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June 8, 2017

Board of Governors
Daviness Community Hospital
1314 E. Walnut Street
Washington, IN 47501

We have reviewed the audit report prepared by BKD, LLP, Independent Public Accountants, for the period January 1, 2015 to December 31, 2015. In our opinion, the audit report was prepared in accordance with the guidelines established by the State Board of Accounts. Per the Independent Auditor's Report, the financial statements included in the report present fairly the financial condition of the Daviness Community Hospital, as of December 31, 2015 and the results of its operations for the period then ended, on the basis of accounting described in the report.

The audit report is filed with this letter in our office as a matter of public record.

A handwritten signature in blue ink that reads "Paul D. Joyce".

Paul D. Joyce, CPA
State Examiner

Daviess Community Hospital
A Component Unit of Daviess County, Indiana

Independent Auditor's Report and Financial Statements

December 31, 2015 and 2014

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
December 31, 2015 and 2014

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Independent Auditor's Report

Board of Governors
Daviess Community Hospital
Washington, Indiana

Report on the Financial Statements

We have audited the accompanying balance sheets of Daviess Community Hospital (Hospital), a component unit of Daviess County, Indiana, as of December 31, 2015 and 2014, 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 basic 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. The financial statements of Daviess Community Hospital Foundation, which are included in the Hospital's financial statements, were not audited in accordance with *Government Auditing Standards*.

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 entity'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 entity'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 that 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 Daviess Community Hospital as of December 31, 2015 and 2014, 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.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 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.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the basic financial statements as a whole. The combining schedules listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 3, 2016 on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control over financial reporting and compliance.

BKD, LLP

Indianapolis, Indiana
May 3, 2016

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Management's Discussion and Analysis
December 31, 2015 and 2014

Introduction

This management's discussion and analysis of the financial performance of Daviess Community Hospital, a component unit of Daviess County, Indiana (Hospital), provides an overview of the Hospital's financial activities for the years ended December 31, 2015 and 2014. It should be read in conjunction with the accompanying financial statements of the Hospital.

Financial Highlights

- Cash and investments increased in 2015 by \$2,177,850 or 34.5% and decreased in 2014 by \$1,860,201 or 22.8%.
- The Hospital's net position decreased in 2015 and 2014 by \$642,956 or 2.7% and \$1,981,322 or 7.6%, respectively.
- The Hospital reported operating income in 2015 of \$384,509 and an operating loss in 2014 of \$922,960. The operating results in 2015 improved by \$1,307,469 or 141.7% over the operating loss reported in 2014.
- Net nonoperating expenses decreased by \$33,404 or 3.0% in 2015 compared to the increase of \$66,206 or 6.4% in 2014.

Using This Annual Report

The Hospital's financial statements consist of three statements—a balance sheet; a statement of revenues, expenses and changes in net position; and a 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 is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

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

One of the most important questions asked about any 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 Revenues, Expenses and Changes in Net Position 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. Using the accrual basis of accounting means that all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net position and changes in net position. The Hospital's total net position—the difference between assets, deferred outflows of resources 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 is 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.

Statements of Cash Flows

The Statements of Cash Flows reports cash receipts, cash payments and net changes in cash resulting from our defined types of 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 and cash equivalents during the reporting period.

Hospital's Net Position

The Hospital's net position is the difference between its assets, deferred outflows of resources and liabilities reported in the balance sheets. The Hospital's net position decreased by \$642,956 or 2.7% in 2015 over 2014 compared to the \$1,981,322 or 7.6% decrease in 2014 over 2013, as shown in Table 1.

	2015	2014	2013
Assets and Deferred Outflows of Resources			
Patient accounts receivable, net	\$ 11,846,541	\$ 6,882,550	\$ 6,051,772
Other current assets	14,229,203	6,060,183	6,763,328
Capital assets, net	28,573,304	28,294,541	30,424,084
Other noncurrent assets and deferred outflows of resources	<u>6,708,982</u>	<u>8,550,682</u>	<u>8,856,400</u>
Total assets and deferred outflows of resources	<u>\$ 61,358,030</u>	<u>\$ 49,787,956</u>	<u>\$ 52,095,584</u>
Liabilities			
Long-term debt (including current portion)	\$ 19,211,224	\$ 19,048,257	\$ 20,036,807
Other current and noncurrent liabilities	<u>18,562,878</u>	<u>6,512,815</u>	<u>5,850,571</u>
Total liabilities	<u>37,774,102</u>	<u>25,561,072</u>	<u>25,887,378</u>
Net Position			
Net investment in capital assets	8,964,517	9,246,284	10,387,277
Restricted for debt service	3,167,413	3,142,988	3,126,887
Unrestricted	<u>11,451,998</u>	<u>11,837,612</u>	<u>12,694,042</u>
Total net position	<u>23,583,928</u>	<u>24,226,884</u>	<u>26,208,206</u>
Total liabilities and net position	<u>\$ 61,358,030</u>	<u>\$ 49,787,956</u>	<u>\$ 52,095,584</u>

The most significant change in assets during 2015 were current assets. Current assets increased by \$13.1 million (101.5%) in 2015 primarily as a result of the acquisition for the operations of six long-term care facilities. The most significant changes in assets during 2014 were current assets as well as capital assets. Current assets increased by \$127,633 (1%) in 2014 primarily as a result of increased patient receivables from long-term care facilities acquired during the year. This increase was partially offset with less cash on hand. Capital assets increased by \$278,763 in 2015 compared to a decrease of \$2,129,543 in 2014. The decrease in 2014 was the result of depreciation expense during the year that exceeded new acquisitions.

Operating Results and Changes in the Hospital's Net Position

In 2015, the Hospital's net position decreased by \$642,956 or 2.7% as shown in Table 2. This decrease is made up of several different components and represents an improvement of 67.6% compared with the decrease in net position for 2014 of \$1,981,322 (7.6%). Of note, during 2015, the Hospital recognized revenue approximating \$4,048,000 related to its participation in the Indiana Medicaid Upper Payment Limit (UPL) program with its expanded nursing home operations. These amounts are recorded in other operating revenues. Also, during 2015 and 2014, the Hospital received approximately \$476,000 and \$1.1 million of revenue, respectively, from electronic health records incentive funding, which is included in other operating revenues.

