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February 10, 2009

Board of Directors
Hancock Regional Hospital
801 North State Street
Greenfield, Indiana 46140

We have reviewed the audit report prepared by Blue & Company, LLC, Independent Public Accountants, for the period January 1, 2007 to December 31, 2007. 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 Hancock Regional Hospital, as of December 31, 2007, 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

HANCOCK REGIONAL HOSPITAL

COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

CPAs / ADVISORS



HANCOCK REGIONAL HOSPITAL

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REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Hancock Regional Hospital
Greenfield, Indiana

We have audited the accompanying combined balance sheets of Hancock Regional Hospital (the Hospital) and component units as of December 31, 2007 and 2006, and the related combined statements of operations and changes in net assets and cash flows for the years then ended. These combined financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

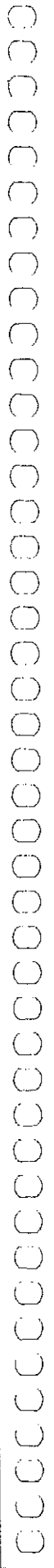
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the Guidelines for Audits of County and City Hospitals by Independent Certified Public Accountants, issued by the Indiana State Board of Accounts. Those standards require that we plan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

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of the Hospital as of December 31, 2007 and 2006, and the results of its combined operations, changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis on pages i through viii is not a required part of the basic combined financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Blue & Co., LLC

April 15, 2008



REQUIRED SUPPLEMENTARY INFORMATION

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

Our discussion and analysis of Hancock Regional Hospitals' financial performance provides an overview of the Hospital's financial activities for the fiscal years ended December 31, 2007 and 2006. Please read it in conjunction with the Hospital's financial statements, which begin on page 2. Unless otherwise indicated, amounts are in thousands.

FINANCIAL HIGHLIGHTS

- The Hospital's net assets increased in each of the past two years with a \$7,141 or 10.26% percent increase in 2007.
- The Hospital reported operating gains in both 2007 of \$6,266 and 2006 of \$3,426.
- Nonoperating revenues increased by \$657 or 301.38% in 2007 compared to 2006.

USING THIS ANNUAL REPORT

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

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

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

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

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

THE STATEMENT OF CASH FLOWS

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

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

THE HOSPITAL'S NET ASSETS

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheet on page 2. The Hospital's net assets increased in each of the past two years with a \$7,141 (10.26 percent) in 2007 as you can see from Table 1.

Table 1: Assets, Liabilities, and Net Assets

	2007	2006	2007 - 2006	
			\$ Change	% Change
Assets				
Current Assets	\$ 27,283	\$ 28,201	\$ (918)	-3.26%
Capital Assets, Net	65,194	64,283	911	1.42%
Restricted and Limited Use Assets	32,632	29,880	2,752	9.21%
Other Noncurrent Assets	6,123	3,649	2,474	67.80%
Total Assets	\$ 131,232	\$ 126,013	\$ 5,219	4.14%
Liabilities				
Long - Term Debt Outstanding	\$ 45,475	\$ 47,297	\$ (1,822)	-3.85%
Other Current and Non Current Liabilities	9,015	9,115	-100	-1.10%
Total Liabilities	\$ 54,490	\$ 56,412	\$ (1,922)	-3.41%
Net Assets				
Unrestricted	\$ 51,666	\$ 48,124	\$ 3,542	7.36%
Invested in Capital Assets, Net of related Debt	17,790	15,061	2,729	18.12%
Restricted by Trustee for Debt Service	6,619	5,940	679	11.43%
Donor Restricted	667	476	191	40.13%
Total Net Assets	\$ 76,742	\$ 69,601	\$ 7,141	10.26%

A significant component of the change in the Hospital's assets is the increase in capital assets net of depreciation. Capital Assets net of Depreciation increased 1.42% or \$911 from 2007 to 2006. Significant capital purchases in 2007 included the construction of a new 48,000 square foot building containing an Outpatient Surgery Center to serve the health needs of the community. Some of the medical equipment additions included a wireless telecommunications system for caregivers, ultrasound imaging equipment, computerized CAD checking, votoc recognition technology to improve the efficiency and accuracy of physician care notes and patient area facility renovations and improvements.

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

OPERATING RESULTS AND CHANGES IN THE HOSPITAL'S NET ASSETS

In 2007, the Hospital's net assets increased by \$7,141 or 10.26%, as shown in Table 2. This increase is made up of very different components.

