



**STATE OF INDIANA**  
AN EQUAL OPPORTUNITY EMPLOYER

B42742

---

STATE BOARD OF ACCOUNTS  
302 WEST WASHINGTON STREET  
ROOM E418  
INDIANAPOLIS, INDIANA 46204-2765

Telephone: (317) 232-2513  
Fax: (317) 232-4711  
Web Site: [www.in.gov/sboa](http://www.in.gov/sboa)

October 2, 2013

Board of Directors  
Floyd Memorial Hospital and Health Services  
1850 State Street  
New Albany, IN 47150

We have reviewed the audit report prepared by BKD, LLP, Independent Public Accountants, for the period January 1, 2012 to December 31, 2012. 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 Floyd Memorial Hospital and Health Services, as of December 31, 2012 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

**Floyd Memorial Hospital and Health Services  
A Component Unit of Floyd County, Indiana**

Auditor's Report and Financial Statements

December 31, 2012 and 2011



**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**  
December 31, 2012 and 2011

**Contents**

<b>Independent Auditor’s Report on Financial Statements and Supplementary Information.....</b>	<b>1</b>
<b>Management’s Discussion and Analysis .....</b>	<b>3</b>
<b>Financial Statements</b>	
Balance Sheets.....	9
Statements of Revenues, Expenses and Changes in Net Position .....	10
Statements of Cash Flows .....	11
Notes to Financial Statements .....	12
<b>Supplementary Information</b>	
Schedule of Funding Progress .....	38

## **Independent Auditor's Report on Financial Statements and Supplementary Information**

Board of Trustees  
Floyd Memorial Hospital and Health Services  
New Albany, Indiana

We have audited the accompanying financial statements of Floyd Memorial Hospital and Health Services (Hospital), a component unit of Floyd County, Indiana, which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended and the related notes to the financial statements.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Hospital's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of December 31, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of a Matter***

As discussed in Note 1 to the financial statements, in 2012, the Hospital changed its method of accounting for GASB No. 65. Our opinion is not modified with respect to this matter.

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that management's discussion and analysis and pension information listed in the table of contents be presented to supplement the basic financial statements. Such information, although not 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 audits 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.

*BKD, LLP*

Louisville, Kentucky  
March 22, 2013

# **Floyd Memorial Hospital and Health Services**

## **A Component Unit of Floyd County, Indiana**

### **Management's Discussion and Analysis**

### **Years Ended December 31, 2012 and 2011**

#### **Introduction**

This management's discussion and analysis of the financial performance of Floyd Memorial Hospital and Health Services (Hospital) provides an overview of the Hospital's financial activities for the years ended December 31, 2012, 2011 and 2010. It should be read in conjunction with the accompanying financial statements of the Hospital.

#### **Financial Highlights**

- Cash and investments, excluding amounts held by trustee for debt service, increased by \$13,189,929, or 15.1% in 2012 as compared to 2011 and decreased by \$1,725,442, or 1.9% in 2011 as compared to 2010.
- The Hospital's net position increased in the past year by \$10,639,339, or 8.3% as compared to 2011 when the Hospital's net position increased by \$1,190,260, or 0.9%.
- The Hospital reported operating gains in 2012 of \$11,921,267, or 4.5% of total operating revenues versus \$4,148,435, or 1.9% of total operating revenues in 2011 and \$5,516,200, or 2.6% of total operating revenues in 2010.
- Net nonoperating revenues increased by \$1,753,257 in 2012 as compared to 2011 and decreased \$1,988,300 in 2011 as compared to 2010.
- Days cash on hand decreased to 152 in 2012 from 156 in 2011 and 169 in 2010.
- Debt service coverage ratio improved to 3.2 in 2012 from 2.3 in 2011 and from 2.6 in 2010.

#### **Using This Annual Report**

The Hospital's financial statements consist of three statements — a balance sheet, statement of revenues, expenses and changes in net position and statement of cash flows. These statements provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by creditors, contributors, grantors or enabling legislation. The Hospital reports as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

#### **The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Position**

The balance sheet and the statement of revenues, expenses and changes in net position report information about the Hospital's resources and activities for purposes of illustrating the effects of the past year's activity on the financial health of the Hospital. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. As the Hospital uses the accrual basis of accounting, current year's revenues and expenses are taken into account regardless of when cash is received or paid.

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Management's Discussion and Analysis Years Ended December 31, 2012 and 2011

The Hospital's total net position — the difference between assets and liabilities — is one measure of the Hospital's financial health or financial position. Over time, increases or decreases in the Hospital's net position are an indicator of whether its financial health is improving or deteriorating. Other nonfinancial factors, such as changes in the Hospital's patient base, changes in legislation and regulations, measures of the quantity and quality of services provided to its patients and local economic factors should also be considered to assess the overall financial health of the Hospital.

### The Statement of Cash Flows

The statement of cash flows reports cash receipts, cash payments and net changes in cash and cash equivalents resulting from four defined types of activities. The statement of cash flows illustrates the uses and sources of cash for the year.

### The Hospital's Net Position

The Hospital's net position is the difference between assets and liabilities reported in the balance sheet. The Hospital's net position increased by \$10,639,339, or 8.3% in 2012 versus 2011 and by \$1,190,260, or 0.9% in 2011 versus 2010, as shown in Table 1.

**Table 1: Balance Sheets Summary**

	2012	Restated	
		2011	2010
<b>Assets</b>			
Patient accounts receivable, net	\$ 33,096,166	\$ 30,844,211	\$ 26,885,624
Other current assets	40,631,501	30,603,533	31,450,765
Capital assets, net	119,793,616	121,207,755	122,675,037
Other noncurrent assets	83,760,137	81,117,071	79,208,200
Total assets	277,281,420	263,772,570	260,219,626
<b>Deferred Outflows of Resources</b>			
Total assets and deferred outflows of resources	19,409,774	19,394,359	6,103,182
	<u>\$ 296,691,194</u>	<u>\$ 283,166,929</u>	<u>\$ 266,322,808</u>
<b>Liabilities</b>			
Long-term debt	\$ 98,695,163	\$ 101,915,288	\$ 92,418,394
Other current and noncurrent liabilities	48,729,799	43,137,493	41,267,523
Fair value of interest rate swap agreement	10,118,289	10,390,179	6,103,182
Total liabilities	157,543,251	155,442,960	139,789,099
<b>Deferred Inflows of Resources</b>			
	784,635	-	-

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Management's Discussion and Analysis Years Ended December 31, 2012 and 2011

	2012	Restated	
		2011	2010
<b>Net Position</b>			
Net investment in capital assets	\$ 25,835,030	\$ 24,676,193	27,745,057
Restricted	6,177,966	6,368,844	7,189,238
Unrestricted	<u>106,350,312</u>	<u>96,678,932</u>	<u>91,599,414</u>
Total net position	<u>138,363,308</u>	<u>127,723,969</u>	<u>126,533,709</u>
 Total liabilities, deferred inflows of resources and net position	 <u>\$ 296,691,194</u>	 <u>\$ 283,166,929</u>	 <u>\$ 266,322,808</u>

Total assets increased \$13,508,850, or 5.1%, in 2012 compared to 2011. This is primarily due to an increase in cash and cash equivalents of \$10,431,669 from 2011. Patient accounts receivable increased by \$2,251,955, or 7.3% from 2011 to 2012, and increased \$3,958,587, or 14.7% from 2010 to 2011.

### Operating Results and Changes in the Hospital's Net Position

The Hospital's net position increased by \$10,639,339, or 8.3% in 2012 compared to an increase of \$1,190,260, or 0.9% in 2011. This increase is made up of several components as shown in Table 2.

