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May 11, 2009

Board of Directors
Henry County Hospital
1000 North 16th Street
New Castle, Indiana 47362

We have reviewed the audit report prepared by Blue & Co., LLC, Independent Public Accountants, for the period January 1, 2008 to December 31, 2008. 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 Henry County Hospital, as of December 31, 2008, 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

HENRY COUNTY HOSPITAL

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REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Henry County Hospital
New Castle, Indiana

We have audited the accompanying combined balance sheets of Henry County Hospital (the Hospital), a component unit of Henry County, as of December 31, 2008 and 2007, and the related combined statements of operations, 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 financial statements based on our audits. We did not audit the financial statements of Henry County Hospital Foundation, a blended component unit, which statements reflect total assets of approximately \$29.2 million and \$34.3 million as of December 31, 2008 and 2007, respectively, and total revenues of \$5.4 million and \$5.3 million for the years then ended. We did not audit the financial statements of HCMH Diversified Management Corporation (DMC), a blended component unit, which statements reflect total assets of approximately \$6.7 million and \$6.6 million as of December 31, 2008 and 2007, respectively, and total revenues of \$21.7 million and \$21.0 million for the years then ended. Those financial statements were audited by other auditors whose reports have been furnished to us, and our opinion on the combined financial statements, in so far as it relates to the amounts included for the Foundation and DMC, is based on the report of the other auditors.

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, as 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 and the reports of other auditors provide a reasonable basis for our opinion.

Board of Trustees
Henry County Hospital
New Castle, Indiana

In our opinion, based on our audits and the reports of other auditors, the combined financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of December 31, 2008 and 2007 and the results of its 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.

Our audits were performed for the purpose of expressing an opinion on the combined financial statements taken as a whole. The combining financial statements and schedule listed in the table of contents are presented for purposes of additional analysis and are not a required part of the combined financial statements of the Hospital. This information has been subjected to the auditing procedures applied in our audits and the audits of the other auditors, and in our opinion and the opinion of the other auditors, is fairly stated, in all material respects in relation to the combined financial statements taken as a whole.

Management's discussion and analysis, on pages i through xii, 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 12, 2009

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

Our discussion and analysis of Henry County Hospital's (the Hospital or HCH) financial performance provides an overview of the Hospital's financial activities for the fiscal years ended December 31, 2008 and 2007. Please read it in conjunction with the Hospital's financial statements, which begin on page 3. As mentioned in Note 1, the financial statements include the Hospital, as well as Henry County Hospital Foundation, Inc. and HCH Diversified Management Corporation (DMC).

USING THIS ANNUAL REPORT

The Hospital's financial statements consist of 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.

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

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

These 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 our 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 we provide to the community, as well as local economic factors to assess the overall health of the Hospital.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

THE STATEMENT OF CASH FLOWS

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

THE HOSPITAL'S NET ASSETS

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheet on page 3. The Hospital's net assets decreased by \$3,290,839 or 5% in 2008 as you can see from Table 1.

Table 1: Assets, Liabilities and Net Assets:

	<u>2008</u>	<u>2007</u>
Assets		
Current assets	\$ 28,174,466	\$ 18,952,797
Capital assets, net	45,557,589	48,270,665
Other investments and assets	19,919,085	30,856,809
Total assets	<u>93,651,140</u>	<u>98,080,271</u>
Liabilities		
Debt outstanding, current and long-term	22,759,498	24,283,835
Other current and noncurrent liabilities	8,764,962	8,378,917
Total liabilities	<u>31,524,460</u>	<u>32,662,752</u>
Net assets		
Invested in capital assets, net of related debt	22,798,091	23,986,830
Restricted for debt service	157,261	277,113
Restricted expendable net assets	8,856,380	9,454,780
Unrestricted	30,314,948	31,698,796
Total net assets	<u>\$ 62,126,680</u>	<u>\$ 65,417,519</u>

There are no major shifts between 2008 and 2007, showing the stability of the Hospital and its operations.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

OPERATING RESULTS AND CHANGES IN THE HOSPITAL'S NET ASSETS

In 2008, the Hospital's net assets decreased by \$3,290,839 or 5% as shown in Table 2.