	2007 - 2006			
	2007	2006	\$ Change	% Change
Operating Revenue				
Net Patient Service Revenue	\$ 79,135	\$ 73,586	\$ 5,549	7.54%
Other	5,729	3,841	1,888	49.15%
Total Operating Revenue	<u>\$ 84,864</u>	<u>\$ 77,427</u>	<u>\$ 7,437</u>	<u>9.61%</u>
Operating Expenses				
Salaries and Benefits	\$ 42,384	\$ 40,883	\$ 1,501	3.67%
Medical Supplies and Drugs	11,691	10,583	1,108	10.47%
Purchased Services and medical fees	15,609	13,598	2,011	14.79%
Depreciation and Amortization	8,223	8,310	(87)	-1.05%
Other Operating Expense	691	627	64	10.21%
Total Operating Expense	<u>\$ 78,598</u>	<u>\$ 74,001</u>	<u>\$ 4,597</u>	<u>6.21%</u>
Operating Income	<u>6,266</u>	<u>3,426</u>	<u>2,840</u>	<u>82.90%</u>
NonOperating Income				
NonOperating Income				
Noncapital Contributions	\$ 336	\$ 491	\$ (155)	-31.57%
Other NonOperating Income	(280)	(322)	42	-13.04%
Interest Expense	(2,491)	(2,797)	306	-10.94%
Investment Income	3,310	2,846	464	16.30%
Total Non Operating Income	<u>\$ 875</u>	<u>\$ 218</u>	<u>\$ 657</u>	<u>301.38%</u>
Excess Revenue and Income over Expense	7,141	3,644	3,497	95.97%
Net Assets				
Beginning Of Year	\$ 69,601	\$ 65,957	\$ 3,644	5.52%
End of Year	<u>\$ 76,742</u>	<u>\$ 69,601</u>	<u>\$ 7,141</u>	<u>10.26%</u>

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

SOURCES OF REVENUE

During 2007, the Hospital derived substantially all of its revenue from patient service and other related activities. Revenue includes, among other items, revenue from the Medicare and Medicaid programs, patients, insurance carriers, preferred provider organizations, and managed care programs.

The table below presents the percentages of Gross revenue for patient services by payer, for the years ended December 31, 2007 and 2006, respectively.

PAYOR MIX

	<u>2007</u>	<u>2006</u>
Medicare	45.93%	46.76%
Medicaid	8.33%	7.94%
Commercial	36.58%	36.97%
Self-Pay	6.46%	5.47%
Other	2.70%	2.87%
	<u>100%</u>	<u>100%</u>

The Hospital provides care to patients under payment arrangement with Medicare, Medicaid, and various managed care programs. Services provided under those arrangements are paid at predetermined rates and /or reimbursable costs as defined. Provisions have been made in the financial statements for contractual adjustments, which represent the difference between the standard charges for services and the actual or estimated payment. It was noted that the payor mix in 2007 shifted from Medicare and Commercial to Medicaid and Self-Pay. This resulted in decreased reimbursement and challenged the maintenance of financial performance compared to the previous year.

OPERATING GAINS

The first component of the overall change in the Hospital's net assets is its operating income, generally the difference between net patient service and the expenses incurred to perform those services. In each of the past two years, the Hospital has reported an operating gain. This is consistent with the Hospital's entire operating history. The Hospital's operations were begun in 1951 as a county owned and operated hospital under Indiana Code 16-22. Operating Gains in 2007 increased by \$2,840 or 82.90% from 2006.

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

The increase in the Hospital's total operating revenue in 2007 of \$7,437 or 9.60% from 2006 is the result of a rate increase and a statistical increase, including real growth in key areas. During 2007, the Hospital increased gross charge rates 8% compared to 2006. More importantly, the Hospital experienced statistical changes in the following areas:

<u>Statistical Growth</u>	<u>2007</u>	<u>2006</u>	<u>2007-2006 % Increase / <Decrease></u>
Patient Days	20,942	23,299	-10.12%
Diagnostic Imaging	58,549	61,986	-5.54%
Lab	377,945	348,224	8.54%
Pharmacy	1,532,037	1,655,498	-7.46%
Rehab Services	84,935	92,001	-7.68%
Home Health Services	41,582	45,167	-7.94%
Outpatient Clinic Services	13,454	10,344	30.07%

Excluded from net patient service revenue are charges for patient service waived under the Hospital's charity care policy. Charity care represents unreimbursed charges incurred by the Hospital in providing uncompensated care to indigent patients. Based on established rates, gross charges of \$2,324 were waived during 2007. Management's commitment to provide emergency care for all patients without regard to their ability to pay contributed to this increase.

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

NON-OPERATING REVENUES AND EXPENSES

Non operating revenues are the result of changes in the Hospital's Investment Income and other Non Capital Grants and Contributions. The Hospital's Investment Income increased due to favorable changes in market values during 2007. The Hospital's Investment Income increased by \$657 or 301.38% from 2006. Market conditions significantly influenced this change.

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2007 AND 2006

GRANTS, CONTRIBUTIONS, AND ENDOWMENTS

The Hospital receives both capital and operating grants from various state and federal agencies for specific programs. These are discussed in detail in Note 10 to the financial statements. Capital and operating grants received in 2007 totaled \$452 compared to 2006 of \$802. Some of the significant grants received by the Hospital are:

- Tobacco Cessation – From Indiana State Department of Health for prevention of tobacco use
- Rural Health Clinic – Knightstown from Indiana State Department of Health – for rural health clinic operations in Knightstown
- Disaster Preparedness – From the State Department of Health – for Community Hospital disaster preparation.
- Lifeline patient monitoring - Central Indiana Power – for remote monitoring of home-bound elderly patients
- Education Department – Substance Abuse Prevention

THE HOSPITAL'S CASH FLOWS

Changes in the Hospital's cash flows are consistent with changes in operations and non-operating revenues and expenses, discussed earlier.

