	-0-	-0-
Large value	928,451	928,451	-0-	-0-
Medium blend	4,891,854	4,891,854	-0-	-0-
Small growth	1,085,379	1,085,379	-0-	-0-
Small value	1,054,054	1,054,054	-0-	-0-
Other (global, commodities, institutional and index)	9,006,739	9,006,739	-0-	-0-
Total mutual funds - equities	29,185,092	29,185,092	-0-	-0-
Mutual funds - fixed income				
Intermediate term bond	5,661,246	5,661,246	-0-	-0-
Ultrashort bond	1,565,714	1,565,714	-0-	-0-
Short-term bond	3,390,086	3,390,086	-0-	-0-
Total mutual funds - fixed income	10,617,046	10,617,046	-0-	-0-
U.S. Government securities	2,512,039	2,512,039	-0-	-0-
		<u>\$ 42,314,177</u>	<u>\$ -0-</u>	<u>\$ -0-</u>
Cash and equivalents	3,299,425			
Certificate of deposit	126,654			
	<u>\$ 45,740,256</u>			
	December 31, 2010			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Investments and assets whose use is limited				
Mutual funds - equities				
Large blend	\$ 10,207,081	\$ 10,207,081	\$ -0-	\$ -0-
Large growth	2,500,061	2,500,061	-0-	-0-
Large value	961,768	961,768	-0-	-0-
Medium blend	5,079,044	5,079,044	-0-	-0-
Small growth	1,128,462	1,128,462	-0-	-0-
Small value	1,096,730	1,096,730	-0-	-0-
Other (global, commodities, institutional and index)	9,261,157	9,261,157	-0-	-0-
Total mutual funds - equities	30,234,303	30,234,303	-0-	-0-
Mutual funds - fixed income				
Intermediate term bond	5,175,954	5,175,954	-0-	-0-
Short-term bond	2,335,975	2,335,975	-0-	-0-
Total mutual funds - fixed income	7,511,929	7,511,929	-0-	-0-
U.S. Government securities	2,512,039	2,512,039	-0-	-0-
		<u>\$ 40,258,271</u>	<u>\$ -0-</u>	<u>\$ -0-</u>
Cash and equivalents	7,126,370			
Certificate of deposit	122,474			
	<u>\$ 47,507,115</u>			

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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

Cash and cash equivalents, patient accounts receivable, assets whose use is limited, accounts payable, other current liabilities, salaries, wages and related liabilities and estimated third-party settlements: The carrying amount reported in the combined balance sheet for cash and cash equivalents, patient accounts receivable, accounts payable, other current liabilities, salaries, wages and related liabilities and estimated third-party settlements approximate fair value based on short-term maturities.

Long-term debt: Fair value of the Hospital's fixed rate revenue bonds is estimated using discounted cash flows based on current fixed rates available to similar entities with similar credit ratings. As of December 31, 2011 and 2010, the carrying value of the fixed rate long-term debt was \$30,205,000 and \$31,125,000, with a fair value of approximately \$31,854,242 and \$31,124,746, respectively.

### 5. ACCOUNTS RECEIVABLE AND PAYABLE

Patient accounts receivable and accounts payable (including expenses) reported as current assets and liabilities as of December 31, 2011 and 2010 is as follows:

	2011	2010
Patient accounts receivable		
Receivable from patients and their insurance carriers	\$ 22,098,765	\$ 18,250,198
Receivable from Medicare	15,796,040	11,196,269
Receivable from Medicaid	2,390,907	3,057,175
Total patient accounts receivable	40,285,712	32,503,642
Less contractual allowances	(17,975,959)	(14,629,784)
Less allowance for uncollectible amounts	(9,512,989)	(7,788,673)
Patient accounts receivable, net	<u>\$ 12,796,764</u>	<u>\$ 10,085,185</u>
Accounts payable and accrued expenses		
Payable to employees (including payroll taxes and benefits)	\$ 6,431,488	\$ 5,679,242
Payable to suppliers and other accrued expenses	5,117,273	4,463,627
Total accounts payable and accrued expenses	<u>\$ 11,548,761</u>	<u>\$ 10,142,869</u>