Table 2: Operating Results and Changes in Net Assets

	2008	2007
Operating revenues		
Net patient service revenues	\$ 87,882,799	\$ 79,254,153
Other operating revenues	4,117,740	4,063,173
Total operating revenues	<u>92,000,539</u>	<u>83,317,326</u>
Operating expenses		
Salaries and benefits	49,892,646	47,588,519
Medical supplies and drugs	13,438,082	13,315,085
Depreciation and amortization	5,551,546	5,706,952
Other operating expenses	18,369,787	16,509,967
Total operating expenses	<u>87,252,061</u>	<u>83,120,523</u>
Operating income	4,748,478	196,803
Non-operating revenues and expenses		
Investment income	(7,268,246)	1,996,507
Other non-operating revenues and expenses, net	(771,071)	(813,959)
Total non-operating revenues (expenses)	<u>(8,039,317)</u>	<u>1,182,548</u>
Change in net assets	(3,290,839)	1,379,351
Net assets beginning of year	<u>65,417,519</u>	<u>64,038,168</u>
Net assets end of year	<u>\$ 62,126,680</u>	<u>\$ 65,417,519</u>

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

OPERATING INCOME

Hospitals throughout the U.S. were shaken in the last quarter of 2008 as a result of the economic crisis, increased cost of credit when attainable and the downgrading by Moody's of the healthcare industry outlook from stable to negative. These factors will also make 2009 an unpredictable year in healthcare.

The economic crisis began affecting HCH in October with a decrease in admissions, outpatient registrations and emergency department visits and admissions. We anticipate that volumes will continue to soften in 2009 as unemployment rises and as companies shift more health insurance costs to employees.

HCH was impacted by the market volatility for the variable rate demand bond market and the Letter of Credit problems that resulted from struggling regional banks. The Hospital is working closely with outside advisors to analyze and assist HCH in obtaining a more permanent solution to these two serious problems.

In 2008 the impact at HCH was not as severe as at some hospitals that began cutting staff in the 4th quarter. HCH has been proactive in looking at ways to decrease expenses through LEAN and reduce FTE's without compromising care. A low turnover rate of 8% for all staff and 5% for RNs in 2008 helped reduce recruitment and training expenses. There is also a continuing focus on increasing revenue through enhanced program development, increasing the physician base and marketing activities.

The decline in outpatient surgeries that started in 2006 was reversed with a gain of nearly 2% in 2008. This is primarily related to the addition of Matthew Barrett, M.D., a third general surgeon who joined our staff in August 2007. The decline in Hospice and Wound Care visits was also reversed in 2008. Obstetrics volumes declined primarily as a result of a decrease from four to three physicians delivering at HCH. The mammography decline was due to the loss of equipment for nearly a month due to needed repairs.

<u>Service</u>	<u>Volume Change 2007-2008</u>
Admissions (excluding newborns)	-0.14%
Emergency Department Visits	+4.35%
Outpatient Registrations	-1.26%
Deliveries	-16.86%
Inpatient Surgeries	+2.29%
Outpatient Surgeries	+1.98%
CT Scans	+17.75%
Nuclear Scans	+22.12%
MRI Scans	-0.82%
Mammography	-18.09%
Home Health	+19.91%

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

Hospice	+28.05%
Wound Care	+13.84%
Sleep Center	-5.76%

BAD DEBT RISING DRAMATICALLY

Bad debt and charity care continue to increase. To try to help slow this increase in 2008 HCH began offering ClaimAid, a free program to help residents apply for government funded health insurance such as Medicaid. ClaimAid will help increase revenue to HCH and also provide better access to medical care for residents of our community who qualify for these programs.

This continued increase is related to the downturn in the economy, loss of health insurance by laid-off workers, increasing self pay and the higher co-pays and deductibles now required by many insurance plans.

HCH also has seen a payor mix change with an increase of 4.5% since 2004 in Medicare, Medicaid and self-pay patients.

These increases further point to the need to expand revenue sources and reduce expenses in order to maintain an adequate operating margin.