CAPITAL ASSETS AND DEBT ADMINISTRATION

CAPITAL ASSETS

At the end of 2007, the Hospital had \$65.2 million invested in capital assets, net of accumulated depreciation, as detailed in Note 7 to the financial statements.

HANCOCK REGIONAL HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2007 AND 2006

DEBT

At year-end, the Hospital had \$45.5 million in revenue notes, mortgage loans, and capital lease obligations outstanding. The Indiana Bond Bank issued new debt in June 2004 totaling \$35 million pursuant to a Trust Indenture with the Trustee – the Bank of New York Trust Company. The Hancock County Association was created in 2004 under Indiana Code and is authorized to enter into leases with a county to provide funds to the Hospital. The Association issued the Series 2004 C Qualified Obligations pursuant to a Trust Indenture dated June 1, 2004 between the Association and Trustee. This debt was issued for a new 122,000 square foot hospital expansion with the expanded services in Emergency Medicine, Cardiology and Critical Care and an expansion of space for future health needs of the community. The Board of Trustees of the Hospital and Hancock County, Indiana, acting through its Board of Commissioners are lessees with the Association for the Hospital additions and improvements. The Lessee has agreed to make payments directly to the Trustee in amounts and times sufficient to pay in full, when due, the principal and interest of the Series 2004 C Obligations. The County and Hospital anticipate that the full lease rental payments will be paid from Hospital Revenues. This debt consists of Revenue Bonds maturing in January 2031. This transaction is further detailed in Note 8.

CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

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

HANCOCK REGIONAL HOSPITAL

COMBINED BALANCE SHEETS DECEMBER 31, 2007 AND 2006

ASSETS	2007	2006
Current assets		
Cash and cash equivalents	\$ 7,294,162	\$ 5,276,309
Investments	4,658,061	10,257,712
Patient accounts receivable, less allowance for uncollectible accounts of \$11,971,041 in 2007 and \$7,781,630 in 2006	11,526,739	9,805,296
Other receivables	131,939	78,994
Inventories	1,187,752	581,951
Prepaid expenses	634,319	440,242
Current portion of assets whose use is limited	1,850,000	1,760,000
Total current assets	27,282,972	28,200,504
Assets whose use is limited		
Board designated funds	27,195,277	25,224,145
Trustee held funds, less current portion	4,769,141	4,180,319
Donor restricted funds	667,652	476,131
Total assets whose use is limited	32,632,070	29,880,595
Capital assets		
Land and land improvements	4,744,146	4,740,333
Buildings and fixed equipment	84,978,604	84,212,720
Major movable equipment	39,161,815	37,783,709
Construction in progress	7,543,450	968,696
Total capital assets	136,428,015	127,705,458
Less accumulated depreciation	71,234,310	63,422,956
Capital assets, net	65,193,705	64,282,502
Other assets		
Bond issuance costs, net of accumulated amortization of \$204,264 in 2007 and \$182,963 in 2006	278,181	299,482
Other assets	5,845,163	3,350,002
Total other assets	6,123,344	3,649,484
Total assets	\$ 131,232,091	\$ 126,013,085

See accompanying notes to financial statements.

HANCOCK REGIONAL HOSPITAL

COMBINED BALANCE SHEETS DECEMBER 31, 2007 AND 2006

LIABILITIES AND NET ASSETS

	<u>2007</u>	<u>2006</u>
Current liabilities		
Current portion of long-term debt	\$ 1,821,965	\$ 1,720,804
Accounts payable and other liabilities	2,740,028	3,658,712
Accrued salaries and related liabilities	3,509,998	2,918,860
Estimated third-party settlements	942,669	816,472
Total current liabilities	<u>9,014,660</u>	<u>9,114,848</u>
Long-term debt, less current portion	<u>45,474,787</u>	<u>47,297,110</u>
Total liabilities	<u>54,489,447</u>	<u>56,411,958</u>
Net assets		
Unrestricted	51,665,781	48,123,848
Invested in capital assets, net of related debt	17,790,070	15,060,829
Restricted by trustee for debt service	6,619,141	5,940,319
Expendable for specific operating activities	667,652	476,131
Total net assets	<u>76,742,644</u>	<u>69,601,127</u>
Total liabilities and net assets	<u>\$ 131,232,091</u>	<u>\$ 126,013,085</u>

See accompanying notes to financial statements.

HANCOCK REGIONAL HOSPITAL

COMBINED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2007 AND 2006

	2007	2006
Operating revenue		
Net patient service revenue	\$ 79,135,145	\$ 73,585,669
Other operating revenue	5,729,071	3,841,472
Total operating revenue	84,864,216	77,427,141
Operating expenses		
Salaries and wages	33,380,525	32,318,023
Employee benefits	9,003,800	8,565,260
Professional medical fees	1,039,434	993,621
Supplies and drugs	11,690,602	10,582,639
Purchased services	11,981,260	10,210,567
Utilities and insurance	2,588,300	2,393,250
Depreciation and amortization	8,222,710	8,310,181
Other	691,203	627,050
Total operating expenses	78,597,834	74,000,591
Operating income	6,266,382	3,426,550
Nonoperating income (expense)		
Noncapital contributions	335,827	491,582
Other nonoperating income (expense)	(280,142)	(322,097)
Interest expense	(2,490,710)	(2,797,258)
Investment income	3,310,160	2,845,765
Total nonoperating income (expense)	875,135	217,992
Excess revenue and income over expenses	7,141,517	3,644,542
Net assets		
Beginning of year	69,601,127	65,956,585
End of year	\$ 76,742,644	\$ 69,601,127

See accompanying notes to financial statements.