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

### 6. INVESTMENTS IN AFFILIATES

HRH owns 50% of Hancock Health Network, LLC (Network) and has recorded the investment on the equity method of accounting in the amount of \$1,064,860 and \$1,101,912 as of December 31, 2011 and 2010, respectively. This investment is included within other assets in the combined financial statements. HRH paid physicians approximately \$1,147,000 and \$640,000 during 2011 and 2010, respectively for management and other operating expenses. HRH received \$880,000 and \$817,000 for 2011 and 2010, respectively from the Network for rental and housecleaning income. HRH contributed capital of \$2,436,000 and \$2,109,000 to the Network during 2011 and 2010, respectively.

HRH has a receivable from the Network of \$229,000 and \$35,000 as of December 31, 2011 and 2010, respectively. The Hospital has a payable to the Network of \$287,000 and \$40,000 as of December 31, 2011 and 2010, respectively. HRH expects to continue providing capital contributions to the Network at a commensurate level with its past experience.

HRH also owns 50% of a Physician Hospital Organization (PHO) and approximately 37% of Parkway, LLC. HRH has recorded these investments in affiliates on the equity method of accounting within other assets in the combined financial statements. Investments in PHO and Parkway, LLC are immaterial to the combined financial statements.

### 7. CAPITAL ASSETS

Capital assets consist of the following as of December 31, 2011 and 2010:

	Balance December 31, 2010	Additions	Retirements	Transfers	Balance December 31, 2011
Land	\$ 270,285	\$ -0-	\$ -0-	\$ -0-	\$ 270,285
Land improvements	5,489,207	-0-	-0-	644	5,489,851
Buildings and fixed equipment	105,200,517	1,070,178	(6,212,281)	-0-	100,058,414
Major movable equipment	46,235,397	4,675,756	-0-	2,130,607	53,041,760
Construction in progress	1,962,525	169,641	-0-	(2,131,251)	915
Total capital assets	<u>159,157,931</u>	<u>5,915,575</u>	<u>(6,212,281)</u>	<u>-0-</u>	<u>158,861,225</u>
Less accumulated depreciation					
Land improvements	(3,096,342)	(378,136)	-0-	-0-	(3,474,478)
Buildings and fixed equipment	(54,366,833)	(4,423,297)	5,801,359	-0-	(52,988,771)
Major movable equipment	(34,653,354)	(3,209,049)	-0-	-0-	(37,862,403)
Total accumulated depreciation	<u>(92,116,529)</u>	<u>(8,010,482)</u>	<u>5,801,359</u>	<u>-0-</u>	<u>(94,325,652)</u>
Capital assets, net	<u>\$ 67,041,402</u>	<u>\$ (2,094,907)</u>	<u>\$ (410,922)</u>	<u>\$ -0-</u>	<u>\$ 64,535,573</u>

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

	Balance December 31, 2009	Additions	Retirements	Transfers	Balance December 31, 2010
Land	\$ 270,285	\$ -0-	\$ -0-	\$ -0-	\$ 270,285
Land improvements	5,216,743	-0-	-0-	272,464	5,489,207
Buildings and fixed equipment	101,094,972	635,657	-0-	3,469,888	105,200,517
Major movable equipment	41,254,792	2,897,045	(2,611,482)	4,695,042	46,235,397
Construction in progress	2,972,982	7,426,937	-0-	(8,437,394)	1,962,525
Total capital assets	150,809,774	10,959,639	(2,611,482)	-0-	159,157,931
Less accumulated depreciation					
Land improvements	(2,717,909)	(378,433)	-0-	-0-	(3,096,342)
Buildings and fixed equipment	(49,996,154)	(4,370,679)	-0-	-0-	(54,366,833)
Major movable equipment	(33,758,112)	(3,422,189)	2,526,947	-0-	(34,653,354)
Total accumulated depreciation	(86,472,175)	(8,171,301)	2,526,947	-0-	(92,116,529)
Capital assets, net	<u>\$ 64,337,599</u>	<u>\$ 2,788,338</u>	<u>\$ (84,535)</u>	<u>\$ -0-</u>	<u>\$ 67,041,402</u>

### 8. LONG-TERM DEBT

The Indiana Bond Bank (the "Bond Bank") issued Special Program Bonds, Series 2004 C (Hancock Memorial Hospital and Health Services Project) on June 1, 2004 pursuant to the provisions of a Trust Indenture with the Trustee, the Bank of New York Trust Company, NA, Indianapolis, Indiana in the aggregate principal amount of \$35,010,000.