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

	2012	Restated	
		2011	2010
<b>Operating Revenues</b>			
Net patient service revenue	\$ 259,113,591	\$ 217,252,137	\$ 206,270,477
Other operating revenues	<u>7,891,379</u>	<u>3,210,524</u>	<u>2,853,863</u>
Total operating revenues	<u>267,004,970</u>	<u>220,462,661</u>	<u>209,124,340</u>
<b>Operating Expenses</b>			
Salaries and wages and employee benefits	125,591,909	113,462,376	103,589,346
Purchased services and professional fees	46,624,334	25,235,979	24,886,596
Depreciation and amortization	11,606,306	11,309,458	11,539,502
Other operating expenses	<u>71,261,154</u>	<u>66,306,413</u>	<u>63,592,696</u>
Total operating expenses	<u>255,083,703</u>	<u>216,314,226</u>	<u>203,608,140</u>
<b>Operating Income</b>	<u>11,921,267</u>	<u>4,148,435</u>	<u>5,516,200</u>

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Management's Discussion and Analysis Years Ended December 31, 2012 and 2011

	2012	Restated	
		2011	2010
<b>Nonoperating Revenues (Expenses)</b>			
Investment income	\$ 2,795,376	\$ 444,919	\$ 1,900,812
Noncapital grants and contributions	690,095	307,060	392,997
Interest expense	(5,311,716)	(5,108,807)	(4,859,949)
Other nonoperating revenues and expenses, net	491,874	1,269,200	1,466,812
Total nonoperating revenues (expenses)	<u>(1,334,371)</u>	<u>(3,087,628)</u>	<u>(1,099,328)</u>
<b>Capital Grants</b>			
Capital grants	52,443	129,453	21,275
Total capital grants	<u>52,443</u>	<u>129,453</u>	<u>21,275</u>
<b>Change in Net Position</b>	<u>\$ 10,639,339</u>	<u>\$ 1,190,260</u>	<u>\$ 4,438,147</u>

### Operating Income (Loss)

The first component of the overall change in the Hospital's net position is its operating income or loss, identified as the difference between net patient service and other operating revenues and the expenses incurred to perform those services.

The operating income for 2012 was \$11,921,267 as compared to an operating income of \$4,148,435 for 2011 and \$5,516,200 for 2010. The primary components of change in operating results are:

- An increase in net patient service revenue of \$41,861,454, or 19.3% in 2012 due to a 1.7% increase in inpatient discharges and a 14.5% increase in outpatient visits. Additionally, the state of Indiana implemented a methodology change in Medicaid reimbursement in June 2012 retroactive to state fiscal year beginning July 2011 resulting in increased net revenue. In 2008, the Hospital implemented revenue cycle initiatives to identify net patient service revenue enhancement opportunities. These initiatives yielded increases in net patient revenue of \$6,300,000 in 2012 and \$9,300,000 in 2011.
- An increase in salaries and benefits of \$12,129,533, or 10.7% in 2012 as compared to an increase of \$9,873,030, or 9.5% in 2011. The increase resulted from additional Hospital volume, the acquisition of physician practices and entering into a long-term care venture.
- An increase in supply and drug costs of \$3,120,176, or 6.0% in 2012 and \$807,549, or 1.6% in 2011. The increases in 2012 and 2011 were the result of increased volume.
- An increase in depreciation and amortization of \$296,848, or 2.6% in 2012 and a decrease of \$230,044, or 2.0% in 2011.

Full-time equivalent employees increased to 1,906 in 2012, or 11.5% from 1,710 in 2011 and 1,607, or 6.4% in 2010. The 2012 and 2011 increases are primarily due to the addition of staff as a result of increases in hospital volume, as well as the acquisition of physician practices and the 2012 long-term care venture.

# **Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana**

## **Management's Discussion and Analysis Years Ended December 31, 2012 and 2011**

The rate of health care inflation has a direct effect on the cost of services provided by the Hospital. Expenditures for medical supplies and prescription drugs are a major component of the Hospital's costs. In 2012, the costs totaled \$54,860,648, or 21.6% of total operating expenses, resulting in an increase of \$3,120,176, or 6.0% over 2011. In 2011, the costs totaled \$51,740,472, or 23.9% of total operating expenses, resulting in an increase of \$807,549, or 1.6% over 2010. In 2010, the costs totaled \$50,932,923, or 25.0% of total operating expenses. Other factors contributing to the increased supply and drug costs include an increase in the complexity of patient cases, increase in cardiac services and procedures, the introduction of new infusion drugs that cannot be obtained in generic form and changes in therapeutic mix. In 2008, the Hospital implemented a clinical quality value analysis (CQVA) program, focused on the quality and cost-effectiveness of supplies. The CQVA program yielded savings of approximately \$1,400,000 in 2012 compared to approximately \$3,200,000 in 2011 and \$1,100,000 in 2010.

### **Nonoperating Revenues and Expenses**

Nonoperating revenues and expenses consist primarily of investment income and interest expense. The Hospital recorded investment income of \$2,795,376 in 2012 versus \$444,919 in 2011. Interest expense increased to \$5,311,716 in 2012, or a 4.0% increase over 2011 of \$5,108,807, due to a full year of interest expense for a note payable and capital leases along with increased interest expense related to the 2012 bond refinancing.

### **The Hospital's Cash Flows**

Increases in the Hospital's cash flows are the result of increased operating income and investment results. Unrealized losses related to investments and the swap agreement do not impact cash balances.

### **Capital Asset and Debt Administration**

#### ***Capital Assets***

At the end of 2012, the Hospital had \$119,793,616 net invested in capital assets compared to \$121,207,755 in 2011 for a decrease of \$1,414,139, or 1.2% from 2011 and a decrease of \$1,467,282, or 1.2% from 2011 to 2010. The decreases are primarily due to numerous assets reaching full depreciation in the respective years.

#### ***Debt***

At December 31, 2012, the Hospital had \$102,465,436 in revenue bonds, notes payable and capital lease obligations outstanding.

# **Floyd Memorial Hospital and Health Services**

## **A Component Unit of Floyd County, Indiana**

### **Management's Discussion and Analysis**

#### **Years Ended December 31, 2012 and 2011**

In April 2010, the Hospital participated in the issuance of \$56,570,000 Indiana Health Facility Financing Authority Hospital Refunding Revenue Bonds, Series 2010 Bonds (2010 Bonds), which bear interest at rates ranging from 3.000% to 5.375%. The proceeds were primarily used for the advanced refunding of the 1998 and 2003 B bonds and the termination of the 2003 B interest rate swap agreement.

In 2011, the Hospital acquired a primary care practice, signing a note payable for total borrowings of \$2,231,000, as well as a \$10,000 deposit at the execution of the agreement. This borrowing bears interest at an annual rate of 4%. The contract requires quarterly payments of \$181,667, beginning December 1, 2011, with a final payment date of June 1, 2014.

In January 2011, the Hospital acquired four new capital lease obligations, with initial borrowings of \$1,954,671. Each lease is scheduled to expire in 2016.

In July 2012, the Hospital participated in the issuance of \$47,245,000 Indiana Health Facility Financing Authority Hospital Refunding Revenue Bonds, Series 2012 Bonds (2012 Bonds), which bear interest at 68% of one-month London Interbank Offering Rate (LIBOR) plus 1.39%. The proceeds were primarily used for the advanced refunding of the 2008 bonds.

### **Other Operating and Future Economic Factors**

#### ***Indiana Hospital Assessment Fee Program***

During 2012, the state of Indiana enacted the Hospital Assessment Fee (HAF) program to replace the disproportionate share hospital (DSH) program. The HAF program includes a state specific provider assessment fee to increase Medicaid payments to hospitals. The program was implemented retroactively to the beginning of the 2012 Indiana State Fiscal Year (July 1, 2011). Therefore, the Hospital recorded an 18-month impact of the new HAF program during 2012. The Hospital recorded \$29,061,000 within net patient service revenues and expensed assessment fees totaling \$18,734,000. The Indiana Legislature is currently considering legislation, which would continue the current program for the next four to five years. Despite this consideration, there is no assurance this program will continue in the future.

### **Contacting the Hospital's Financial Management**

This financial report is designed to provide our patients, suppliers and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the chief financial officer by telephoning 812.948.7402.