HANCOCK REGIONAL HOSPITAL

COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2007 AND 2006

	2007	2006
Operating activities		
Cash received from patients and third party payors	\$ 77,539,899	\$ 72,330,683
Cash paid to employees for wages and benefits	(41,793,187)	(40,683,723)
Cash paid to vendors for goods and services	(29,762,306)	(23,949,302)
Other operating receipts, net	5,729,071	3,841,472
Net cash from operating activities	<u>11,713,477</u>	<u>11,539,130</u>
Noncapital financing activities		
Noncapital contributions	335,827	491,582
Other nonoperating	(280,142)	(132,899)
Net cash from noncapital financing activities	<u>55,685</u>	<u>358,683</u>
Capital and related financing activities		
Acquisition and construction of capital assets	(9,165,664)	(8,103,886)
Interest expense on long-term debt	(2,490,710)	(2,797,258)
Principal payments on long-term debt, net	(1,721,162)	(865,948)
Net cash from capital and related financing activities	<u>(13,377,536)</u>	<u>(11,767,092)</u>
Investing activities		
Other assets and liabilities	(2,495,161)	(3,198,849)
Investment income	3,310,160	2,845,765
Other change in assets whose use is limited, net	(4,521,252)	(200,093)
Net cash from investing activities	<u>(3,706,253)</u>	<u>(553,177)</u>
Net change in cash and cash equivalents	(5,314,627)	(422,456)
Cash and cash equivalents		
Beginning of year	18,980,737	19,403,193
End of year	<u>\$ 13,666,110</u>	<u>\$ 18,980,737</u>

See accompanying notes to financial statements.

HANCOCK REGIONAL HOSPITAL

COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
Reconciliation of operating income to net cash from operating activities		
Operating income	\$ 6,266,382	\$ 3,426,550
Adjustment to reconcile operating income to net cash from operating activities		
Depreciation and amortization	8,222,710	8,310,181
Bad debts	6,705,779	5,407,183
Changes in assets and liabilities		
Patient accounts receivable	(8,427,222)	(6,272,531)
Other current assets	(852,823)	315,481
Accounts payable and other liabilities	(918,684)	542,344
Accrued salaries and related liabilities	591,138	199,560
Estimated third-party settlements	126,197	(389,638)
Net cash from operating activities	<u>\$ 11,713,477</u>	<u>\$ 11,539,130</u>
 Reconciliation of cash and cash equivalents to the balance sheets		
Cash and cash equivalents:		
In current assets	\$ 7,294,162	\$ 5,276,309
In investments	3,109,288	7,764,109
In assets whose use is limited	<u>3,262,660</u>	<u>5,940,319</u>
Total cash and cash equivalents	<u>\$ 13,666,110</u>	<u>\$ 18,980,737</u>

See accompanying notes to financial statements.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

1. SIGNIFICANT ACCOUNTING POLICIES

Organization and Reporting Entity

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

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

Blended Component Units

The accompanying combined financial statements include the accounts of Hancock Memorial Hospital Foundation, Inc. (the Foundation), a separate not-for-profit entity organized to support the operations of the Hospital. All significant transactions between the Hospital and the Foundation have been eliminated for financial reporting purposes. The accompanying combined financial statements also include the accounts of the Wellness Center, LLC, a separate for-profit entity organized to support the operations of the Hospital. These separate financial statements may be obtained through contacting management of the Hospital.

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. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Proprietary Fund Accounting

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

Accounting Standards

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

Cash and Cash Equivalents

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

Patient Accounts Receivable and Net Patient Service Revenue

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

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

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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

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

Revenue from the Medicare and Medicaid programs accounted for approximately 32 percent and 8 percent, respectively, of the Hospital's net patient revenue for the year ended 2007, and 34 percent and 8 percent, respectively, of the Hospital's net patient revenue, for the year ended 2006. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

The Hospital recognized revenue related to the Medicaid Disproportionate Share Hospital and the Upper Payment Limitation programs of \$2,756,667 and \$1,267,776 for the years ended December 31, 2007 and 2006, respectively. These amounts are reimbursements for providing care to the uninsured and underinsured during periods prior to 2007 and 2006.

This program is a Federal program administered by the state. There is currently a one year moratorium on a change in the regulation related to the eligibility to participate in the program, which if left unchanged would expire in May 2008. The ultimate outcome and potential impact of the change in the regulation is unknown.