	2015	2014	2013
Operating Revenues			
Net patient service revenue	\$ 95,923,449	\$ 53,837,586	\$ 49,224,083
Other operating revenues	6,765,112	2,007,031	2,226,834
Total operating revenues	<u>102,688,561</u>	<u>55,844,617</u>	<u>51,450,917</u>
Operating Expenses			
Salaries, wages, contract labor and employee benefits	52,056,098	28,895,523	28,588,103
Purchased services and professional fees	14,509,023	8,368,612	7,228,956
Depreciation and amortization	3,014,084	3,088,725	3,193,596
Provider hospital assessment fee	2,010,528	3,598,202	1,905,791
Other operating expenses	30,714,319	12,816,515	11,731,893
Total operating expenses	<u>102,304,052</u>	<u>56,767,577</u>	<u>52,648,339</u>
Operating Income (Loss)	<u>384,509</u>	<u>(922,960)</u>	<u>(1,197,422)</u>
Nonoperating Revenues (Expenses)			
Investment income	51,331	39,078	14,087
Interest expense	(1,131,657)	(1,165,777)	(1,177,325)
Other nonoperating revenues and expenses, net	7,748	20,717	123,462
Total nonoperating expenses	<u>(1,072,578)</u>	<u>(1,105,982)</u>	<u>(1,039,776)</u>
Capital Grants and Contributions	<u>45,113</u>	<u>47,620</u>	<u>8,188</u>
Decrease in Net Position	<u>\$ (642,956)</u>	<u>\$ (1,981,322)</u>	<u>\$ (2,229,010)</u>

Operating Losses

The first component of the overall change in the Hospital's net position is its operating income or loss—generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. In each of the past three years, the Hospital has reported improved operating results, with an operating loss in the prior two years and operating income in the current year. This is consistent with the Hospital's recent operating history as the Hospital was formed and is operated primarily to serve residents of Daviess and the surrounding area.

Operating income for 2015 improved by \$1,307,469 or 141.7% as compared to 2014. The primary changes in operating income are:

- An increase in net patient service revenue of \$42.1 million or 78.2%.
- An increase in other operating revenues of \$4.6 million or 229.6%.
- An increase in total operating expenses of \$45.4 million or 80.0%.

Net patient service revenue increased during 2015 as a result of long-term care facilities acquired during the year, along with increased volumes and revenues of the Hospital.

Increases in other operating revenues are attributed to UPL revenue approximating \$4,048,000 recognized with the increase in nursing home operations.

Total operating expenses increased in 2015 as a result of long-term care facilities acquired during the year. Salaries, wages, contract labor and employee benefits increased \$23.2 million or 80.2% while purchased services and professional fees increased \$6.1 million or 73.4%.

Operating income for 2015 of \$384,509 was an improvement compared to the operating loss of \$922,960 recognized in 2014. This improvement was the result of increased revenue above the increased expenses as mentioned above.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of investment income and interest expense. The Hospital recognized a slight decrease in interest expense in 2015 as compared to 2014, resulting primarily from principal payments made during the year on the Hospital's 2011 bonds outstanding.

Hospital's Cash Flows

Changes in the Hospital's cash flows are consistent with changes in operating results and net nonoperating revenues and expenses for 2015 and 2014, discussed earlier.

Capital Asset and Debt Administration

Capital Assets

At the end of 2015 and 2014, the Hospital had \$28,573,304 and \$28,294,541 invested in capital assets, net of accumulated depreciation, respectively, as detailed in Note 5 to the financial statements. The Hospital purchased new furnishings and equipment costing \$2,027,358 in 2015 and \$960,261 in 2014. The Hospital also acquired assets through capital lease obligations totaling \$1,271,671 in 2015.

Debt

At December 31, 2015, the Hospital had \$17,605,000 in revenue bonds outstanding compared to \$18,475,000 at December 31, 2014. The Hospital issued no new debt outside of the capital leases described above in 2015. The Hospital's formal revenue bonds are subject to limitations imposed by state law. See Note 9 to the basic financial statements for more information regarding long-term debt.

Line of Credit

The Hospital has a \$6,000,000 revolving bank line of credit expiring in February 20, 2016. At December 31, 2015, there was \$1,944,987 borrowed against this line. The line is collateralized by certain deposit accounts held with the bank. Interest varies with the bank's prime rate less 1.5%, which was 2.0% on December 31, 2015, and is payable monthly.

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. Questions about this report and requests for additional financial information should be directed to the Hospital Business Administration by telephoning 812.254.2760.

Daviess Community Hospital
A Component Unit of Daviess County, Indiana

Balance Sheets
December 31, 2015 and 2014

Assets and Deferred Outflows of Resources

	2015	2014
Current Assets		
Cash	\$ 4,848,201	\$ 1,137,284
Patient accounts receivable, net of allowance of \$2,180,383 and \$2,570,318 for 2015 and 2014, respectively	11,846,541	6,882,550
Supplies	1,189,481	1,074,860
Prepaid expenses and other	7,851,855	3,293,917
Estimated amounts due from third-party payers	339,666	554,122
Total current assets	26,075,744	12,942,733
Noncurrent Cash and Investments		
Internally designated	465,920	2,023,412
Held by trustee for debt service	3,167,413	3,142,988
	3,633,333	5,166,400
Capital Assets, net	28,573,304	28,294,541
Other Assets	264,497	358,265
Deferred Outflows of Resources - debt defeasance costs	2,811,152	3,026,017
Total assets and deferred outflows of resources	\$ 61,358,030	\$ 49,787,956