	<u>Bad Debt</u>	<u>Charity</u>	<u>Total</u>	<u>% Chg</u>
2004	\$2,572,753	\$2,302,176	\$4,874,929	
2005	\$2,513,837	\$3,041,023	\$5,554,860	13.95%
2006	\$2,381,820	\$4,909,890	\$7,291,710	31.26%
2007	\$4,289,252	\$5,296,468	\$9,585,720	31.46%
2008	\$3,331,450	\$7,236,232	\$10,567,682	10.24%

STRATEGIC PLANNING AND PHYSICIAN RECRUITMENT

The 2008 Strategic Plan highlighted the need to improve retention of appropriate medical services within our system. While it showed that our market share had improved, the plan cautioned that we must maintain and improve programs so that we do not lose market share. Improved primary care access will focus on recruitment efforts as well as working with our current primary care physicians to determine if they can increase their availability. Issues identified in the Strategic Plan will be addressed throughout 2009.

We are continuing to recruit new physicians in family medicine and internal medicine. A Hospitalist program was implemented third-quarter 2008 which will improve our ability to recruit primary care physicians.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

In 2008 a new pediatrician, anesthesiologist and internist joined Henry County Hospital Medical Group—the Hospital's employed physician practices. A new orthopedic surgeon has been recruited for 2009.

MARKETING FOCUSES ON PRIMARY SERVICE AREAS

We continue to focus marketing efforts on our primary service areas. Advertising in 2008 focused on increasing awareness of the cardiology services offered by Nathan Millikan, M.D., FACC and the addition of new physicians to our staff.

The Hospital continues to work on expanding market share in western Wayne County and areas of Henry County outside of New Castle. Our physician liaison regularly calls on physicians practicing in those areas who are not members of the HCH medical staff to encourage them to use HCH services. Direct mail, publicity, advertising and billboards are used to inform local residents about HCH services.

A new Hospital web site debuted in spring, 2008 followed by a new website for Henry County Hospital Medical Group. E-marketing efforts will continue to accelerate in 2009. A new Parish Nurse program provides information about HCH services as well as helping faith communities develop their own Parish Nurse Program. The Hospital participates in numerous health fairs and other community health-related projects.

General surgeons and two obstetricians/gynecologists expanded their service area and began seeing patients and performing outpatient surgery at St. Vincent Medical Center Northeast in Fishers which opened in the fall.

REVENUE ENHANCEMENT ALSO LOOKS TO DECREASED EXPENSES

HCH began LEAN in 2006, and it has become an integral part of the operational system in the Hospital and in employed physician practices.

In 2008 fourteen Rapid Improvement Events were held throughout the Hospital and in physician offices to streamline workflow, improve efficiency and reduce costs. Participating departments include:

- Dietary
- Imaging
- Progressive Care Unit
- Surgery
- Surgery/Physician Offices
- Pharmacy
- Respiratory Care
- New Castle Pediatrics
- Medical Records

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

Six Value Stream Mapping Events (VSA) were held in Human Resources, Pharmacy, Respiratory Care, Dietary, Imaging and Registration to help determine what processes should be targeted for a Rapid Improvement Event.

HENRY COUNTY HOSPITAL MEDICAL GROUP

Henry County Hospital Medical Group is a part of the Henry County Hospital "family" serving Henry, northern Rush and western Wayne counties. It includes 31 physicians providing a wide range of primary care and specialty services. The physicians in the group are 96% board certified/board eligible.

Physician practices include family medicine, pediatrics, obstetrics/gynecology, cardiology, general surgery, anesthesiology and orthopedics.

We consolidated New Castle Pediatrics and New Castle Clinic billing services into the Centralized Billing Office for the system. We have used our LEAN Operational Improvement Team to begin analyzing workflows in the physician offices.

New Castle Family Physicians has utilized NextGen Electronic Medical Record (EMR) since 1999. They began upgrading their current NextGen system in the fall of 2008. New Castle Pediatrics was one of the first EMR adopters in Indiana. They will convert their current system to NextGen in 2009.

New Castle Family Physicians participated in Diabetes Measurements 1, 2, 3 for the 2007 CMS Physician Quality Reporting Initiative (PQRI). They are one of the early practice leaders in this initiative.

COMMUNITY BENEFITS

HCH provided just over \$7.2 million in charity care in 2008 which is an increase of nearly \$2,000,000 from 2007. The Hospital provides health education programs including childbirth classes, diabetes classes, smoking cessation and stress management. We also participate in a number of community initiatives including health fairs and Community Matters, an initiative to decrease obesity. Henry County Sports Medicine provides low-cost game coverage, injury checks and performance enhancement programs for area high schools. HCH is the county's largest employer and also contributes a significant economic impact through payroll, local purchasing when possible and employee involvement in the community.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

CLINICAL CAPABILITIES EXPAND FOR ELECTRONIC HEALTH RECORDS

Soarian™, our electronic health record, continues to expand online clinical capabilities for our physicians and staff.