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**

**Balance Sheets**

**December 31, 2012 and 2011**

**Assets and Deferred Outflows of Resources**

	<b>2012</b>	<b>(Restated) 2011</b>
<b>Current Assets</b>		
Cash and cash equivalents	\$ 31,119,742	\$ 20,688,073
Restricted investments – current	1,768,930	1,906,409
Patient accounts receivable, net of allowance; 2012 – \$19,902,436; 2011 – \$16,852,273	33,096,166	30,844,211
Supplies	4,333,569	4,193,071
Prepaid expenses and other current assets	3,409,260	3,815,980
	<b>73,727,667</b>	<b>61,447,744</b>
<b>Noncurrent Cash and Investments</b>		
Internally designated	69,522,544	66,764,284
Held by trustee for debt service	6,177,966	6,368,844
	<b>75,700,510</b>	<b>73,133,128</b>
Less amount required to meet current obligations	1,768,930	1,906,409
	<b>73,931,580</b>	<b>71,226,719</b>
<b>Capital Assets, Net</b>	<b>119,793,616</b>	<b>121,207,755</b>
<b>Other Assets</b>		
Other	9,828,557	9,890,352
	<b>277,281,420</b>	<b>263,772,570</b>
<b>Deferred Outflows of Resources</b>	<b>19,409,774</b>	<b>19,394,359</b>
<b>Total assets and deferred outflows of resources</b>	<b>\$ 296,691,194</b>	<b>\$ 283,166,929</b>

**Liabilities, Deferred Inflows of Resources and  
Net Position**

	<b>2012</b>	<b>(Restated) 2011</b>
	<u>2012</u>	<u>2011</u>
<b>Current Liabilities</b>		
Current maturities of long-term debt	\$ 3,770,273	\$ 3,620,454
Payable to suppliers and contractors	12,580,139	9,909,214
Payable to employees (including payroll taxes and benefits)	12,439,631	11,292,808
Estimated amounts due to third-party payers	1,449,574	1,143,480
Accrued expenses	2,959,096	2,157,154
Payable to Northgate Surgery Center	555,168	506,859
	<u>33,753,881</u>	<u>28,629,969</u>
<b>Fair Value of Interest Rate Swap Agreement</b>	10,118,289	10,390,179
<b>Long-Term Debt</b>	98,695,163	101,915,288
<b>Accrued Pension and Other Long-Term Liabilities</b>	<u>14,975,918</u>	<u>14,507,524</u>
Total liabilities	<u>157,543,251</u>	<u>155,442,960</u>
<b>Deferred Inflows of Resources</b>	<u>784,635</u>	<u>-</u>
<b>Net Position</b>		
Net investment in capital assets	25,835,030	24,676,193
Restricted	6,177,966	6,368,844
Unrestricted	<u>106,350,312</u>	<u>96,678,932</u>
Total net position	<u>138,363,308</u>	<u>127,723,969</u>
Total liabilities, deferred inflows of resources and net position	<u>\$ 296,691,194</u>	<u>\$ 283,166,929</u>

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**Years Ended December 31, 2012 and 2011**

	<b>2012</b>	<b>(Restated) 2011</b>
<b>Operating Revenues</b>		
Net patient service revenue, net of provision for uncollectible accounts; 2012 – \$25,700,000; 2011 – \$25,500,000	\$ 259,113,591	\$ 217,252,137
Other	7,891,379	3,210,524
Total operating revenues	267,004,970	220,462,661
<b>Operating Expenses</b>		
Salaries and benefits	125,591,909	113,462,376
Purchased services and professional fees	46,624,334	25,235,979
Supplies	54,860,648	51,740,472
Other expenses	15,910,707	14,566,954
Depreciation and amortization	11,606,306	11,309,458
(Gain) loss on sale of property and equipment	489,799	(1,013)
Total operating expenses	255,083,703	216,314,226
<b>Operating Income</b>	11,921,267	4,148,435
<b>Nonoperating Revenues (Expenses)</b>		
Investment income	2,795,376	444,919
Interest expense	(5,311,716)	(5,108,807)
Noncapital grants and contributions	690,095	307,060
Gain on investment in equity investees	1,086,874	1,269,200
Debt issuance cost	(595,000)	-
Total nonoperating revenues (expenses)	(1,334,371)	(3,087,628)
<b>Excess of Revenues Over Expenses     Before Capital Grants</b>	10,586,896	1,060,807
<b>Capital Grants</b>	52,443	129,453
<b>Increase in Net Position</b>	10,639,339	1,190,260
<b>Net Position, Beginning of Year, as Previously Reported</b>	127,723,969	128,040,780
<b>Cumulative Effect of Change of Adoption of Accounting     Principle</b>	-	1,507,071
<b>Net Position, Beginning of Year</b>	127,723,969	126,533,709
<b>Net Position, End of Year</b>	\$ 138,363,308	\$ 127,723,969

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**

**Statements of Cash Flows**

**Years Ended December 31, 2012 and 2011**

	<b>2012</b>	<b>(Restated) 2011</b>
	<hr/>	<hr/>
<b>Operating Activities</b>		
Receipts from and on behalf of patients	\$ 257,167,730	\$ 211,195,307
Payments to suppliers and contractors	(114,315,736)	(92,057,944)
Payments to employees	(123,065,926)	(112,027,120)
Other receipts, net	7,891,379	3,210,524
	<hr/>	<hr/>
Net cash provided by operating activities	27,677,447	10,320,767
	<hr/>	<hr/>
<b>Noncapital Financing Activities</b>		
Noncapital grants and contributions	690,095	307,060
	<hr/>	<hr/>
Net cash provided by noncapital financing activities	690,095	307,060
	<hr/>	<hr/>
<b>Capital and Related Financing Activities</b>		
Capital grants and contributions	52,443	129,453
Interest payments on long-term obligations	(4,787,440)	(4,676,646)
Principal paid on long-term debt and capital leases	(50,521,308)	(3,070,902)
Purchase of capital assets	(10,557,562)	(8,233,437)
Payment of bond issuance costs	(595,000)	-
Proceeds from issuance of long-term debt	47,245,000	2,231,000
	<hr/>	<hr/>
Net cash used in capital and related financing activities	(19,163,867)	(13,620,532)
	<hr/>	<hr/>
<b>Investing Activities</b>		
Proceeds from disposition of investments	13,626,548	35,799,717
Purchase of investments	(14,758,251)	(36,506,400)
Interest and dividends on investments	1,359,697	1,584,622
Proceeds from sale of capital assets	1,000,000	1,950
	<hr/>	<hr/>
Net cash provided by investing activities	1,227,994	879,889
	<hr/>	<hr/>
<b>Increase (Decrease) in Cash and Cash Equivalents</b>	10,431,669	(2,112,816)
	<hr/>	<hr/>
<b>Cash and Cash Equivalents, Beginning of Year</b>	20,688,073	22,800,889
	<hr/>	<hr/>
<b>Cash and Cash Equivalents, End of Year</b>	\$ 31,119,742	\$ 20,688,073
	<hr/> <hr/>	<hr/> <hr/>

	<b>2012</b>	<b>(Restated) 2011</b>
<b>Reconciliation of Operating Income to Net Cash Provided by Operating Activities</b>		
Operating income	\$ 11,921,267	\$ 4,148,435
Depreciation and amortization	11,606,306	11,309,458
Provision for uncollectible accounts	25,700,001	25,513,934
(Gain) loss on disposition of assets	489,799	(1,013)
Changes in operating assets and liabilities		
Patient accounts receivable	(27,951,956)	(29,472,521)
Estimated amounts due to third-party payers	306,094	(2,098,237)
Accounts payable and accrued expenses	4,428,948	3,268,984
Prepaid assets, supplies and other assets	1,176,988	(2,348,273)
	<u>\$ 27,677,447</u>	<u>\$ 10,320,767</u>
<b>Supplemental Cash Flows Information</b>		
Property, plant and equipment additions in accounts payable	\$ 1,118,252	\$ 449,445
Property, plant and equipment acquired through capital lease obligations	\$ 178,232	\$ 1,954,671
Deferred loss on defeasance of bonds	\$ (39,463)	\$ -
Change in fair value of interest rate swap agreements	\$ 271,890	\$ (4,286,997)

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

#### **Note 1: Nature of Operations and Summary of Significant Accounting Policies**

##### ***Nature of Operations and Reporting Entity***

Floyd Memorial Hospital and Health Services (Hospital) is an acute care hospital located in New Albany, Indiana. The Hospital is a component unit of Floyd County (County) and the Board of County Commissioners appoints members to the board of trustees of the Hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in Floyd County and the surrounding six county areas.