Liabilities and Net Position

Current Liabilities		
Current maturities of long-term debt	\$ 1,305,726	\$ 1,020,114
Line of credit	1,944,987	-
Interest payable	440,662	462,412
Accounts payable	4,633,794	2,513,823
Accrued expenses	11,543,435	3,536,580
Total current liabilities	19,868,604	7,532,929
Long-Term Debt	17,905,498	18,028,143
Total liabilities	37,774,102	25,561,072
Net Position		
Net investment in capital assets	8,964,517	9,246,284
Restricted for debt service	3,167,413	3,142,988
Unrestricted	11,451,998	11,837,612
Total net position	23,583,928	24,226,884
Total liabilities and net position	\$ 61,358,030	\$ 49,787,956

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2015 and 2014

	2015	2014
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts of \$4,625,215 and \$3,299,586 for 2015 and 2014, respectively	\$ 95,923,449	\$ 53,837,586
Other	6,765,112	2,007,031
Total operating revenues	102,688,561	55,844,617
Operating Expenses		
Salaries, wages and contract labor	41,257,672	23,462,806
Employee benefits	10,798,426	5,432,717
Purchased services and professional fees	14,509,023	8,368,612
Supplies	9,890,300	6,220,244
Insurance	962,311	539,782
Utilities	2,542,281	1,023,437
Rent	6,987,662	608,893
Repairs and maintenance	3,366,270	2,869,757
Provider hospital assessment fee	2,010,528	3,598,202
Depreciation and amortization	3,014,084	3,088,725
Other	6,965,495	1,554,402
Total operating expenses	102,304,052	56,767,577
Operating Income (Loss)	384,509	(922,960)
Nonoperating Revenues (Expenses)		
Investment income	51,331	39,078
Interest expense	(1,131,657)	(1,165,777)
Other	7,748	20,717
Total nonoperating expenses	(1,072,578)	(1,105,982)
Deficiency of Revenues Over Expenses Before Capital Grants and Contributions	(688,069)	(2,028,942)
Capital Grants and Contributions	45,113	47,620
Decrease in Net Position	(642,956)	(1,981,322)
Net Position, Beginning of Year	24,226,884	26,208,206
Net Position, End of Year	\$ 23,583,928	\$ 24,226,884

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Statements of Cash Flows
Years Ended December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Operating Activities		
Receipts from and on behalf of patients	\$ 93,977,309	\$ 53,075,834
Payments to suppliers and contractors	(31,378,616)	(19,398,442)
Payments to employees	(52,146,573)	(29,591,705)
Payments, net	<u>(6,263,214)</u>	<u>(3,150,245)</u>
Net cash provided by operating activities	<u>4,188,906</u>	<u>935,442</u>
Capital and Related Financing Activities		
Capital grants and gifts	45,113	47,620
Principal paid on capital leases	(234,032)	(143,878)
Principal paid on long-term debt	(870,000)	(840,000)
Borrowings on line of credit	1,944,987	-
Interest paid on long-term debt and capital leases	(938,542)	(963,512)
Purchase of capital assets	(2,027,358)	(960,261)
Other capital and related financing activities	9,697	4,593
Net cash used in capital and related financing activities	<u>(2,070,135)</u>	<u>(2,855,438)</u>
Investing Activities		
Interest and dividends on investments	51,331	39,078
Proceeds from sale of investments	1,533,067	113,351
Other investing activities	7,748	20,717
Net cash provided by investing activities	<u>1,592,146</u>	<u>173,146</u>
Increase (Decrease) in Cash	3,710,917	(1,746,850)
Cash, Beginning of Year	<u>1,137,284</u>	<u>2,884,134</u>
Cash, End of Year	<u>\$ 4,848,201</u>	<u>\$ 1,137,284</u>
Reconciliation of Net Operating Income (Loss) to Net Cash Provided by Operating Activities		
Operating income (loss)	\$ 384,509	\$ (922,960)
Depreciation and amortization	3,014,084	3,088,725
Provision for uncollectible accounts	4,625,215	3,299,586
Changes in operating assets and liabilities:		
Patient accounts receivable	(9,589,206)	(4,130,364)
Estimated amounts due to/from third-party payers	214,456	69,026
Accounts payable and accrued expenses	10,126,826	674,844
Other assets and liabilities	<u>(4,586,978)</u>	<u>(1,143,415)</u>
Net cash provided by operating activities	<u>\$ 4,188,906</u>	<u>\$ 935,442</u>
Supplemental Cash Flows Information		
Capital lease obligations incurred for capital assets	\$ 1,271,671	\$ -
Amortization of debt defeasance costs	214,865	214,865

Daviess Community Hospital

A Component Unit of Daviess County, Indiana

Notes to Financial Statements **December 31, 2015 and 2014**

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

Nature of Operations and Reporting Entity

Daviess Community Hospital (Hospital) is an acute care hospital located in Washington, Indiana. The Hospital is a component unit of Daviess County (County) and the Board of County Commissioners appoints members to the Board of Governors of the Hospital, pursuant to the provisions of Indiana Code 16-22-2-2. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in the Daviess County area.

The Hospital operates eight long-term care facilities (LTC) through various lease arrangements. These facilities provide inpatient and therapy services in its geographic area and supports the Hospital's mission to provide quality care and services to the facility's residents. The facilities are managed by third parties under various management agreements. The revenues from operations are the property of the Hospital and the Hospital is responsible for the associated operating expenses and working capital requirements.

In accordance with GASB Statement No. 61, the financial statements include the financial statements of the Daviess Community Hospital Foundation (Foundation). The Foundation's purpose is to provide philanthropic support through fundraising and other activities for the acquisition of equipment, facility development and support of programs at the Hospital, and has therefore been reported as a blended component unit.

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 (principally 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, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses.

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.

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Notes to Financial Statements
December 31, 2015 and 2014

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; medical malpractice; 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 three 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 employee health claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Investments and Investment Income

Investments in nonnegotiable certificates of deposit are carried at amortized cost. All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income.

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 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	5 - 25 years
Buildings and leasehold improvements	5 - 40 years
Equipment	3 - 20 years

Daviess Community Hospital

A Component Unit of Daviess County, Indiana

Notes to Financial Statements **December 31, 2015 and 2014**

Deferred Outflows of Resources

A deferred outflow of resources is a consumption of net position by the Hospital that is applicable to a future reporting period. Deferred outflows of resources are reported in the balance sheets, but are not recognized in the financial statements as expenses until the periods to which they relate. Deferred outflows of resources of the Hospital consist of deferred losses on debt refundings (defeasance costs).