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

Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Amounts deemed to be charity care are reported as deductions from revenues.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Combined Statements of Cash Flows

For purposes of the combined statements of cash flows, cash consists of unrestricted cash that is readily available for use in operations. Cash paid for interest, net of amount capitalized in 2007 and 2006 was \$2,460,081 and \$2,691,690 respectively. Capitalized interest was \$241,208 and \$5,012 for 2007 and 2006, respectively.

Inventories

Inventories are valued at the lower of cost (first-in, first-out method) or market.

Assets Whose Use is Limited

These assets include investments designated by the Hospital Board for internal purposes, investments and other assets restricted by donors for a specific purpose and investments held by trustees for debt service and continued construction projects.

Investments in Debt and Equity Securities

Investments in debt and equity securities are reported at fair value except for short-term highly liquid investments that have a remaining maturity at the time they are purchased of one year or less. These investments are carried at amortized cost. Interest, dividends, and gains and losses, both realized and unrealized, on investments in debt and equity securities are included in nonoperating income when earned.

Capital Assets and Depreciation

Capital assets such as property and equipment are stated at cost and include expenditures for new additions and other costs added to existing facilities which exceed \$1,000 and meet certain useful life thresholds. Maintenance, repairs and minor renewals are expensed as incurred. The Hospital provides for depreciation of property and equipment using annual rates, which are sufficient to depreciate the cost of depreciable assets over their estimated useful lives using the straight-line method. The ranges of useful lives in computing depreciation are land improvements 8-15 years, buildings and fixed equipment 5-40 years and major movable equipment 3-20 years.

Costs of Borrowing

Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Bond Issuance Costs

The Hospital provides for the amortization of costs incurred for the issuance of bonds over the life of the debt. Bond issuance costs are amortized over the life of the bond utilizing the straight-line method.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, patient accounts receivable, assets whose use is limited, accounts payable, accrued liabilities, estimated third-party settlements and long-term debt. The carrying amounts reported in the combined balance sheets for cash and cash equivalents, patient accounts receivable, accounts payable, accrued liabilities and estimated third-party settlements approximate fair value. The fair values of assets whose use is limited are estimated based on quoted market prices for those or similar investments.

The fair value of the Hospital's long-term debt is estimated based on market prices for similar issues on current rates offered to the Hospital. The fair value of the Revenue Bonds, Series 1996 and 2004 as of December 31, 2007 and 2006 approximated \$46,017,000 and \$47,160,000, respectively, with a carrying value of \$45,885,000 and 47,645,000, respectively. The fair value of the variable rate obligations is estimated using discounted cash flow analyses, based on the Hospital's current incremental borrowing rates for similar types of borrowing arrangements.

Federal or State Income Taxes

The Hospital is a governmental instrumentality organized under Title 16, Article 12, of the Indiana statutes. The Hospital is exempt from federal income tax as a unit of local government. Hancock Memorial Hospital Foundation, Inc. is a 501(c)(3) not-for-profit organization. Hancock Wellness, LLC is a limited liability company whereby, net taxable income is taxed directly to the members and not the Company.

Investments in Affiliates

The Hospital owns 50% of a Physician Hospital Organization (PHO) and Hancock Health Network, LLC, approximately 37% of Parkway, LLC, and approximately 46% of Hancock Regional Surgery Center, LLC. The investments are recorded on the equity method in the Hospital's combined financial statements. These separate financial statements may be obtained through contacting management of the Hospital.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Compensated Absences

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

Reclassifications

Certain amounts from the 2006 financial statements have been reclassified to conform to the 2007 presentation.

Net Assets

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

Operating Revenues and Expenses

The Hospital's statement of operations and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services which is the Hospital's principal activity. Contributions, investment income, fund development costs and certain other nonhealthcare activities are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Contributions

From time to time, the Hospital receives contributions from individuals and private organizations. Revenues from contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Contributions may be restricted either for specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Restricted Resources

When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources.

Litigation

The Hospital is involved in litigation arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Hospital's future financial position or results from operations.

Risk Management

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

2. CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy. The charity care provided during 2007 and 2006 was \$2,323,923 and \$1,952,885, respectively.

3. INVESTMENTS AND ASSETS WHOSE USE IS LIMITED

Board Designated Funds

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

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Donor Restricted Funds

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

Trustee Held Assets

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

The following represents assets whose use is limited and investments as of December 31, 2007 and 2006:

	<u>2007</u>	<u>2006</u>
Board designated funds	\$ 27,195,277	\$ 25,224,145
Donor restricted funds	667,652	476,131
Trustee held assets for debt service	<u>6,619,141</u>	<u>5,940,319</u>
Total assets whose use is limited	34,482,070	31,640,595
Investments	<u>4,658,061</u>	<u>10,257,712</u>
	<u>\$ 39,140,131</u>	<u>\$ 41,898,307</u>
Hospital mutual funds - equities	\$ 27,974,516	\$ 25,886,663
Foundation mutual funds - equities	1,847,168	1,816,071
Certificates of deposit	195,763	186,952
Money market funds	6,371,948	13,704,428
Government securities	2,512,099	-0-
Other assets	<u>238,697</u>	<u>304,193</u>
	<u>\$ 39,140,191</u>	<u>\$ 41,898,307</u>

4. DEPOSITS AND INVESTMENTS

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

Investments are carried at fair market value. Net realized gains and losses on security transactions are determined on the specific identification cost basis. Assets whose use is limited investments consist of cash equivalents, mutual funds and U.S. Government securities. Market value approximated cost as of December 31, 2007 and 2006.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

The Hospital's investments generally are reported at fair value, as discussed in Note 1. As of December 31, 2007 and 2006, the Hospital had the following investments and maturities, all of which were held in the Hospital's name by custodial banks that are agents of the Hospital.