Henry County Hospital Pharmacy installed a new Siemens Pharmacy System in preparation for the implementation of a new Medication Administration Check (MAK) scheduled for March 2009. MAK is an electronic medication administration process which involves scanning the medication and the patient's identification bracelet prior to giving medications. If there is a discrepancy with either, the system will alert the caregiver. The MAK system also includes electronic documentation of medications. This helps to ensure patient safety by verifying the patient is receiving the correct medication.

Epiphany, a new cardiology system that eliminates "paper" results for Holter Monitors and EKGs, was installed in 2008. With Epiphany, physicians can electronically read, interpret and sign studies. This information will then be pushed to Soarian™. Stress tests will be added to Epiphany in 2009.

Fusion, our new dictation system, is interfaced with Soarian™. It decreases turnaround time for dictation by having the dictation, transcription and Business One systems interfaced to streamline the transcription process. Fusion also has front and backend speech recognition capabilities.

Radiologist's reports and images such as chest x-rays can now be viewed through Soarian™. An upgraded work station application now allows quicker logins. All alerts related to nursing care plans are in the process of development.

IMAGING UPGRADES PACS - BEGINS PLANNING FOR DIGITAL MAMMOGRAPHY

Imaging is upgrading the Philips I-Site PACS system so that it can accommodate a new Digital Mammography System which is expected to be installed in 2009. The current PACS system is totally integrated with our electronic health record Soarian™ providing improved work flow and turnaround time.

PATIENT SATISFACTION EMPHASIS CONTINUES

HCH exceeded national and state averages in all but one category in the Medicare HCAHPS patient survey. Individuals choosing the top scores of 9 and 10 for the overall rating gave HCH a 71% compared to a state average of 67% and a national average of 64%. Seventy percent indicated they would "definitely recommend" compared to 69% for the state average and 68% for the national average.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

Our goal for 2009 continues to be in the 90th percentile or above on Inpatient, Outpatient and Emergency Department patient surveys from Press Ganey.

Our average scores in 2008 were:

- Inpatient 90%
- Emergency Department 76%
- Outpatient 53%

The Inpatient average dropped 1%, the Emergency Department average improved by 3%, and the Outpatient average dropped by 10% from our 2007 scores. Problems have been identified with the outpatient data transmission with corrections to be implemented in 1st quarter 2009. The low volume of the surveys returned compared to the volume of patients makes it difficult to improve, but each of the outpatient departments is addressing issues identified and implementing actions for improvement.

All employees are required to participate in customer service training. Discharge phone calls are made to assess patient satisfaction and a formalized service recovery program is ongoing. Inpatient nursing units have initiated hourly rounding to proactively address patient needs. Focus has been on addressing needs for improvement identified in the HCAHPS survey. The Hospital also has an ongoing employee recognition program for superior customer service.

PATIENT SAFETY FOCUSES ON MULTIPLE MEASUREMENTS AND AREAS

Henry County Hospital is accredited by the Healthcare Facilities Accreditation Program (HFAP). Our triennial survey was conducted in 2008 with full accreditation received.

HCH is participating in numerous local and national patient safety measurements. Our goal in 2008 was to obtain 90% or above for CMS measures for heart failure, AMI (heart attack), surgical complication improvement program (SCIP) and pneumonia. This goal was reached in all measures but one pneumonia measure which was 89% for the 3rd quarter of 2008, the last reporting period available. The goal for 2009 was increased to 98%.

An electronic incident reporting system, Event Management System (EMS), was implemented in collaboration with other Suburban Health Organization (SHO) hospitals. The system is user friendly and has reporting capabilities for the individual department as well as hospital-wide, and enables the SHO participating hospitals to compare data and identify opportunities for improvement.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

HCH also uses national Quality Forum's patient safety indicators as guidelines for patient safety improvement. The Hospital is also part of the Surgical Care Improvement Project (SCIP) collaborative with Health Care Excel.