##### ***Basis of Accounting and Presentation***

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (primarily federal and state grants and county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific (such as county appropriations), investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position is available.

During the year ended December 31, 2012, the Hospital adopted Statement of Governmental Accounting Standards Board (GASB) No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which supersedes GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, thereby eliminating the election provided in Paragraph 7 of that statement for business-type activities to apply post-November 30, 1989, FASB statements and interpretations that do not conflict with or contradict GASB pronouncements. GASB No. 62 has been applied retrospectively and had no impact on the Hospital's net position or changes in net position and minimal changes to financial reporting disclosures.

During the year ended December 31, 2012, the Hospital adopted GASB No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position* and No. 65, *Items Previously Reported as Assets and Liabilities*.

The objective of GASB No. 63 is to provide guidance for reporting deferred outflows of resources, deferred inflows of resources and net position in a statement of financial position and related disclosures. GASB No. 63 has been applied retrospectively, by reclassifying certain 2011 financial statement line items to conform with the presentation requirements of the standard.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

The objective of GASB No. 65 is to either (a) properly classify certain items that were previously reported as assets and liabilities as deferred outflows of resources or deferred inflows of resources or (b) recognize certain items that were previously reported as assets and liabilities as outflows of resources (expenses or expenditures) or inflows of resources (revenues). GASB No. 65 has been applied retrospectively by restating the Hospital's prior years' net position and changes in net position related to: (1) bond issuance costs that had previously been capitalized and amortized, but are no longer recognized as assets and (2) to reflect deferred bond defeasance costs as a deferred outflow of resources. Due to the adoption of GASB No. 65, long-term debt increased by \$9,004,180 in 2011 as deferred losses on refunding were reclassified as deferred outflow of resources. Also, due to the adoption of GASB No. 65, the 2011 beginning net position was decreased by \$1,507,071, depreciation and amortization expense was decreased by \$63,831, other assets was decreased by \$1,443,240.

#### ***Use of Estimates***

The preparation of 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### ***Cash Equivalents***

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2012 and 2011, cash equivalents consisted primarily of money market accounts.

#### ***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 other than employee health claims. Settled claims have not exceeded this commercial coverage in any of the two preceding years.

The Hospital is self-insured for a portion of its exposure to risk of loss from employee health claims. Annual estimated provisions are accrued for the self-insured portion of employee health claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

#### ***Investments and Investment Income***

Investments generally include U.S. Treasury, agency and instrumentality obligations with various maturities at time of acquisition, money market accounts, corporate bonds and securities and mutual funds. The investments in equity investees are reported on the equity method of accounting. All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income, realized gains and losses on investments and the net change for the year in the fair value of investments carried at fair value.

#### ***Patient Accounts Receivable***

The Hospital reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Hospital provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

#### ***Supplies***

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

#### ***Capital Assets***

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line half-year convention method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital:

Land improvements	2 – 25 years
Buildings and leasehold improvements	5 – 40 years
Equipment	2 – 20 years

The Hospital capitalizes interest costs as a component of construction in progress, based on interest costs of borrowing specifically for the project, net of interest earned on investments acquired with the proceeds of the borrowing. There was no interest capitalized and incurred at December 31, 2012 and 2011, respectively.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

#### **Other Assets**

*Split-Dollar Life Insurance Policies.* Other assets include the cumulative paid premiums under a split-dollar life insurance policy for certain employees of the Hospital. In accordance with the policy agreement, the Hospital will receive the greater of the cash surrender value of the policy or cumulative premiums upon termination of the contract by the employees upon their death.

*Investment in Joint Ventures.* The investment in joint ventures is accounted for by the equity method of accounting and is further described in Note 5.

#### **Deferred Amounts on Refunding**

Deferred amounts on refunding, which are included in deferred outflow of resources on the balance sheets, represent losses incurred in connection with the refunding of various long-term debt. Such losses are being amortized over the shorter of the term of the respective original debt or the term of the new debt using the straight-line method.

#### **Other Long-Term Liabilities**

Other long-term liabilities consist of deferred compensation agreements with key employees. The agreements are to be funded with proceeds from operations.

#### **Interest Rate Swap Agreement**

The Hospital uses an interest rate swap agreement to manage financial risks related to interest rate movements and the effects on its cash flows. The Hospital is accounting for the interest rate swap agreement as a hedging instrument. As a result, the agreement is recorded at its fair value in the balance sheets. The net cash payments or receipts under the interest rate swap agreement are recorded as an increase or decrease to interest expense.

#### **Compensated Absences**

Hospital policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as vacation benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Expense for sick leave benefits is recognized when earned to the extent the employee is expected to realize the benefit in cash determined using the termination payment method. Sick leave benefits expected to be realized as paid time off are

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

recognized as expense when the time off occurs and no liability is accrued for such benefits employees have earned but not yet realized. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date, plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at that date. The estimated compensated absences liability expected to be paid more than one year after the balance sheet date is included in other long-term liabilities.

#### ***Net Position***

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

#### ***Net Patient Service Revenue***

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

#### ***Charity Care***

The Hospital provides charity care to patients who are unable to pay for services. The amount of charity care is included in net patient service revenue and is not separately classified from the provision for uncollectible accounts.

#### ***Income Taxes***

As an essential government function of the county, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Hospital is subject to federal income tax on any unrelated business taxable income.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements December 31, 2012 and 2011

#### ***Electronic Health Records Incentive Program***

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records technology (EHR). Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services (CMS). Payment under both programs are contingent on the Hospital continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Hospital recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

In 2012, the Hospital completed the first-year requirements under both the Medicare and Medicaid programs and has recorded revenue of approximately \$4,706,000, which is included in other operating revenues in the statement of revenues, expenses and changes in net position.

#### **Note 2: Net Patient Service Revenue**

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

**Medicare.** Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

**Medicaid.** Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed at a prospectively determined rate per discharge for inpatient services and outpatient fee for services.

The Hospital qualifies as a Medicaid Disproportionate Share Hospital (DSH) provider under Indiana Law (HEA 1095, Public Law 27-1992) and, as such, is eligible to receive supplemental Medicaid payments. The amounts of these additional supplemental payments are dependent on regulatory approval by agencies of the federal and state governments and is determined by level, extent and cost of uncompensated care (as defined) and various other factors. Supplemental payments have been made by the state of Indiana and the Hospital

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

records such amounts as revenue when reasonably determined that the funds will be received. The Hospital recognized approximately \$4,900,000 of net patient service revenue related to the supplemental payment program for the years ended December 31, 2011. The Hospital recognized receivables from this program in the amount of \$500,000 at December 31, 2011, for various Indiana state fiscal years, which ends June 30 each year. It is reasonably possible estimates associated with the supplemental payment program could change materially in the near term.

During 2012, the state of Indiana enacted the Hospital Assessment Fee (HAF) program to replace the disproportionate share hospital (DSH) program. The HAF program includes a state specific provider assessment fee to increase Medicaid payments to hospitals. The program was implemented retroactively to the start of the 2012 Indiana State Fiscal Year (July 1, 2011). Therefore, the Hospital recorded an 18-month impact of the new HAF program during 2012. The Hospital recorded \$29,061,000 within net patient service revenues and expensed assessment fees totaling \$18,734,000. The Indiana Legislature is currently considering legislation which would continue the current program for the next four to five years. Despite this consideration, there is no assurance that this program will continue in the future.

Approximately 54% and 55% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2012 and 2011, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also 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.

### **Note 3: Deposits, Investments and Investment Income**

#### ***Deposits***

Custodial credit risk is the risk that in the event of a bank failure, a government's deposit may not be returned to it. The Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law.