December 31, 2007

Carrying Amount	Investment Maturities (in years)				
	Less than 1	1-5	6-10	More than 10	
Cash and money market funds	\$ 6,371,948	\$ 6,371,948	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit	195,763	138,769	56,994	-0-	-0-
Mutual funds - equities	29,821,684	29,821,684	-0-	-0-	-0-
Government securities	2,512,039	-0-	-0-	-0-	2,512,039
Other assets	238,697	238,697	-0-	-0-	-0-
\$ 39,140,131	\$ 36,571,098	\$ 56,994	\$ -0-	\$ 2,512,039	

December 31, 2006

Carrying Amount	Investment Maturities (in years)				
	Less than 1	1-5	6-10	More than 10	
Cash and money market funds	\$ 13,704,428	\$ 13,704,428	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit	186,952	-0-	186,952	-0-	-0-
Mutual funds - equities	27,702,734	27,702,734	-0-	-0-	-0-
Other assets	304,193	304,193	-0-	-0-	-0-
\$ 41,898,307	\$ 41,711,355	\$ 186,952	\$ -0-	\$ -0-	

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

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

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

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Deposits and investments consist of the following as of December 31, 2007 and 2006:

	<u>2007</u>	<u>2006</u>
Carrying amount		
Deposits	\$ 7,294,162	\$ 5,276,309
Investments	39,140,131	41,898,307
	<u>\$ 46,434,293</u>	<u>\$ 47,174,616</u>
Included in the balance sheet captions		
Cash and cash equivalents	\$ 7,294,162	\$ 5,276,309
Investments	4,658,061	10,257,712
Current portion of assets whose use is limited	1,850,000	1,760,000
Board designated funds	27,195,277	25,224,145
Trustee held funds, less current portion	4,769,141	4,180,319
Donor restricted funds	667,652	476,131
	<u>\$ 46,434,293</u>	<u>\$ 47,174,616</u>

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

5. ACCOUNTS RECEIVABLE AND PAYABLE

Patient accounts receivable and accounts payable (including expenses) reported as current assets and liabilities as of December 31, 2007 and 2006 is as follows:

	<u>2007</u>	<u>2006</u>
Patient accounts receivable		
Receivable from patients and their insurance carriers	\$ 21,424,354	\$ 15,845,994
Receivable from Medicare	11,198,436	9,012,041
Receivable from Medicaid	<u>2,777,338</u>	<u>2,061,082</u>
Total patient accounts receivable	35,400,128	26,919,117
Less allowance for contractual agreements and uncollectible amounts	<u>(23,873,389)</u>	<u>(17,113,821)</u>
Patient accounts receivable, net	<u>\$ 11,526,739</u>	<u>\$ 9,805,296</u>
Accounts payable and accrued expenses		
Payable to employees (including payroll taxes and benefits)	\$ 3,509,997	\$ 2,918,859
Payable to suppliers	1,523,334	2,374,553
Accrued interest	1,095,691	1,126,320
Other	<u>121,004</u>	<u>157,840</u>
Total accounts payable and accrued expenses	<u>\$ 6,250,026</u>	<u>\$ 6,577,572</u>

6. INVESTMENTS IN AFFILIATES

The Hospital owns 50% of Hancock Health Network, LLC and has recorded the investment on the equity method of accounting in the amount of \$790,223 and \$699,749 as of December 31, 2007 and 2006, respectively. The Hospital paid physicians approximately \$268,000 and \$248,000 during 2007 and 2006, respectively for management and other operating expenses. The Hospital received \$423,108 and \$399,562 for 2007 and 2006, respectively from the Network for rental and housecleaning income. The Hospital contributed capital of \$1,515,341 and \$1,533,713 to the Network during 2007 and 2006, respectively. The Hospital has a receivable from the Network of \$63,987 and \$57,013 as of December 31, 2007 and 2006, respectively. The Hospital expects to continue providing capital contributions to the Network at a commensurate level with its past experience.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

The Hospital owns approximately 37% of Parkway, LLC and has recorded the investment on the equity method of accounting in the amount of \$32,050 and \$221,002 as of December 31, 2007 and 2006, respectively.

The Hospital owns approximately 46% of Hancock Regional Surgery Center, LLC and has recorded the investment on the equity method of accounting in the amount of \$2,803,730 and \$260,930 as of December 31, 2007 and 2006, respectively.