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 and the related liability for sick leave benefits are 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 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 is expected to be paid within one year of the balance sheet date, and is therefore included in current liabilities.

Net Position

Net position of the Hospital is classified in three components. 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. The restricted component of net position is 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 is the remaining assets less remaining liabilities that do not meet the definition of investment in capital assets, or restricted.

Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue. Charges excluded from revenue under the Hospital's charity care policy were \$1,131,233 for 2015 and \$1,213,410 for 2014.

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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. In addition, the Hospital is exempt from taxes under Section 501(c)(3) of the Internal Revenue Code. However, the Hospital is subject to federal income tax on any unrelated business taxable income.

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the U.S. Internal Revenue Code and a similar provision of state law. However, the Foundation is subject to federal income tax on any unrelated business taxable income. The Foundation files federal tax returns in the U.S. federal jurisdiction.

Foundation

Daviess Community Hospital Foundation, Inc. (Foundation) is a legally separate, tax-exempt component unit of the Hospital. The Foundation's primary function is to raise and hold funds to support the Hospital and its programs. The board of the Foundation is self-perpetuating. Separate financial statements of the Foundation may be obtained by contacting their office at 1314 East Walnut Street, Washington, IN 47501.

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. 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.

The Hospital began recognizing incentive payment revenues earned for qualified EHR technology expenditures during 2012, which was the period when they first finished attestation for year one. In 2015 and 2014, the Hospital recorded revenue of approximately \$476,000 and \$1.1 million for the Medicare and Medicaid incentive programs, which is included in other operating revenues in the statements of revenues, expenses and changes in net position.

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Notes to Financial Statements December 31, 2015 and 2014

Reclassifications

Certain reclassifications have been made to the 2014 financial statements to conform to the 2015 financial statement presentation. The reclassifications had no effect on the 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. 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. A summary of 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. Inpatient skilled nursing services are paid at prospectively determined per diem rates that are based on the patients' acuity. Certain inpatient nonacute services are paid based on a cost reimbursement methodology. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary.

Long-term care services rendered to Medicare program beneficiaries are paid under a prospectively determined payment system on a per diem basis based on each resident's health at admission. Medicare reimburses for 100 days of skilled nursing facility care is subject to certain eligibility requirements.

Medicaid. Inpatient and outpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates. These rates vary according to the service provided and the patient diagnosis.

Long-term care services rendered to Medicaid program beneficiaries are paid on a per diem basis.

Approximately 53% and 55% of net patient service revenue are from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2015 and 2014, 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.

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The Hospital participates in a state specific provider assessment program to increase Medicaid payments to hospitals. The Hospital paid approximately \$2.0 million and \$3.6 million for 2015 and 2014, respectively, into this Medicaid program, which is recorded as an operating expense in the statements of revenues, expenses and changes in net position. During 2014, this program was re-instated retroactively to July 1, 2013 and this program is scheduled to sunset on June 30, 2017. There is no assurance this program will continue to be implemented in the future.

The Hospital also qualified as a Medicaid Disproportionate Share Hospital (DSH) provider under Indiana law and, as such, is eligible to receive supplemental Medicaid payments. The amounts of these 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 and various other factors. Supplemental payments have been made by the State of Indiana, and the Hospital records such amounts as revenue when it has been reasonably determined that the funds will be received. The Hospital recognized approximately \$770,000 within patient service revenue related to this supplemental payment program for each of the years ended December 31, 2015 and 2014. At December 31, 2015 and 2014, respectively, \$936,000 and \$796,000 is accrued as a receivable in other current assets. This represents management's best estimate of DSH funds due to the Hospital, which are typically paid in arrears.

The long-term care operations of the Hospital qualify for supplemental Medicaid payments through the Upper Payment Limit (UPL) program. The UPL is established to pay qualifying providers the difference between what Medicare would have paid and what Medicaid actually paid. The UPL is distributed through an intergovernmental transfer (IGT) arrangement. The Hospital is responsible for funding the IGT long-term care operations. Revenue associated with the UPL program is recorded net of IGT payments made to the program and are included in other operating revenue. The Hospital recognized approximately \$4,048,000 related to this supplement payment program for the year ended December 31, 2015. At December 31, 2015, \$1,287,000 is accrued and included in other current assets.

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 deposits may not be returned to it. The Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law.

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Deposits with financial institutions in the State of Indiana at year end were entirely insured by the Federal Depository 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 are considered collateralized.

Investments

The Hospital may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in certain deposit accounts, mutual funds, repurchase agreements and pooled investment funds as authorized by Indiana Code 16-22-3-20.

At December 31, 2015 and 2014, the Hospital had the following investments and maturities:

		December 31, 2015				
		Maturities in Years				
Type	Fair Value	Less Than 1	1-5	6-10	More Than 10	
Money market mutual funds	\$ 3,268,455	\$ 3,268,455	\$ -	\$ -	\$ -	-

		December 31, 2014				
		Maturities in Years				
Type	Fair Value	Less Than 1	1-5	6-10	More Than 10	
Money market mutual funds	\$ 3,240,736	\$ 3,240,736	\$ -	\$ -	\$ -	-

Interest Rate Risk - Interest rate risk is the risk that the changes in interest rates will adversely affect the fair value of an investment. The Hospital does not have a formal investment policy for interest rate risk.

Credit Risk - Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The Hospital does not have a formal investment policy for credit risk. At December 31, 2015 and 2014, the Hospital's investments were not rated.

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. The Hospital's investment policy does not address how securities underlying repurchase agreements are to be held.

Concentration of Credit Risk - The Hospital places no limit on the amount that may be invested in any one issuer.