Deposits with financial institutions in the state of Indiana at year-end were entirely insured by the Federal Deposit Insurance Corporation (FDIC) or by the Indiana Public Deposit Insurance Fund (IPDIF). This includes any deposit accounts issued or offered by a qualifying financial institution. Accordingly, all deposits in excess of FDIC levels are covered by the IPDIF and considered collateralized.

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Notes to Financial Statements December 31, 2012 and 2011

### **Investments**

The Hospital may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury, U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in corporate bonds and equity securities.

At December 31, the Hospital had the following investments and maturities:

Type	2012				
	Fair Value	Maturities in Years			More Than 10
		Less Than One	One to Five	Six to 10	
Corporate bonds and securities	\$ 14,438,639	\$ 3,790,634	\$ 10,648,005	\$ -	\$ -
Money market mutual funds	6,754,960	6,754,960	-	-	-
U.S. agencies	13,086,896	3,026,115	10,060,781	-	-
Mutual funds	41,420,015	41,420,015	-	-	-
	<u>\$ 75,700,510</u>	<u>\$ 54,991,724</u>	<u>\$ 20,708,786</u>	<u>\$ -</u>	<u>\$ -</u>
	<b>2011</b>				
Type	Fair Value	Maturities in Years			More Than 10
		Less Than One	One to Five	Six to 10	
Corporate bonds and securities	\$ 11,601,613	\$ 1,620,680	\$ 9,980,933	\$ -	\$ -
Money market mutual funds	6,750,861	6,750,861	-	-	-
U.S. agencies	15,585,205	3,955,833	11,629,372	-	-
Mutual funds	39,195,449	39,195,449	-	-	-
	<u>\$ 73,133,128</u>	<u>\$ 51,522,823</u>	<u>\$ 21,610,305</u>	<u>\$ -</u>	<u>\$ -</u>

*Interest Rate Risk* – Interest rate risk is the risk of fair value losses arising from rising interest rates. The Hospital does not have a formal policy to limit its interest rate risk. The money market mutual funds are presented as an investment with a maturity of less than one year because they are redeemable in full immediately.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements December 31, 2012 and 2011

*Credit Risk* – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. It is the Hospital’s policy to limit its investments in corporate bonds to the top two ratings issued by nationally recognized statistical rating organizations (NRSROs). At December 31, 2012 and 2011, the Hospital’s investments in U.S. agencies obligations not directly guaranteed by the U.S. Government were rated Aaa by Moody’s Investor Services.

*Custodial Credit Risk* – For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Hospital will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. At December 31, 2012 and 2011, the Hospital held no investments in repurchase agreements.

*Concentration of Credit Risk* – The Hospital places no limit on the amount that may be invested in any one issuer. At December 31, 2012 and 2011, the Hospital had \$14,438,639 and \$11,601,613 invested in corporate bonds, respectively.

#### **Summary of Carrying Values**

The carrying values of deposits and investments shown above are included in the balance sheets at December 31 as follows:

	<b>2012</b>	<b>2011</b>
Carrying value		
Deposits	\$ 31,119,742	\$ 20,688,073
Investments	75,700,510	73,133,128
	\$ 106,820,252	\$ 93,821,201

Included in the following balance sheet captions:

	<b>2012</b>	<b>2011</b>
Cash and cash equivalents	\$ 31,119,742	\$ 20,688,073
Restricted investments – current	1,768,930	1,906,409
Noncurrent cash and investments	73,931,580	71,226,719
	\$ 106,820,252	\$ 93,821,201

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**

**Notes to Financial Statements**  
**December 31, 2012 and 2011**

***Investment Income***

Investment income for the years ended December 31 consisted of:

	<b>2012</b>	<b>2011</b>
Interest and dividend income	\$ 1,359,697	\$ 1,584,622
Net (decrease) increase in fair value of investments	1,435,679	(1,139,703)
	\$ 2,795,376	\$ 444,919

**Note 4: Patient Accounts Receivable**

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31 consisted of:

	<b>2012</b>	<b>2011</b>
Medicare	\$ 14,247,803	\$ 15,193,023
Medicaid	5,314,170	1,085,212
Other third-party payers	14,922,216	14,361,551
Patients	18,514,413	17,056,698
	52,998,602	47,696,484
Less allowance for uncollectible accounts	19,902,436	16,852,273
	\$ 33,096,166	\$ 30,844,211

**Note 5: Investments in Uncombined Entities**

The investments in uncombined entities are accounted for on the equity method. The equity earnings of the uncombined entities are accounted for on the equity method and are included in nonoperating revenues. Investments in uncombined entities consist of a 33.33% interest in Southern Indiana Rehabilitation Hospital (an acute rehabilitation hospital), a 48% interest in

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Notes to Financial Statements December 31, 2012 and 2011

Kleinert, Kutz Associates Surgery Center, LLC (KKA), d/b/a Northgate Surgery Center, LLC (Joint Venture) (an outpatient surgery center), a 10% interest in Indiana Healthcare Reciprocal Risk Retention Group (Risk Retention Group) (a medical malpractice insurance captive) and a 50% interest in Northgate Medical Imaging, LLC, d/b/a Priority Imaging (an outpatient diagnostic imaging center).

### **Guarantees**

The Hospital guarantees certain third-party debt and capital leases of unconsolidated affiliated organizations.

At December 31, 2012 and 2011, the Hospital has guaranteed 33% of the \$2,550,000 and \$3,150,000, respectively, outstanding debt of Southern Indiana Rehabilitation Hospital. The debt guarantee expires on April 15, 2016.

At December 31, 2012 and 2011, the Hospital has guaranteed 50% of the \$449,315 and \$836,274, respectively, for a line of credit, note and capital leases of Northgate Medical Imaging, LLC.

### **Note 6: Capital Assets**

Capital assets activity for the years ended December 31 were:

	<b>2012</b>				<b>Ending Balance</b>
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	
Land	\$ 7,820,099	\$ -	\$ (1,492,978)	\$ -	\$ 6,327,121
Land improvements	3,655,556	12,005	-	-	3,667,561
Buildings and leasehold improvements	130,746,893	246,582	-	-	130,993,475
Equipment	122,005,516	10,960,026	(24,980)	-	132,940,562
Construction in progress	357,077	213,757	-	-	570,834
	<u>264,585,141</u>	<u>11,432,370</u>	<u>(1,517,958)</u>	<u>-</u>	<u>274,499,553</u>

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**

**Notes to Financial Statements**  
**December 31, 2012 and 2011**

	<b>2012</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Less accumulated depreciation					
Land improvements	\$ 2,898,264	\$ 103,072	\$ -	\$ -	\$ 3,001,336
Buildings and leasehold improvements	50,847,673	3,794,344	-	-	54,642,017
Equipment	89,631,449	7,431,525	(390)	-	97,062,584
Total accumulated depreciation	143,377,386	11,328,941	(390)	-	154,705,937
Capital assets, net	<u>\$ 121,207,755</u>	<u>\$ 103,429</u>	<u>\$ (1,517,568)</u>	<u>\$ -</u>	<u>\$ 119,793,616</u>
	<b>2011</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Land	\$ 7,820,099	\$ -	\$ -	\$ -	\$ 7,820,099
Land improvements	3,522,429	154,451	(21,324)	-	3,655,556
Buildings and leasehold improvements	129,861,424	496,302	(42,443)	431,610	130,746,893
Equipment	117,327,019	8,985,306	(4,399,617)	92,808	122,005,516
Construction in progress	710,184	171,311	-	(524,418)	357,077
	<u>259,241,155</u>	<u>9,807,370</u>	<u>(4,463,384)</u>	<u>-</u>	<u>264,585,141</u>
Less accumulated depreciation					
Land improvements	2,784,828	113,436	-	-	2,898,264
Buildings and leasehold improvements	46,985,306	3,862,367	-	-	50,847,673
Equipment	86,795,984	7,295,886	(4,460,421)	-	89,631,449
Total accumulated depreciation	136,566,118	11,271,689	(4,460,421)	-	143,377,386
Capital assets, net	<u>\$ 122,675,037</u>	<u>\$ (1,464,319)</u>	<u>\$ (2,963)</u>	<u>\$ -</u>	<u>\$ 121,207,755</u>

**Note 7: Medical Malpractice Claims**

The Hospital purchases medical malpractice insurance from Risk Retention Group under a claims-made policy. The Hospital pays an annual premium to Risk Retention Group for its torts insurance coverage. The Risk Retention Group's governing agreement specifies that the Risk Retention Group will be self-sustaining through member premiums and will re-insure through commercial

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

carriers for claims in excess of stop-loss amounts. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claims experience, no liabilities were recorded at December 31, 2012 and 2011. It is possible this estimate could change materially in the near term.

Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term but reported subsequently will be uninsured. However, the *Indiana Malpractice Act* (Act) limits professional liability for claims prior to July 1, 1999, to a maximum recovery of \$750,000 per occurrence (\$3,000,000 annual aggregate), \$100,000 of which would be paid through malpractice insurance coverage, and the balance would be paid by the State of Indiana Patient Compensation Fund (Fund). For claims on or after July 1, 1999, the maximum recovery is \$1,250,000 per occurrence (\$7,500,000 annual aggregate), \$250,000 of which would be paid through insurance coverage and the remainder by the Fund.

#### Note 8: Employee Health Claims

Substantially all of the Hospital's employees and their dependents are eligible to participate in the Hospital's employee health insurance plan. The Hospital is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$125,000. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is possible the Hospital's estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability during the years ended December 31 is summarized as follows:

	2012	2011
Balance, beginning of year	\$ 900,340	\$ 1,046,015
Current year claims incurred and changes in estimates for claims incurred in prior years	11,813,829	10,867,772
Claims and expenses paid	(11,395,648)	(11,013,447)
Balance, end of year	\$ 1,318,521	\$ 900,340



# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Notes to Financial Statements December 31, 2012 and 2011

The following is a summary of other long-term obligations for the Hospital for the years ended December 31:

	<b>2012</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Deductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Accrued pension liabilities	\$ 14,160,868	\$ 2,758,796	\$ 2,480,083	\$ 14,439,581	\$ -
Other long-term liabilities	346,656	189,681	-	536,337	-
<b>Total other long-term obligations</b>	<b>\$ 14,507,524</b>	<b>\$ 2,948,477</b>	<b>\$ 2,480,083</b>	<b>\$ 14,975,918</b>	<b>\$ -</b>
	<b>2011</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Deductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Accrued pension liabilities	\$ 12,211,718	\$ 1,949,150	\$ -	\$ 14,160,868	\$ -
Other long-term liabilities	387,006	186,924	227,274	346,656	-
<b>Total other long-term obligations</b>	<b>\$ 12,598,724</b>	<b>\$ 2,136,074</b>	<b>\$ 227,274</b>	<b>\$ 14,507,524</b>	<b>\$ -</b>

### **Revenue Bonds Payable**

The Hospital has revenue bonds payable with the Indiana Healthcare Facility Financing Authority (Authority). The Master Trust Indenture requires certain funds be established with the trustee. Accordingly, these funds are included as assets held by trustee for debt service in the balance sheets. The Master Trust Indenture also places limits on the incurrence of additional borrowings and requires that certain measures of financial performance be maintained so long as the bonds are outstanding. At December 31, 2012, the Hospital was in compliance with such requirements.

### **Series 2008**

In December 2008, the Hospital participated in the issuance of \$49,800,000 Indiana Health and Educational Facility Financing Authority Adjustable Rate Hospital Revenue Bonds, Series 2008 (2008 Bonds). The 2008 Bonds were issued as variable rate demand bonds under an agreement with Piper Jaffray & Co. The proceeds were used to refinance the Series 2003A and Series 2006 Bonds.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

In July 2012, the Hospital defeased the remaining balance of the 2008 Bonds with proceeds from the issuance of the 2012 Bonds. However, the swap agreement associated with the 2003A and 2008 Bonds was not terminated as part of the defeasance (Note 11).

#### **Series 2010**

In April 2010, the Hospital participated in the issuance of \$56,570,000 Indiana Health Facility Financing Authority Hospital Refunding Revenue Bonds, Series 2010 Bonds (2010 Bonds), which bear interest at rates ranging from 3.000% to 5.375%. The proceeds were primarily used for the advanced refunding of the 1998 and 2003B Bonds. The 2010 Bonds are subject to retirement in varying principal amounts through 2034. The bonds are secured by the gross revenues of the Hospital and the assets restricted under the bond indenture agreement.

#### **Series 2012**

In July 2012, the Hospital participated in the issuance of \$47,245,000 Indiana Health Facility Financing Authority Hospital Refunding Revenue Bonds, Series 2012 Bonds (2012 Bonds), which bear interest at 68% of one-month London Interbank Offering Rate (LIBOR) rate plus 1.39%. Under the trust indenture, the 2012 Bonds were issued between the Indiana Finance Authority and The Bank of New York Mellon Trust Company and in conjunction with the trust indenture, a loan agreement was entered into for the proceeds of the sale of the 2012 Bonds to be loaned to the Hospital. The proceeds were primarily used for the advanced refunding of the 2008 Bonds. The 2012 Bonds are subject to retirement in varying principal amounts through 2036 as noted in the Master Note Series 2012. The bonds are secured by the gross revenues of the Hospital and the assets restricted under the bond indenture agreement. The sole bond holder of the Series 2012 Bonds, Branch Banking & Trust Bank, entered into a contract of purchase and promissory note for a 10 year term.

#### **Note Payable**

In 2011, the Hospital entered into an unsecured note payable related to a primary care practice acquisition. The note totaled \$2,231,000, payable quarterly over three years with 4% annual interest. At December 31, 2012, the Hospital had \$1,035,384 in outstanding principal, including \$687,888 due in 2013.

#### **Capital Lease Obligations**

The Hospital is obligated under leases for certain medical equipment that are accounted for as capital leases. The lease agreements bear interest at various amounts up to 4.40%. The historical cost of assets under capital leases, net of accumulated depreciation of \$638,900 and \$195,467 at December 31, 2012 and 2011, respectively, was \$1,490,770 and \$1,759,203 at December 31, 2012 and 2011, respectively.

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**

**Notes to Financial Statements**  
**December 31, 2012 and 2011**

The debt service requirements for long-term obligations as of December 31, 2012, were as follows:

	<b>Total to be Paid</b>	<b>Principal</b>	<b>Interest</b>
2013	\$ 9,280,442	\$ 3,770,273	\$ 5,510,169
2014	8,633,128	3,552,367	5,080,761
2015	7,911,079	3,353,194	4,557,885
2016	7,766,967	3,352,445	4,414,522
2017	7,447,645	3,185,000	4,262,645
2018–2022	37,181,581	18,415,000	18,766,581
2023–2027	35,791,279	21,935,000	13,856,279
2028–2032	35,627,919	28,085,000	7,542,919
2033–2036	18,262,698	17,405,000	857,698
	<u>\$ 167,902,738</u>	<u>\$ 103,053,279</u>	<u>\$ 64,849,459</u>

**Note 10: Line of Credit**

The Hospital has an unsecured open-ended demand line of credit in the amount of \$5,000,000 with a bank. Amounts outstanding under the line of credit bear interest at the 30-day LIBOR, plus 1.25% adjusted monthly. There were no borrowings on the line of credit at December 31, 2012 and 2011.

**Note 11: Interest Rate Swap Agreement**

***Objective of the Interest Rate Swap Agreement***

The Hospital's asset/liability strategy is to have a mixture of fixed- and variable-rate debt to take advantage of market fluctuations. As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations and to lower its borrowing costs when compared against fixed-rate debt at the time of issuance, the Hospital entered into interest rate swap agreements in connection with its 2003A Bonds and 2003B Bonds. The original intention of the swap agreements was to effectively change the Hospital's variable interest rate on the 2003A Bonds and 2003B Bonds to a synthetic fixed rate of 4.05%.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

The 2003A Bonds were defeased in December 2008 and related swap agreement was redesignated to a portion of the 2008 Bonds. The 2003B Bonds were defeased in April 2010 and the related swap agreement was terminated at the time of the issuance of the 2010 Bonds.