The Bond Bank is the obligor to the bondholders. The bonds are insured. The proceeds from the sale of the Series 2004 C Bonds were used to provide funds to (a) purchase Series 2004 C Qualified Obligations in the amount of \$34,475,000, (b) provide a credit facility for the Debt Service Reserve fund, (c) pay a portion of the interest on the Series 2004 C Bonds, (d) pay the premium for bond insurance, and (e) pay all of the Costs of Issuance of the Series 2004 C Bonds, including the underwriters discount.

The Hancock County Hospital Association (the "Association") was created in 2004 under the Indiana Code and is authorized to enter into leases with a county in order to provide funds to finance, acquire, renovate, equip and lease land and buildings. The Association issued the Series 2004 C Qualified Obligations pursuant to a Trust Indenture dated June 1, 2004 between the Association and the Trustee.

The net proceeds from the Series 2004 C Qualified Obligations were used for Hospital additions and improvements, which will include a new Emergency Department, Intensive Care and Cardiac Care Center and expansion of space for future hospital and healthcare needs.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The Board of Trustees of the Hospital and Hancock County, Indiana, acting through its Board of Commissioners are lessees (collectively, the "Lessee") under a lease agreement dated April 1, 2004 (the "Lease") with the Association (the "Lessor") for the Hospital additions and improvements (the "Leased Premises").

Pursuant to the Lease, the Lessee has agreed to make payments directly to the Trustee in such amounts and at such times as are sufficient to pay in full, when due, the principal and interest of the Series 2004 C Obligations. The County and the Hospital anticipate that the full lease rental payments will be paid from Hospital revenues.

The Series 2004 C Obligations and the Lease have essentially the same terms with interest rates ranging from 2.94% to 5.52% to be paid semi-annually on January 15 and July 15 through January 15, 2031. The Trust Indenture has certain compliance requirements for which management believes it is in compliance. The lease rental revenues are pledged to secure the Series 2004 C obligations.

Long-term debt as of December 31, 2011 and 2010 includes the following:

	Balance December 31, 2010	Additions	Reductions	Balance December 31, 2011	Current Portion	Long-Term Portion
The Series 2004 C Obligations Capital Lease	\$ 31,125,000	\$ -0-	\$ (920,000)	\$ 30,205,000	\$ 960,000	\$ 29,245,000
	Balance December 31, 2009	Additions	Reductions	Balance December 31, 2010	Current Portion	Long-Term Portion
The Series 2004 C Obligations Capital Lease	\$ 32,005,000	\$ -0-	\$ (880,000)	\$ 31,125,000	\$ 920,000	\$ 30,205,000
Surgery Center Investor Buyouts	140,000	-0-	(140,000)	-0-	-0-	-0-
Total long-term debt	\$ 32,145,000	\$ -0-	\$ (1,020,000)	\$ 31,125,000	\$ 920,000	\$ 30,205,000

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Aggregate maturities of long-term debt are as follows:

Year Ending December 31,	Principal	Interest	Total
2012	\$ 960,000	\$ 1,552,271	\$ 2,512,271
2013	1,000,000	1,511,015	2,511,015
2014	1,040,000	1,466,593	2,506,593
2015	1,090,000	1,418,987	2,508,987
2016	1,140,000	1,368,015	2,508,015
2017-2021	6,595,000	5,944,188	12,539,188
2022-2026	8,505,000	4,029,262	12,534,262
2027-2031	9,875,000	1,410,357	11,285,357
	<u>\$ 30,205,000</u>	<u>\$ 18,700,688</u>	<u>\$ 48,905,688</u>

### 9. PATIENT SERVICE REVENUE

Patient service revenue for 2011 and 2010 consists of the following:

	2011	2010
Inpatient	\$ 57,637,724	\$ 57,746,447
Outpatient	132,997,609	118,771,274
Transitional Care/Inpatient Rehabilitation	4,124,796	5,211,934
Geriatric Psychiatric	4,019,960	4,478,910
Gross patient service revenue	<u>198,780,089</u>	<u>186,208,565</u>
Contractual allowance	94,690,907	84,315,782
Bad debts	10,157,492	10,155,216
Charity care	4,568,751	4,111,283
Deductions from revenue	<u>109,417,150</u>	<u>98,582,281</u>
Net patient service revenue	<u>\$ 89,362,939</u>	<u>\$ 87,626,284</u>

### 10. PENSION PLAN

The Hospital offers a defined contribution plan that covers all employees who meet eligibility requirements as to age and length of service and who elect to participate. The Hospital matches 50% of the employee contribution up to 4% of the eligible wages. Pension expense related to the defined contribution plan was \$1,262,872 and \$1,230,173 in 2011 and 2010, respectively.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

### 11. CONCENTRATION OF CREDIT RISK

The Hospital is located in Greenfield, Indiana. The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The mix of gross patient accounts receivable and gross revenue from patients and third-party payors at December 31 was as follows:

	Receivables		Revenue	
	2011	2010	2011	2010
Medicare	39%	35%	49%	47%
Medicaid	6%	9%	8%	8%
Commercial	29%	31%	34%	35%
Self pay and other	26%	25%	9%	10%
	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

### 12. ACCOUNTING FOR NON-CONTROLLING INTEREST

The following depicts the changes in combined net assets attributable to the controlling financial interest of the Hospital and the non-controlling interest as of December 31, 2011 and 2010:

	Controlling interest	Non-controlling interest	Total
<b>Net asset balances</b>			
December 31, 2009	\$ 89,148,538	\$ 3,315,380	\$ 92,463,918
Change in net assets before capital distributions	6,419,566	390,489	6,810,055
Capital distributions	-0-	(857,345)	(857,345)
Change in net assets	<u>6,419,566</u>	<u>(466,856)</u>	<u>5,952,710</u>
December 31, 2010	95,568,104	2,848,524	98,416,628
Change in net assets before capital distributions	(140,638)	756,459	615,821
Capital distributions	-0-	(734,710)	(734,710)
Change in net assets	<u>(140,638)</u>	<u>21,749</u>	<u>(118,889)</u>
December 31, 2011	<u>\$ 95,427,466</u>	<u>\$ 2,870,273</u>	<u>\$ 98,297,739</u>

### 13. SELF-INSURED HEALTH CLAIMS PROGRAM AND OTHER POSTEMPLOYMENT BENEFITS

The Hospital is self-insured for employee health claims. A third party administrator processes the claims for the Hospital. The Hospital maintains an estimated liability for the amount of claims incurred but not reported.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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The Hospital maintains reinsurance including a stop loss for specific incident claims over \$225,000 and an employee lifetime maximum of \$1,775,000. Substantially all employees are covered for major medical benefits. The total health claims expense was \$6,949,383 and \$6,368,712 for 2011 and 2010, respectively.

Claim expenditures and liabilities 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. The Hospital has recorded the accrual for the unpaid claims estimate within accrued salaries and related liabilities on the combined financial statements.

Changes in the accrual for unpaid claims for 2011 and 2010 are as follows:

	2011	2010
Unpaid claims estimate, beginning of year	\$ 659,251	\$ 541,543
Incurred claims and changes in estimates	6,949,383	6,368,712
Claims payments	<u>(6,961,470)</u>	<u>(6,251,004)</u>
Unpaid claims estimate, end of year	<u>\$ 647,164</u>	<u>\$ 659,251</u>

As a component of the self-insured employee health program the Hospital provides for continued coverage of medical benefits for eligible retired employees and their beneficiaries. To be eligible for postemployment healthcare benefits, the employees must retire in good standing after the age of fifty-nine and one half with at least ten years of continuous service and must continue to make the stipulated required employee contributions. The coverage may be continued under the same health plan option as was enrolled in at the time of retirement through December 31<sup>st</sup> of that year. Beginning the following January 1<sup>st</sup> and all subsequent years of eligible retirement, coverage the retiree is only eligible for the high deductible plan option. Coverage generally terminates at the date the retiree becomes Medicare eligible.