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Notes to Financial Statements
December 31, 2015 and 2014

Summary of Carrying Values

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

	2015	2014
Carrying value:		
Deposits	\$ 5,213,079	\$ 3,062,948
Investments	3,268,455	3,240,736
	\$ 8,481,534	\$ 6,303,684
Included in the following balance sheets captions:		
Cash	\$ 4,848,201	\$ 1,137,284
Noncurrent cash and investments	3,633,333	5,166,400
	\$ 8,481,534	\$ 6,303,684

Investment Income

Investment income for the years ended December 31 consisted of:

	2015	2014
Interest and dividend income	\$ 51,331	\$ 39,078

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:

	2015	2014
Medicare	\$ 4,568,296	\$ 2,524,207
Medicaid	3,195,442	958,767
Other third-party payers	3,172,801	2,473,606
Patients	3,090,385	3,496,288
	14,026,924	9,452,868
Less allowance for uncollectible accounts	2,180,383	2,570,318
	\$ 11,846,541	\$ 6,882,550

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Notes to Financial Statements
December 31, 2015 and 2014

Note 5: Capital Assets

The Hospital's property and equipment consist of the following:

	2015				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 1,280,955	\$ -	\$ -	\$ -	\$ 1,280,955
Land improvements	687,865	-	-	-	687,865
Buildings and leasehold improvements	38,741,531	578,914	-	65,175	39,385,620
Equipment	31,025,790	1,635,221	(315,654)	343,400	32,688,757
Construction in progress	104,307	1,084,894	-	(408,575)	780,626
	<u>71,840,448</u>	<u>3,299,029</u>	<u>(315,654)</u>	<u>-</u>	<u>74,823,823</u>
Less accumulated depreciation:					
Land improvements	659,074	9,847	-	-	668,921
Buildings and leasehold improvements	17,624,500	1,086,682	-	-	18,711,182
Equipment	25,262,333	1,914,040	(305,957)	-	26,870,416
	<u>43,545,907</u>	<u>3,010,569</u>	<u>(305,957)</u>	<u>-</u>	<u>46,250,519</u>
Capital assets, net	<u>\$ 28,294,541</u>	<u>\$ 288,460</u>	<u>\$ (9,697)</u>	<u>\$ -</u>	<u>\$ 28,573,304</u>
	2014				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 1,280,955	\$ -	\$ -	\$ -	\$ 1,280,955
Land improvements	687,865	-	-	-	687,865
Buildings and leasehold improvements	38,611,259	123,437	-	6,835	38,741,531
Equipment	30,097,161	381,834	(109,025)	655,820	31,025,790
Construction in progress	311,972	454,990	-	(662,655)	104,307
	<u>70,989,212</u>	<u>960,261</u>	<u>(109,025)</u>	<u>-</u>	<u>71,840,448</u>
Less accumulated depreciation:					
Land improvements	641,493	17,581	-	-	659,074
Buildings and leasehold improvements	16,571,342	1,053,158	-	-	17,624,500
Equipment	23,352,293	2,014,472	(104,432)	-	25,262,333
	<u>40,565,128</u>	<u>3,085,211</u>	<u>(104,432)</u>	<u>-</u>	<u>43,545,907</u>
Capital assets, net	<u>\$ 30,424,084</u>	<u>\$ (2,124,950)</u>	<u>\$ (4,593)</u>	<u>\$ -</u>	<u>\$ 28,294,541</u>

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Notes to Financial Statements
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Note 6: Medical Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. 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 such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

Note 7: 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 \$90,000 per enrollee. 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 reasonably possible that the Hospital's estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability, which is included in other current liabilities in the balance sheets, during 2015 and 2014, is summarized as follows:

	2015	2014
Balance, beginning of year	\$ 521,000	\$ 622,000
Current year claims incurred and changes in estimate	3,823,959	3,080,434
Claims and expenses paid	(3,944,959)	(3,181,434)
Balance, end of year	\$ 400,000	\$ 521,000

Note 8: Operating Leases

The Hospital has operating leases for long-term care nursing facilities (see Note 14) and equipment that expire at various dates through 2016. In addition to base monthly rent, certain agreements require the Hospital to pay its proportionate share of excess operating costs associated with the facilities.

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Future minimum lease payments at December 31, 2015 were:

2016	\$ 7,535,877
2017	3,239,459
2018	1,119,958
2019	1,153,556
2020	1,188,163
Thereafter	7,561,410
Future minimum lease payments	\$ 21,798,423

Rental expense for all operating leases amounted to \$7,052,672 and \$608,893 for the years ended December 31, 2015 and 2014, respectively.

Note 9: Long-Term Debt

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

	2015				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt:					
Series 2011 refunding revenue bonds	\$ 18,475,000	\$ -	\$ (870,000)	\$ 17,605,000	\$ 910,000
Unamortized bond premium	65,794	-	(4,672)	61,122	-
Capital lease obligations	507,463	1,271,671	(234,032)	1,545,102	395,726
Total long-term debt	\$ 19,048,257	\$ 1,271,671	\$ (1,108,704)	\$ 19,211,224	\$ 1,305,726

	2014				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt:					
Series 2011 refunding revenue bonds	\$ 19,315,000	\$ -	\$ (840,000)	\$ 18,475,000	\$ 870,000
Unamortized bond premium	70,466	-	(4,672)	65,794	-
Capital lease obligations	651,341	-	(143,878)	507,463	150,114
Total long-term debt	\$ 20,036,807	\$ -	\$ (988,550)	\$ 19,048,257	\$ 1,020,114

Daviness Community Hospital

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Notes to Financial Statements December 31, 2015 and 2014

Series 2011 Revenue Refunding Bonds Payable

The Series 2011 revenue refunding bonds payable consist of lease rental revenue bonds (bonds) in the original amount of \$20,135,000 dated May 2011, which bear interest at 3% to 5.25%. Beginning in 2013, the bonds are payable in annual installments through January 15, 2029. The Hospital is required to make monthly deposits to the debt service fund held by the trustee, and interest payments are payable January 15th and July 15th annually. The bonds are secured by the net revenues and accounts receivable of the Hospital and the assets restricted under the bond indenture agreement.