The 2008 Bonds were defeased in July 2012; however, the swap agreement remained. In accordance with GASB No. 53, in connection with the debt refunding, the deferred outflows related to the accumulation of changes in fair value of the swap agreement, were included in deferred amounts on refunding. Changes in fair value of the swap agreement subsequent to the refunding are recorded in deferred outflows, in accordance with hedge accounting prescribed by GASB No. 53.

#### **Terms**

The 2003A swap agreement was entered into on November 10, 2003, and is scheduled to expire on March 1, 2034, and required no initial net cash receipt or payment by the Hospital. The agreement provides for the Hospital to receive interest from the counterparty at 70.00% of the one-month LIBOR and to pay interest to the counterparty at a fixed rate of 4.17% on notional amounts of \$32,200,000 and \$32,725,000 at December 31, 2012 and 2011, respectively. Beginning in 2009, the notional amount of the swap agreement declines by a corresponding amount each time a principal payment is scheduled to become due on the associated debt until the notional amount reaches \$2,650,000 at the termination of the swap agreement. Under the swap agreement, the Hospital pays or receives the net interest amount monthly, with the monthly settlements included in interest expense.

#### **Fair Value**

As of December 31, 2012 and 2011, the swap agreement had a fair value of \$(10,118,289) and \$(10,390,179), respectively, calculated using the par-value method, *i.e.*, the fixed rate on the swap agreement was compared with the current fixed rates that could be achieved in the marketplace should the swap agreement be unwound. The fixed-rate components were valued by discounting the fixed-rate cash flows using the current yield to maturity of a comparable bond. The variable-rate components were assumed to be at par value because the interest rates reset to the market rate at every reset date. The fair value was then calculated by subtracting the estimated market value of the fixed components from the established market value of the variable components. The fair value of the swap agreement is recognized in long-term liabilities. Through the date of the defeasance of the 2008 Bonds, the swap agreement was an effective hedging instrument and therefore the offsetting balance was reflected as a deferred outflow of resources on the Hospital's balance sheets. The cumulative amount of changes in fair value through the date of the 2008 Bond defeasance (\$10,902,924) was included in the loss on defeasance which is reported in deferred outflows.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

Subsequent to the defeasance, hedge accounting was resumed and changes in fair value of \$784,635 are reflected in deferred inflows and \$(4,286,997) are reflected in deferred outflows for the years ended December 31, 2012 and 2011, respectively. The total changes in fair value of the swap agreement was \$271,890 and \$(4,286,997) for the years ended December 31, 2012 and 2011, respectively.

#### ***Credit Risk***

The swap agreement's fair value represented the Hospital's credit exposure to the counterparty as of December 31, 2012. Should the counterparty to this transaction fail to perform according to the terms of the swap agreement, the Hospital has a maximum possible loss equivalent to the swap agreement's fair value at that date. As of December 31, 2011, the Hospital was not exposed to credit risk because the swap agreement had a negative fair value. The swap agreement counterparty was rated A by Fitch Ratings and Standard & Poor's and A2 by Moody's Investors Service as of December 31, 2011 and 2010. To mitigate the potential for credit risk, if the counterparty's credit quality rating falls below the current rating for at least two of the three rating agencies, the fair value of the swap agreement is to be fully collateralized by the counterparty with U. S. Treasury obligations to be held by a third-party custodian on behalf of the Hospital. The Hospital does not currently have a policy of requiring the counterparty post collateral in the event the Hospital becomes exposed to credit risk. The Hospital does not currently have a policy requiring a master netting agreement with the counterparty and does not currently have such an agreement in place.

#### ***Basis Risk***

The interest rate swap agreement exposes the Hospital to basis risk should the relationship between LIBOR and the auction rate set by the Hospital's remarketing agent change in a manner adverse to the Hospital. If an adverse change occurs in the relationship between these rates, the expected cost savings may not be realized.

#### ***Termination Risk***

The Hospital or the counterparty may terminate the interest rate swap agreement if the other party fails to perform under the terms of the contract. If the interest rate swap agreement is terminated, the variable-rate bonds would no longer have a synthetic fixed rate of interest. Also, if the interest rate swap agreement has a negative fair value at the time of termination, the Hospital would be liable to the counterparty for a payment equal to the interest rate swap agreement's fair value.

**Floyd Memorial Hospital and Health Services**  
**A Component Unit of Floyd County, Indiana**

**Notes to Financial Statements**  
**December 31, 2012 and 2011**

**Swap Payments and Associated Debt**

Using rates as of December 31, 2012, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same, for their term are set forth in the table below. As rates vary, variable-rate interest payments and net swap payments will vary.

Years Ending December 31	2012 Bonds		Hedging Derivative Instrument, Net	Total to be Paid
	Principal	Interest		
2013	\$ 910,000	\$ 719,388	\$ 1,237,883	\$ 2,867,271
2014	940,000	705,447	1,214,203	2,859,650
2015	990,000	691,047	1,189,529	2,870,576
2016	1,025,000	675,881	1,163,033	2,863,914
2017	1,110,000	660,179	1,136,206	2,906,385
2018–2022	6,360,000	3,032,734	5,199,318	14,592,052
2023–2027	11,020,000	2,407,483	3,686,301	17,113,784
2028–2032	13,980,000	1,477,533	1,571,772	17,029,305
2033–2036	10,625,000	373,022	17,602	11,015,624
	<u>\$ 46,960,000</u>	<u>\$ 10,742,714</u>	<u>\$ 16,415,847</u>	<u>\$ 74,118,561</u>

**Note 12: Billing Under Arrangement**

As noted in Note 5, the Hospital has had since 2007 a 48% interest in Northgate Surgery Center, LLC, formerly known as KKA Surgery Center, LLC, which has been accounted for on the equity method as the Hospital's joint venture with Kleinert Kutz and Associates PLLC, which holds the other 52% interest (Joint Venture) for the purpose of offering greater surgical capacity to Hospital patients. As part of the Joint Venture, the Hospital has entered into a billing under arrangement agreement, in which nongovernmental program patient revenues are billed under the Hospital's employer identification number (EIN) and 95% of net patient revenue is remitted to the Joint Venture as a management fee, inclusive of all operating expenses and costs associated with the services being rendered. For the years ended December 31, 2012 and 2011, net patient service revenue related to the Joint Venture was \$4,268,571 and \$4,213,101, respectively, and associated management fee expense was \$4,266,001 and \$4,206,610, respectively. At December 31, 2012 and 2011, net patient accounts receivable related to the Joint Venture was \$672,294 and \$533,543, respectively, and accounts payable to the counterparty of the Joint Venture, KKA, was \$555,168 and \$506,859, respectively.

**Floyd Memorial Hospital and Health Services  
A Component Unit of Floyd County, Indiana**

**Notes to Financial Statements  
December 31, 2012 and 2011**

**Note 13: Operating Leases**

The Hospital has entered into various operating leases for office space and medical equipment expiring at various years through 2021. Rent expense was \$5,150,028 and \$4,282,150 for the years ended December 31, 2012 and 2011, respectively.

Future minimum lease payments at December 31, 2012, are:

2013	\$ 3,480,899
2014	3,103,967
2015	3,023,167
2016	2,637,242
2017	1,325,620
2018–2021	<u>5,002,054</u>
Future minimum lease payments	<u><u>\$ 18,572,949</u></u>

**Note 14: Defined Benefit Pension Plan**

***Plan Description***

The Hospital's defined benefit pension plan is a single-employer defined benefit pension plan administered by the plan's board of trustees who are appointed by the County Commissioners of Floyd County, Indiana. The plan provides retirement, disability and death benefits to plan members and beneficiaries. The authority to establish and amend benefit provisions is set forth in Indiana Code 16-22-3-11. The plan issues a publicly available financial report that includes financial statements and required supplementary information for the plan. The report may be obtained by writing to the investment manager at Renaissance Investment Management, Inc., 1700 Young Street, Cincinnati, OH 45210-1521 or by calling 513.723.4500.