7. CAPITAL ASSETS

Capital assets consist of the following as of December 31, 2007 and 2006:

	Balance December 31, 2006				Balance December 31, 2007
		Additions	Retirements	Transfers	
Land	\$ 270,285	\$ -0-	\$ -0-	\$ -0-	\$ 270,285
Land improvements	4,470,048	-0-	-0-	3,813	4,473,861
Buildings and fixed equipment	84,212,720	658,070	(9,613)	149,077	85,010,254
Major movable equipment	37,783,709	1,714,936	(433,494)	65,014	39,130,165
Construction in progress	968,696	6,792,668	-0-	(217,904)	7,543,450
Total property and equipment	127,705,458	9,165,664	(443,107)	-0-	136,428,015
Less accumulated depreciation					
Land improvements	(1,709,963)	(311,631)	-0-	-0-	(2,021,594)
Buildings and fixed equipment	(38,027,633)	(3,896,354)	1,958	-0-	(41,922,029)
Major movable equipment	(23,685,360)	(3,994,362)	389,035	-0-	(27,290,687)
Total accumulated depreciation	(63,422,956)	(8,202,347)	390,993	-0-	(71,234,310)
Property and equipment, net	\$ 64,282,502	\$ 963,317	\$ (52,114)	\$ -0-	\$ 65,193,705

	Balance December 31, 2005				Balance December 31, 2006
		Additions	Retirements	Transfers	
Land	\$ 270,285	\$ -0-	\$ -0-	\$ -0-	\$ 270,285
Land improvements	4,242,942	-0-	-0-	227,108	4,470,048
Buildings and fixed equipment	78,085,516	776,844	-0-	5,350,360	84,212,720
Major movable equipment	37,936,631	3,283,835	(3,468,407)	31,651	37,783,710
Construction in progress	2,636,327	4,043,207	(101,721)	(5,609,117)	968,696
Total property and equipment	123,171,701	8,103,886	(3,570,128)	-0-	127,705,459
Less accumulated depreciation					
Land improvements	(1,391,036)	(318,927)	-0-	-0-	(1,709,963)
Buildings and fixed equipment	(33,946,417)	(4,081,216)	-0-	-0-	(38,027,633)
Major movable equipment	(23,208,252)	(3,916,980)	3,439,872	-0-	(23,685,360)
Total accumulated depreciation	(58,545,705)	(8,317,123)	3,439,872	-0-	(63,422,956)
Property and equipment, net	\$ 64,625,996	\$ (213,237)	\$ (130,256)	\$ -0-	\$ 64,282,503

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

8. LONG-TERM DEBT

The Hospital issued tax-exempt revenue bonds, dated November 1, 1996, totaling \$20,065,000. The bonds mature serially on an annual basis through August 15, 2017 at interest rates ranging from 5.9% to 6.2%. Interest on these bonds is to be paid semi-annually on February 15 and August 15. Net revenues and certain assets held by the trustee secure the tax-exempt revenue bonds.

The Series 1996 bonds require the Hospital to maintain certain financial debt coverage ratios. As of December 31, 2007 and 2006, the Hospital was in compliance with the debt coverage ratios.

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

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

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

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

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

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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

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

Long-term debt as of December 31, 2007 and 2006 includes the following:

	Balance December 31, 2006	Additions	Reductions	Balance December 31, 2007	Current Portion	Long-Term Portion
The Series 2004 C Obligations Capital Lease	\$ 34,475,000	\$ -0-	\$ (795,000)	\$ 33,680,000	\$ 825,000	\$ 32,855,000
Indiana Health Facility Financing Authority, series 1996	13,170,000	-0-	(965,000)	12,205,000	1,025,000	11,180,000
Note payable; due January 4, 2021; interest rate at 6.75%; real estate and property as collateral	2,110,330	-0-	(78,484)	2,031,846	82,533	1,949,313
Less: unamortized loss on refunding	(737,416)	-0-	117,322	(620,094)	(110,568)	(509,526)
Total long-term debt	<u>\$ 49,017,914</u>	<u>\$ -0-</u>	<u>\$ (1,721,162)</u>	<u>\$ 47,296,752</u>	<u>\$ 1,821,965</u>	<u>\$ 45,474,787</u>
	Balance December 31, 2005	Additions	Reductions	Balance December 31, 2006	Current Portion	Long-Term Portion
The Series 2004 C Obligations Capital Lease	\$ 34,475,000	\$ -0-	\$ -0-	\$ 34,475,000	\$ 795,000	\$ 33,680,000
Indiana Health Facility Financing Authority, series 1996	14,085,000	-0-	(915,000)	13,170,000	965,000	12,205,000
Note payable; due January 4, 2021; interest rate at 6.75%; real estate and property as collateral	2,184,624	-0-	(74,294)	2,110,330	78,126	2,032,204
Less: unamortized loss on refunding	(860,762)	-0-	123,346	(737,416)	(117,322)	(620,094)
Total long-term debt	<u>\$ 49,883,862</u>	<u>\$ -0-</u>	<u>\$ (865,948)</u>	<u>\$ 49,017,914</u>	<u>\$ 1,720,804</u>	<u>\$ 47,297,110</u>

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

Aggregate maturities of long-term debt are as follows:

Year Ending December 31,	Principal	Interest	Total
2008	\$ 1,821,965	\$ 2,527,574	\$ 4,349,539
2009	1,920,907	2,433,004	4,353,911
2010	2,030,654	2,331,272	4,361,926
2011	2,149,580	2,233,494	4,383,074
2012	2,286,304	2,115,564	4,401,868
2013-2017	12,345,174	8,510,118	20,855,292
2018-2022	7,729,625	5,773,557	13,503,182
2023-2027	9,127,543	3,571,261	12,698,804
2028-2031	7,885,000	893,745	8,778,745
	<u>\$ 47,296,752</u>	<u>\$ 30,389,589</u>	<u>\$ 77,686,341</u>

9. PATIENT SERVICE REVENUE

Patient service revenue for 2007 and 2006 consists of the following:

	2007	2006
Inpatient	\$ 49,556,266	\$ 43,624,389
Outpatient	98,067,607	83,396,747
Transitional Care/Inpatient Rehabilitation	4,936,680	7,157,901
Geriatric Psychiatric	3,494,860	3,354,066
Gross patient service revenue	<u>156,055,413</u>	<u>137,533,103</u>
Contractual allowance	67,890,566	56,587,366
Bad debts	6,705,779	5,407,183
Charity care	2,323,923	1,952,885
Deductions from revenue	<u>76,920,268</u>	<u>63,947,434</u>
Net patient service revenue	<u>\$ 79,135,145</u>	<u>\$ 73,585,669</u>

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

10. DONOR RESTRICTED NET ASSETS

Donor restricted net assets are available for the following purposes:

	<u>2007</u>	<u>2006</u>
Specific purpose funds	<u>\$ 667,652</u>	<u>\$ 476,131</u>

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

11. PENSION PLAN

The Hospital offers a defined contribution plan that covers all employees who meet eligibility requirements as to age and length of service and who elect to participate. The Hospital matches 50% of the employee contribution up to 4% of the eligible wages. Pension expense related to the defined contribution plan was \$1,064,594 and \$947,374 in 2007 and 2006, respectively.

12. CONCENTRATION OF CREDIT RISK

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

	<u>2007</u>	<u>2006</u>
Medicare	32%	34%
Medicaid	8%	8%
Other third-party payors	34%	34%
Patients	26%	24%
	<u>100%</u>	<u>100%</u>

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

13. SELF INSURANCE

The Hospital is self insured for employee health claims. A third party administrator processes the claims for the Hospital. The Hospital maintains an estimated liability for the amount of claims incurred but not reported. The Hospital maintains reinsurance including a stop loss for specific incident claims over \$150,000 and an employee life time maximum of \$1,000,000. Substantially all employees are covered for major medical benefits. The total health claims expense was \$5,008,062 and \$5,593,659 for 2007 and 2006, respectively.

Claim expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

Changes in balance of health claim liabilities during the past two years are as follows:

	<u>2007</u>	<u>2006</u>
Unpaid claims estimate, beginning of year	\$ 613,397	\$ 616,982
Incurred claims and changes in estimates	5,008,062	5,593,659
Claims payments	<u>(4,899,022)</u>	<u>(5,597,244)</u>
Unpaid claims estimate, end of year	<u>\$ 722,437</u>	<u>\$ 613,397</u>

14. POSTEMPLOYMENT HEALTHCARE PLAN

The Hospital's defined benefit postemployment healthcare plan, Hancock Regional Hospital Postemployment Healthcare Plan (HRHPHP), provides medical benefits to eligible retired employees and their beneficiaries. The Hospital's estimated obligation to the HRHPHP as of December 31, 2007 is approximately \$200,000 representing the present value of the estimated future cash flows.

HANCOCK REGIONAL HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

15. COMMITMENTS AND CONTINGENCIES

Malpractice Insurance

The Indiana Medical Malpractice Act, IC 27-12 (the Act), provides a recovery for an occurrence of malpractice and for any injury or death of a patient due to an act of malpractice in excess of certain thresholds. The Act requires the Hospital to maintain medical malpractice liability insurance on a per occurrence basis and in the annual aggregate for amounts below the thresholds of the Act. During 2001, the Hospital's malpractice carrier filed bankruptcy. The Hospital has obtained malpractice coverage through another carrier. The Hospital may be liable for certain pending claims incurred while with the former carrier. Management is not aware of any related material adverse effects to its financial condition. Prior to July 1, 1999, the Indiana Medical Malpractice Act provided for a maximum recovery of \$750,000 per occurrence (\$3,000,000 annual aggregate) for professional liability, \$100,000 of which would be paid through the Hospital's malpractice insurance coverage and the balance would be paid by the State of Indiana Patient Compensation Fund. For claims on or after July 1, 1999, the Indiana Medical Malpractice Act provides for a maximum recovery of \$1,250,000 per occurrence (\$7,500,000 annual aggregate) with the first \$250,000 covered by the Hospital's insurance and the remainder by the Fund.

Effective July 1, 2006, the Hospital became a member in a captive insurance company, Suburban Health Organization Segregated Portfolio Company, LLC, to fund the Hospital's required portion of the professional and physician insurance coverage pursuant to the Act as well as its general liability insurance and excess coverage. This provides protection from liability in an amount not to exceed \$250,000 per incident and aggregate liability protection not to exceed \$7,500,000 per year.