The debt service requirements as of December 31, 2015 are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2016	\$ 1,768,575	\$ 910,000	\$ 858,575
2017	1,775,306	955,000	820,306
2018	1,779,788	1,000,000	779,788
2019	1,768,788	1,040,000	728,788
2020	1,770,988	1,090,000	680,988
2021-2025	8,806,744	6,290,000	2,516,744
2026-2029	7,408,124	6,320,000	1,088,124
	<u>\$ 25,078,313</u>	<u>\$ 17,605,000</u>	<u>\$ 7,473,313</u>

Capital Lease Obligations

The Hospital is obligated under leases for equipment that are accounted for as capital leases. The following is a schedule by year of future minimum lease payments under the capital lease including interest at rates ranging from 3.42% to 4.25% together with the present value of the future minimum lease payments as of December 31, 2015:

2016	\$ 447,174
2017	422,323
2018	341,986
2019	278,394
2020	179,439
Total minimum lease payments	1,669,316
Less amount representing interest	124,214
Present value of future minimum lease payments	\$ 1,545,102

Daviess Community Hospital
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Notes to Financial Statements
December 31, 2015 and 2014

Assets under capital leases at December 31, totaled:

	2015	2014
Machinery and equipment	\$ 2,024,450	\$ 752,779
Accumulated depreciation	(513,830)	(279,798)
	\$ 1,510,620	\$ 472,981

Note 10: Line of Credit

In 2015, the Hospital entered into a \$6,000,000 revolving bank line of credit expiring on February 20, 2016. At December 31, 2015, there was \$1,944,987 borrowed against this line. The line is collateralized by certain deposit accounts held with the bank. Interest varies with the bank's prime rate less 1.5%, which was 2.0% on December 31, 2015, and is payable monthly. Subsequent to December 31, 2015, the agreement was amended to extend the maturity date to February 2017.

Note 11: Pension Plan

The Hospital contributes to a defined-contribution 403(b) pension plan covering substantially all employees after one year of service. 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 governors. The plan provides retirement and death 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 board of governors. The Hospital will match 50% of the employee's contributions into the plan up to a maximum of 4% contribution by the employee. Employees are 100% vested in their own contributions and are vested on an increasing scale from 0% to 100% over 5 years in Hospital contributions. Hospital contributions aggregated \$184,829 and \$174,413 during 2015 and 2014, respectively.

Note 12: Contingencies

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 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 legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

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Notes to Financial Statements **December 31, 2015 and 2014**

Note 13: 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 required the establishment of health insurance exchanges, which provides 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 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 will be substantially decreased. Each state's participation in an expanded Medicaid program is optional. In 2015, the state of Indiana expanded its Medicaid program with the implementation of the Healthy Indiana Plan (HIP) 2.0. Under HIP 2.0, the first \$2,500 of beneficiary medical expenses are reimbursed from special savings accounts funded partly by the state and partly by the beneficiary.

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 that 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.

Note 14: Long-Term Care Operating Leases and Management Agreements

The Hospital has entered into various agreements to lease the facilities and equipment for the operation of eight nursing homes. Along with the lease agreements, the Hospital also entered into management agreements with the facilities' previous managers (Managers) to continue to operate the facilities. The agreements expire at various times through September 2026 and include optional two to three-year extensions. The management agreements include optional termination clauses by either party if material changes in circumstances, as defined in the agreements, occur. The lease agreements include termination clauses where the leases shall automatically end at the termination of the management agreements between the Hospital and Managers.

The lease agreements call for monthly base rent payments as outlined in the agreements. Certain facilities include annual rent increases of 2% to 5%. Rental expense approximated \$5.5 million and \$173,000 in 2015 and 2014, respectively. See Note 8 for future minimum lease payments, including those due under these lease agreements.

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The management agreements include management fees consisting of base management fees, subordinated management fees and incentive management fees. Base and subordinate management fees are determined on percentages of net patient service revenue of the individual facilities and range from 0.5% to 5.0%. Incentive management fees are to be paid only if sufficient working capital exists. The management agreements also call for quality, royalty and capital improvement fees to be paid to the Managers. Management and other fees approximated \$2.7 million and \$167,000 in 2015 and 2014, respectively, and are included in purchased services and professional fees on the statements of revenues, expenses and changes in net position.

Under the management agreements, the employees necessary to operate the facilities are contracted by the Hospital. The majority of all costs in the ordinary course of business are paid by the Managers who are then reimbursed by the Hospital from operations of the facilities. Similarly, Managers of certain facilities have provided working capital to cover insufficient cash flows from operations. Consequently, the majority of accounts payable and accrued expenses of the long-term care operations approximating \$10.7 million and \$983,000 at December 31, 2015 and 2014 reflect amounts due to Managers.

Note 15: Blended Component Unit

The Hospital's financial statements include the blended component unit accounts of the Foundation. The following is a financial summary of the Foundation as of and for the years ended December 31, 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Current assets	\$ 37,140	\$ 55,988
Noncurrent assets	<u>364,878</u>	<u>411,062</u>
Total assets	<u>\$ 402,018</u>	<u>\$ 467,050</u>
Current and total liabilities	\$ -	\$ -
Net position	<u>402,018</u>	<u>467,050</u>
Total liabilities and net position	<u>\$ 402,018</u>	<u>\$ 467,050</u>
Revenues	\$ 47,713	\$ 54,496
Expenses	<u>112,745</u>	<u>202,008</u>
Increase (decrease) in net position	(65,032)	(147,512)
Net position, beginning of year	<u>467,050</u>	<u>614,562</u>
Net position, end of year	<u>\$ 402,018</u>	<u>\$ 467,050</u>

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Notes to Financial Statements
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Note 16: Subsequent Events

Effective February 1, 2016, the Hospital entered into an additional agreement to lease the facility and equipment for the operation of a nursing home. The lease and management agreements have similar terms as nursing home arrangements currently in place.