Effective May 1, 2010, the plan was amended to freeze the traditional benefit formula and modify the benefit formula for employees employed or re-employed on or after May 1, 2010. These benefits will now accrue under an account-based formula.

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Notes to Financial Statements December 31, 2012 and 2011

### ***Funding Policy***

The authority to establish and amend obligations of plan members is established by the written agreement between the Hospital's board of trustees and the plan administrator. Plan members are required to contribute 0% of their annual covered salary. The Hospital is required to contribute at an actuarially determined rate. The Hospital's annual required contributions for 2012 and 2011, were \$3,759,770 and \$2,812,346, respectively, and contributions made to the plan for 2012 and 2011, were \$2,480,083 and \$0, respectively.

### ***Annual Pension Cost and Net Pension Obligation***

The Hospital's annual pension cost and net pension obligation to the plan for December 31 were as follows:

	<b>2012</b>	<b>2011</b>
Annual required contribution	\$ 3,759,770	\$ 2,812,346
Interest on net pension obligation	1,062,065	915,879
Adjustment to annual required contribution	(2,063,039)	(1,779,075)
Annual pension cost	2,758,796	1,949,150
Contributions made	(2,480,083)	-
Increase in net pension obligation	278,713	1,949,150
Net pension obligation at beginning of the year	14,160,868	12,211,718
Net pension obligation at end of the year	\$ 14,439,581	\$ 14,160,868

### ***Funded Status and Funding Progress***

As of May 1, 2012, the most recent actuarial valuation date, the plan was 58% funded. The actuarial accrued liability for benefits was \$51,972,343 and the actuarial value of assets was \$30,091,776, resulting in an unfunded actuarial accrued liability (UAAL) of \$21,880,567. The covered payroll (annual payroll of active employees covered by the plan) was \$73,977,468 and the ratio of the UAAL to the covered payroll was 30%.

As of December 31, 2012, the fair value of the pension trust fund assets had decreased to \$30,238,277.

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Notes to Financial Statements December 31, 2012 and 2011

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 health care 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. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

### **Actuarial Methods and Assumptions**

The annual required contribution for 2012 was determined as part of an actuarial valuation on May 1, 2012, using the projected unit credit actuarial cost method. The actuarial assumptions included (a) 7.0% investment rate of return (net of administrative expenses) and (b) projected salary increases of 3.5% per year. The actuarial value of assets was determined using market value. The UAAL is being amortized on a level dollar basis over a 10-year period.

### **Three Year Trend Information**

Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
December 31, 2010	\$ 2,181,718	23%	\$ 12,211,718
December 31, 2011	\$ 1,949,150	0%	\$ 14,160,868
December 31, 2012	\$ 2,758,796	90%	\$ 14,439,581

### **Note 15: Defined Contribution Pension Plan**

The Hospital contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's required contributions, determined in accordance with the terms of the plan. The plan is administered by a board of trustees appointed by the County Commissioners of Floyd County, Indiana. The plan provides retirement benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Hospital's governing body. Contributions made by plan members at December 31, 2012 and 2011, were \$4,346,669 and \$4,177,683, or 5%, respectively, of total payroll for both years. Contributions made by the Hospital at December 31, 2012 and 2011, were \$1,217,572 and \$1,155,518, or 1%, respectively, of total payroll for both years.

# Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana

## Notes to Financial Statements December 31, 2012 and 2011

### **Note 16: Deferred Outflows and Inflows of Resources**

The Hospital has recorded deferred outflows of resources of \$19,409,774 and \$19,394,359 at December 31, 2012 and 2011, respectively. In fiscal year 2012, the deferred outflows of resources consist of \$19,409,774 in deferred bond losses related to various defeased bond issuances and the deferred inflows consist of \$784,635 in changes in fair value of the interest rate swap agreement. In fiscal year 2011, the deferred outflows of resources consist of \$10,390,179 in deferred interest rate swap asset and \$9,004,180 in deferred bond losses related to various defeased bond issuances.

### **Note 17: Long-Term Care Facility**

Effective September 1, 2012, the Hospital entered into a venture with a long-term care facility, Lincoln Hills of New Albany. The revenues and expenses associated with the operations of Lincoln Hills from September 1, 2012, are within the financial statements of the Hospital.

### **Note 18: Significant Estimates and Concentrations**

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

#### ***Allowance for Net Patient Service Revenue Adjustments***

Estimates of allowances for adjustments included in net patient service revenue are described in Notes 1 and 2.

#### ***Malpractice Claims***

Estimates related to the accrual for medical malpractice claims are described in Notes 1 and 7.

#### ***Incurred, But Not Reported, Employee Health Insurance Claims***

Estimates of incurred, but not reported, health insurance claims are described in Note 8.

# Floyd Memorial Hospital and Health Services

## A Component Unit of Floyd County, Indiana

### Notes to Financial Statements

#### December 31, 2012 and 2011

#### ***Litigation***

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Hospital's self-insurance program (discussed elsewhere in these notes) or by commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Hospital evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of ultimate expected loss, if any, for each of these matters. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

#### ***Current Economic Conditions***

The current protracted economic decline continues to present hospitals with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair value of investments and other assets, large declines in contributions, constraints on liquidity and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to the Hospital.

Current economic conditions, including the rising unemployment rate, have made it difficult for certain patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net patient service revenue, which could have an adverse impact on the Hospital's future operating results. Further, the effect of economic conditions on the state may have an adverse effect on cash flows related to the Medicaid program.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in investment values (including defined benefit pension plan investments) and allowances for accounts receivable that could negatively impact the Hospital's ability to meet debt covenants or maintain sufficient liquidity.

#### **Note 19: Patient Protection and Affordable Care Act**

The *Patient Protection and Affordable Care Act* (PPACA) will substantially reform the United States health care system. The legislation impacts multiple aspects of the health care system, including many provisions that change payments from Medicare, Medicaid and insurance companies. Starting in 2014, the legislation requires the establishment of health insurance exchanges, which will provide individuals without employer provided health care coverage the opportunity to purchase insurance. It is anticipated that some employers currently offering insurance to employees will opt to have employees seek insurance coverage through the insurance exchanges. It is possible the reimbursement rates paid by insurers participating in the insurance

# **Floyd Memorial Hospital and Health Services A Component Unit of Floyd County, Indiana**

## **Notes to Financial Statements December 31, 2012 and 2011**

exchanges may be substantially different than rates paid under current health insurance products. Another significant component of the PPACA is the expansion of the Medicaid program to a wide range of newly eligible individuals. In anticipation of this expansion, payments under certain existing programs, such as Medicare disproportionate share, will be substantially decreased. Each state's participation in an expanded Medicaid program is optional.

The state of Indiana has not indicated whether or not it will participate in the expansion of the Medicaid program. The impact of that decision on the overall reimbursement to the Hospital cannot be quantified at this point.

The PPACA is extremely complex and may be difficult for the federal government and each state to implement. While the overall impact of the PPACA cannot currently be estimated, it is possible it will have a negative impact on the Hospital's net patient service revenue. Additionally, it is possible the Hospital will experience payment delays and other operational challenges during PPACA's implementation.

## **Supplementary Information**

**Floyd Memorial Hospital and Health Services  
A Component Unit of Floyd County, Indiana**

**Schedule of Funding Progress  
December 31, 2012 and 2011**

**Required Supplementary Information**

Schedule of funding progress for defined employee pension plan consisted of the following:

*(Dollar amounts in thousands)*

Actuarial Valuation Date	Actuarial Value of Assets a	Actuarial Accrued Liability (AAL) – Entry Age b	Unfunded AAL (UAAL) b-a	Funded Ratio a/b	Covered Payroll c	UAAL as a Percentage of Covered Payroll (b-a)/c
May 1, 2010	\$ 31,053	\$ 39,668	\$ 8,615	78%	\$ 58,966	15%
May 1, 2011	\$ 31,496	\$ 41,777	\$ 10,281	75%	\$ 70,878	15%
May 1, 2012	\$ 30,092	\$ 51,972	\$ 21,880	58%	\$ 73,977	30%