As of December 31, 2011, the most recent actuarial valuation date, this plan was not funded. The Hospital provides funding for expenditures on a pay-as-you-go basis. 2011 was the first year the plan had an actuarial valuation performed. The unfunded actuarial accrued liability for benefits was approximately \$1,671,000 as of December 31, 2011. The unfunded accrued liability estimated by the Hospital was \$1,419,000 as of December 31, 2010. These liabilities are included in the combined balance sheets within the accrued salaries and related liabilities.

The covered payroll (annual payroll of active employees covered by the plan) was approximately \$23.9 million, and the ratio of the unfunded actuarial accrued liability to the covered payroll was 7 percent at December 31, 2011. The estimated annual required employer contribution and employer annual benefit approximate \$500,000.

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# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2011 actuarial valuation, the projected unit credit cost method was used. The significant applicable assumptions utilized in calculating the estimated obligation under the retiree continuance of coverage provision for 2011 include a healthcare cost trend rate of 10%, a premium growth rate of 10%, a discount rate of 4.5% and average years to termination of benefits of 9 years. The plan does not issue a separate report.

### 14. COMMITMENTS AND CONTINGENCIES

#### Malpractice Insurance

The Indiana Medical Malpractice Act, IC 27-12 (the Act), provides a recovery for an occurrence of malpractice and for any injury or death of a patient due to an act of malpractice in excess of certain thresholds. The Act requires the Hospital to maintain medical malpractice liability insurance on a per occurrence basis and in the annual aggregate for amounts below the thresholds of the Act. During 2001, the Hospital's malpractice carrier filed bankruptcy. The Hospital has obtained malpractice coverage through another carrier.

The Hospital may be liable for certain pending claims incurred while with the former carrier. Management is not aware of any related material adverse effects to its financial position, results of operations, and cash flows. Prior to July 1, 1999, the Indiana Medical Malpractice Act provided for a maximum recovery of \$750,000 per occurrence (\$3,000,000 annual aggregate) for professional liability, \$100,000 of which would be paid through the Hospital's malpractice insurance coverage and the balance would be paid by the State of Indiana Patient Compensation Fund.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

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For claims on or after July 1, 1999, the Indiana Medical Malpractice Act provides for a maximum recovery of \$1,250,000 per occurrence (\$7,500,000 annual aggregate) with the first \$250,000 covered by the Hospital's insurance and the remainder by the Fund.

The Hospital is a member in a captive insurance company, Suburban Health Organization Segregated Portfolio Company, LLC, to fund the Hospital's required portion of the professional and physician insurance coverage pursuant to the Act as well as its general liability insurance and excess coverage.

### 15. SUBSEQUENT EVENTS

#### Management Agreement

Subsequent to December 31, 2011, HRH entered into an agreement with a distinct lessor entity to lease a long-term care facility operated by a related management company. Additionally, HRH entered into an agreement with the related management company to manage the leased long-term care facility. As part of the agreement, HRH will pay the management company a fee to continue managing the long-term care facility on behalf of HRH in accordance with the terms of the agreement. While the lease is in effect, the performance of all activities of the management company shall be on behalf of HRH. Furthermore, HRH retains ultimate authority and legal responsibility for the operation and control of the long-term care facility.

Under the agreement, all gross patient revenues from the operation of the long-term care facility will be the property of HRH and HRH shall be responsible for all operating expenses and working capital requirements. The agreements expire on January 31, 2013 and are automatically extended for successive terms of two years unless appropriately terminated. All parties involved can terminate the agreements without cause with 90 days written notice.

#### Joint Venture

During 2012, HRH entered into an operating agreement with National Green Gas, LLC to form O3PureMed, LLC (Company). HRH is a 75% owner of the Company. The Company has been formed primarily for the purpose of operating a medical and infectious waste treatment facility.