Supplementary Information

Daviess Community Hospital
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Combining Balance Sheet Information
December 31, 2015

Assets and Deferred Outflows of Resources

	2015			
	Hospital	LTC	Hospital Foundation	Total
Current Assets				
Cash	\$ 266,941	\$ 4,544,120	\$ 37,140	\$ 4,848,201
Patient accounts receivable, net of allowance of \$2,180,383	7,096,446	4,750,095	-	11,846,541
Supplies	1,189,481	-	-	1,189,481
Prepaid expenses and other	3,872,483	3,979,372	-	7,851,855
Estimated amounts due from third-party payers	339,666	-	-	339,666
Total current assets	<u>12,765,017</u>	<u>13,273,587</u>	<u>37,140</u>	<u>26,075,744</u>
Noncurrent Cash and Investments				
Internally designated	101,042	-	364,878	465,920
Held by trustee for debt service	3,167,413	-	-	3,167,413
	<u>3,268,455</u>	<u>-</u>	<u>364,878</u>	<u>3,633,333</u>
Capital Assets, net	<u>28,175,741</u>	<u>397,563</u>	<u>-</u>	<u>28,573,304</u>
Other Assets	<u>264,497</u>	<u>-</u>	<u>-</u>	<u>264,497</u>
Deferred Outflows of Resources - debt defeasance costs	<u>2,811,152</u>	<u>-</u>	<u>-</u>	<u>2,811,152</u>
Total assets and deferred outflows of resources	<u>\$ 47,284,862</u>	<u>\$ 13,671,150</u>	<u>\$ 402,018</u>	<u>\$ 61,358,030</u>

Liabilities and Net Position

Current Liabilities				
Current maturities of long-term debt	\$ 1,305,726	\$ -	\$ -	\$ 1,305,726
Line of credit	1,944,987	-	-	1,944,987
Interest payable	440,662	-	-	440,662
Accounts payable	2,144,439	2,489,355	-	4,633,794
Accrued expenses	3,310,411	8,233,024	-	11,543,435
Total current liabilities	<u>9,146,225</u>	<u>10,722,379</u>	<u>-</u>	<u>19,868,604</u>
Long-Term Debt	<u>17,905,498</u>	<u>-</u>	<u>-</u>	<u>17,905,498</u>
Total liabilities	<u>27,051,723</u>	<u>10,722,379</u>	<u>-</u>	<u>37,774,102</u>
Net Position				
Net investment in capital assets	8,964,517	-	-	8,964,517
Restricted for debt service	3,167,413	-	-	3,167,413
Unrestricted	8,101,209	2,948,771	402,018	11,451,998
Total net position	<u>20,233,139</u>	<u>2,948,771</u>	<u>402,018</u>	<u>23,583,928</u>
Total liabilities and net position	<u>\$ 47,284,862</u>	<u>\$ 13,671,150</u>	<u>\$ 402,018</u>	<u>\$ 61,358,030</u>

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Combining Balance Sheet Information
December 31, 2014

Assets and Deferred Outflows of Resources

	2014			
	Hospital	LTC	Hospital Foundation	Total
Current Assets				
Cash	\$ 993,896	\$ 87,400	\$ 55,988	\$ 1,137,284
Patient accounts receivable, net of allowance of \$2,570,318	6,035,252	847,298	-	6,882,550
Supplies	1,074,860	-	-	1,074,860
Prepaid expenses and other	3,293,917	-	-	3,293,917
Estimated amounts due from third-party payers	554,122	-	-	554,122
Total current assets	<u>11,952,047</u>	<u>934,698</u>	<u>55,988</u>	<u>12,942,733</u>
Noncurrent Cash and Investments				
Internally designated	1,612,350	-	411,062	2,023,412
Held by trustee for debt service	3,142,988	-	-	3,142,988
	<u>4,755,338</u>	<u>-</u>	<u>411,062</u>	<u>5,166,400</u>
Capital Assets, net	<u>28,294,541</u>	<u>-</u>	<u>-</u>	<u>28,294,541</u>
Other Assets	<u>297,997</u>	<u>60,268</u>	<u>-</u>	<u>358,265</u>
Deferred Outflows of Resources - debt defeasance costs	<u>3,026,017</u>	<u>-</u>	<u>-</u>	<u>3,026,017</u>
Total assets and deferred outflows of resources	<u>\$ 48,325,940</u>	<u>\$ 994,966</u>	<u>\$ 467,050</u>	<u>\$ 49,787,956</u>
Liabilities and Net Position				
Current Liabilities				
Current maturities of long-term debt	\$ 1,020,114	\$ -	\$ -	\$ 1,020,114
Interest payable	462,412	-	-	462,412
Accounts payable	1,951,530	562,293	-	2,513,823
Accrued expenses	3,115,543	421,037	-	3,536,580
Total current liabilities	<u>6,549,599</u>	<u>983,330</u>	<u>-</u>	<u>7,532,929</u>
Long-Term Debt	<u>18,028,143</u>	<u>-</u>	<u>-</u>	<u>18,028,143</u>
Total liabilities	<u>24,577,742</u>	<u>983,330</u>	<u>-</u>	<u>25,561,072</u>
Net Position				
Net investment in capital assets	9,246,284	-	-	9,246,284
Restricted for debt service	3,142,988	-	-	3,142,988
Unrestricted	11,358,926	11,636	467,050	11,837,612
Total net position	<u>23,748,198</u>	<u>11,636</u>	<u>467,050</u>	<u>24,226,884</u>
Total liabilities and net position	<u>\$ 48,325,940</u>	<u>\$ 994,966</u>	<u>\$ 467,050</u>	<u>\$ 49,787,956</u>

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Combining Statement of Revenues, Expenses and
Changes in Net Position Information
Year Ended December 31, 2015

	2015				
	Hospital	LTC	Hospital Foundation	Eliminations	Total
Operating Revenues					
Net patient service revenue, net of provision for uncollectible accounts of \$4,625,215	\$ 54,747,244	\$ 41,176,205	\$ -	\$ -	\$ 95,923,449
Other	1,312,831	5,452,281	-	-	6,765,112
Total operating revenues	<u>56,060,075</u>	<u>46,628,486</u>	<u>-</u>	<u>-</u>	<u>102,688,561</u>
Operating Expenses					
Salaries, wages and contract labor	23,783,048	17,474,624	-	-	41,257,672
Employee benefits	6,250,411	4,548,015	-	-	10,798,426
Purchased services and professional fees	8,618,176	5,890,847	-	-	14,509,023
Supplies	6,638,187	3,252,113	-	-	9,890,300
Insurance	484,196	478,115	-	-	962,311
Utilities	984,676	1,557,605	-	-	2,542,281
Rent	461,997	6,525,665	-	-	6,987,662
Repairs and maintenance	3,009,703	356,567	-	-	3,366,270
Provider hospital assessment fee	2,010,528	-	-	-	2,010,528
Depreciation and amortization	2,993,156	20,928	-	-	3,014,084
Other	1,438,483	5,414,267	112,745	-	6,965,495
Total operating expenses	<u>56,672,561</u>	<u>45,518,746</u>	<u>112,745</u>	<u>-</u>	<u>102,304,052</u>
Operating Income (Loss)	<u>(612,486)</u>	<u>1,109,740</u>	<u>(112,745)</u>	<u>-</u>	<u>384,509</u>
Nonoperating Revenues (Expenses)					
Investment income	48,731	-	2,600	-	51,331
Interest expense	(1,131,657)	-	-	-	(1,131,657)
Other	7,748	-	-	-	7,748
Total nonoperating revenues (expenses)	<u>(1,075,178)</u>	<u>-</u>	<u>2,600</u>	<u>-</u>	<u>(1,072,578)</u>
Excess (Deficiency) of Revenues Over Expenses Before Capital Grants and Contributions	<u>(1,687,664)</u>	<u>1,109,740</u>	<u>(110,145)</u>	<u>-</u>	<u>(688,069)</u>
Transfers	<u>(1,827,395)</u>	<u>1,827,395</u>	<u>-</u>	<u>-</u>	<u>-</u>
Capital Grants and Contributions	<u>-</u>	<u>-</u>	<u>45,113</u>	<u>-</u>	<u>45,113</u>
Increase (Decrease) in Net Position	<u>(3,515,059)</u>	<u>2,937,135</u>	<u>(65,032)</u>	<u>-</u>	<u>(642,956)</u>
Net Position, Beginning of Year	<u>23,748,198</u>	<u>11,636</u>	<u>467,050</u>	<u>-</u>	<u>24,226,884</u>
Net Position, End of Year	<u>\$ 20,233,139</u>	<u>\$ 2,948,771</u>	<u>\$ 402,018</u>	<u>\$ -</u>	<u>\$ 23,583,928</u>

Daviess Community Hospital
A Component Unit of Daviess County, Indiana
Combining Statement of Revenues, Expenses and
Changes in Net Position Information
Year Ended December 31, 2014

	2014				
	Hospital	LTC	Hospital Foundation	Eliminations	Total
Operating Revenues					
Net patient service revenue, net of provision for uncollectible accounts of \$3,299,586	\$ 52,472,072	1,365,514	\$ -	\$ -	\$ 53,837,586
Other	2,157,031	-	-	(150,000)	2,007,031
Total operating revenues	<u>54,629,103</u>	<u>1,365,514</u>	<u>-</u>	<u>(150,000)</u>	<u>55,844,617</u>
Operating Expenses					
Salaries and wages	22,988,337	474,469	-	-	23,462,806
Employee benefits	5,274,560	158,157	-	-	5,432,717
Purchased services and professional fees	8,051,505	317,107	-	-	8,368,612
Supplies	6,050,879	132,857	36,508	-	6,220,244
Insurance	519,158	20,624	-	-	539,782
Utilities	999,055	24,382	-	-	1,023,437
Rent	455,856	153,037	-	-	608,893
Repairs and maintenance	2,869,757	-	-	-	2,869,757
Provider hospital assessment fee	3,598,202	-	-	-	3,598,202
Depreciation and amortization	3,088,725	-	-	-	3,088,725
Other	1,465,657	73,245	165,500	(150,000)	1,554,402
Total operating expenses	<u>55,361,691</u>	<u>1,353,878</u>	<u>202,008</u>	<u>(150,000)</u>	<u>56,767,577</u>
Operating Income (Loss)	<u>(732,588)</u>	<u>11,636</u>	<u>(202,008)</u>	<u>-</u>	<u>(922,960)</u>
Nonoperating Revenues (Expenses)					
Investment income	34,952	-	4,126	-	39,078
Interest expense	(1,165,777)	-	-	-	(1,165,777)
Other	17,967	-	2,750	-	20,717
Total nonoperating revenues (expenses)	<u>(1,112,858)</u>	<u>-</u>	<u>6,876</u>	<u>-</u>	<u>(1,105,982)</u>
Deficiency of Revenues Over Expenses Before Capital Grants and Contributions	<u>(1,845,446)</u>	<u>11,636</u>	<u>(195,132)</u>	<u>-</u>	<u>(2,028,942)</u>
Capital Grants and Contributions	<u>-</u>	<u>-</u>	<u>47,620</u>	<u>-</u>	<u>47,620</u>
Increase (Decrease) in Net Position	<u>(1,845,446)</u>	<u>11,636</u>	<u>(147,512)</u>	<u>-</u>	<u>(1,981,322)</u>
Net Position, Beginning of Year	<u>25,593,644</u>	<u>-</u>	<u>614,562</u>	<u>-</u>	<u>26,208,206</u>
Net Position, End of Year	<u>\$ 23,748,198</u>	<u>\$ 11,636</u>	<u>\$ 467,050</u>	<u>\$ -</u>	<u>\$ 24,226,884</u>

Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance With *Government Auditing Standards*

Board of Governors
Daviess Community Hospital
Washington, Indiana

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Daviess Community Hospital (Hospital), a component unit of Daviess County, Indiana, which comprise the balance sheet as of December 31, 2015, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated May 3, 2016. The financial statements of Daviess Community Hospital Foundation, which is included in the Hospital's financial statements, were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

Management of the Hospital is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered the Hospital's internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Hospital's financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hospital's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to the Hospital's management in a separate letter dated May 3, 2016.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Indianapolis, Indiana
May 3, 2016