Indiana has an Adverse Event Reporting program and HCH had no reportable adverse events in 2008. HCH also participates in the Institute for Healthcare Improvement (IHI) 5 Million Lives Campaign and a Best Practice Sharing with other Suburban Health Organization hospitals on areas that relate to CMS measures and Anthem Quality Scorecard issues. The hospital-wide performance improvement team for 2008 focused on the areas of implementation of the electronic health record. Individual department teams focused on improving quality and safety issues identified within their department.

CMS initiated a reduction in payment for certain hospital acquired conditions. Conditions must be identified as "Present on Admission (POA)" through billing codes. Extensive education was provided to the medical records staff to identify these conditions accurately for coding. We are participating with the Indiana Hospital Association to develop a reporting system to assist hospitals in identifying missed opportunities through incorrect coding and to capture financial data as a result of hospital acquired condition.

Nursing staff in collaboration with the Wound Care Center staff have developed a system for assessing and accurately staging pressure ulcer sores on admission. Standard Care Bundles have been implemented to prevent blood stream infections and ventilator associated pneumonia. The Infection Control Coordinator is developing a program to reduce Foley Catheter usage in an effort to reduce catheter-associated urinary tract infections.

Installation of the Pyxis PAR_x[®] system in the Pharmacy in 2008 provided improved patient safety and supports compliance with HFAP requirements. The Pyxis PAR_x[®] system automates the pick-check-delivery process to provide increased security during medication replenishment throughout the Hospital. The system utilizes bar code scanning technology for real-time tracking and monitoring of medication handling, pharmacist review and delivery of medications. By providing a complete chain-of-custody on medications during distribution to the nursing unit and helping to ensure the right medication is getting to the right station and the right pocket in the station, the Pyxis PAR_x[®] system is a valuable technology that provides improved patient safety.

The Pharmacy became compliant with USP Chapter 797(1) in April, 2008 when the final piece of equipment needed for compliance was installed. Enacted January 1, 2004, USP Chapter 797(1) presents the first enforceable standards for sterile compounding to help ensure consistent practices across the US and to require that compounding rooms (such as where IVs are prepared) have the same cleanliness standards as a surgical suite. All practice settings where sterile preparations are compounded were expected to be compliant with the new regulations by June, 2008.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

SCHOLARSHIPS AND "TEACHING HOSPITAL" AID RECRUITMENT

Henry County Hospital is a "teaching" hospital that not only helps train medical professionals, but also aids HCH recruitment. Each year students take various clinical rotations at HCH and are often hired as permanent staff. We serve as a clinical site for Ivy Tech State College's two-year RN program in New Castle, their Anderson RN program and their Richmond LPN program. We also are a clinical site for Ivy Tech's Surgical Technician program, for the School of Radiological Technology at Hancock Regional Hospital and training for Butler University's Pharmacy program.

Each year 20-25 high school seniors spend mornings at Henry County Hospital in a variety of clinical settings through a Health Occupations program sponsored by New Castle Vocational Schools for college bound students interested in healthcare careers.

The Dr. Cloyd L. and Mary Lou Dye scholarship fund provides financial support for medical students, interns, residents and fellows. Six scholarships were awarded in 2008 to Henry County residents.

The Henry County Hospital Foundation offers a variety of scholarships for students interested in health care careers and working at Henry County Hospital after graduation. They are available for high school seniors as well as for adults who are considering a new or second career in health care.

In the last four years 98 nursing and other healthcare scholarships worth \$164,645 have been awarded. Funding for the scholarships comes from the Foundation's annual Gala and Employee Silent Auction, the HCH Cookbook, donations from the Henry County Hospital Auxiliary and endowments established by Sylvira Flanagan Koons, Alice Catherine Ratcliffe, LaVaughn Bailey, Gordon Sparks and Ralph Bunner.

CAPITAL ASSET AND DEBT ADMINISTRATION

CAPITAL ASSETS

At the end of 2008, the Hospital had \$45.6 million invested in capital assets, net of accumulated depreciation, as detailed in note 7 to the financial statements. In 2008 and 2007, the Hospital purchased new capital assets in the amount of \$2.8 million and \$1.8 million, respectively.

HENRY COUNTY HOSPITAL

MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 2008 AND 2007

DEBT

At year-end, the Hospital had \$22.8 million in revenue notes, mortgage loans, and capital lease obligations outstanding as detailed in note 8 to the financial statements. New debt in the amount of \$5.9 million was issued during 2008 to retire the Series 1985 revenue bonds.

CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

This financial report is designed to provide our patients, county residents, suppliers 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 Controller, Henry County Hospital, 1000 North 16th Street, New Castle, Indiana 47362.

HENRY COUNTY HOSPITAL

COMBINED BALANCE SHEETS DECEMBER 31, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 10,013,119	\$ 5,441,917
Restricted cash equivalents	310,323	262,543
Patient accounts receivable, net of estimated allowance for uncollectible accounts of \$3,643,609 in 2008 and \$4,049,938 in 2007	10,010,838	10,892,478
Supplies and other current assets	1,463,848	1,177,871
Current portion of assets whose use is limited	<u>6,376,338</u>	<u>1,177,988</u>
Total current assets	28,174,466	18,952,797
Investments	12,913,050	18,107,964
Assets whose use is limited		
Internally designated	8,073,745	8,558,746
Held by trustee	<u>157,261</u>	<u>277,113</u>
	8,231,006	8,835,859
Less current portion	<u>6,376,338</u>	<u>1,177,988</u>
Total assets whose use is limited	1,854,668	7,657,871
Capital assets, net	45,557,589	48,270,665
Other assets	5,151,367	5,090,974
Total assets	<u>\$ 93,651,140</u>	<u>\$ 98,080,271</u>

See accompanying notes to combined financial statements.

HENRY COUNTY HOSPITAL

COMBINED BALANCE SHEETS
DECEMBER 31, 2008 AND 2007

LIABILITIES AND NET ASSETS

	2008	2007
Current liabilities		
Current portion of long-term debt	\$ 7,121,671	\$ 2,085,514
Accounts payable and accrued expenses	4,677,113	4,641,118
Accrued wages and related liabilities	3,574,517	3,223,313
Estimated third-party settlements	382,187	434,486
Total current liabilities	<u>15,755,488</u>	<u>10,384,431</u>
Other long-term liabilities	131,145	80,000
Long-term debt, net of current portion	<u>15,637,827</u>	<u>22,198,321</u>
Total liabilities	31,524,460	32,662,752
Net assets		
Unrestricted	30,314,948	31,698,796
Invested in capital assets, net of related debt	22,798,091	23,986,830
Restricted		
Expendable - debt service	157,261	277,113
Expendable - funded depreciation	8,073,745	8,558,746
By donor - expendable - for capital acquisition	782,635	896,034
Total net assets	<u>62,126,680</u>	<u>65,417,519</u>
Total liabilities and net assets	<u>\$ 93,651,140</u>	<u>\$ 98,080,271</u>

See accompanying notes to combined financial statements.

HENRY COUNTY HOSPITAL

COMBINED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
Operating revenue		
Net patient service revenue	\$ 87,882,799	\$ 79,254,153
Other revenue	4,117,740	4,063,173
Total revenue	<u>92,000,539</u>	<u>83,317,326</u>
Operating expenses		
Salaries and benefits	49,892,646	47,588,519
Medical professional fees	3,028,477	2,165,451
Other professional fees	5,436,338	4,980,917
Medical supplies and drugs	13,438,082	13,315,085
Other supplies	1,163,249	876,978
Depreciation and amortization	5,551,546	5,706,952
Utilities	1,507,138	1,535,870
Rent	877,150	862,682
Other	6,357,435	6,088,069
Total expenses	<u>87,252,061</u>	<u>83,120,523</u>
Operating income	4,748,478	196,803
Nonoperating income		
Investment income	(7,268,246)	1,996,507
Interest expense	(1,172,637)	(1,201,519)
Other nonoperating	401,566	387,560
Total nonoperating income (expense)	<u>(8,039,317)</u>	<u>1,182,548</u>
Change in net assets	(3,290,839)	1,379,351
Net assets		
Beginning of year	65,417,519	64,038,168
End of year	<u>\$ 62,126,680</u>	<u>\$ 65,417,519</u>

See accompanying notes to combined financial statements.

HENRY COUNTY HOSPITAL

COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
Cash flows from operating activities		
Cash received from patients and third party payors	\$ 88,712,140	\$ 78,589,333
Cash paid to employees for wages and benefits	(49,541,442)	(47,354,074)
Cash paid to vendors for goods and services	(29,423,862)	(26,868,701)
Other operating receipts, net	1,535,196	3,074,849
Net cash flows from operating activities	<u>11,282,032</u>	<u>7,441,407</u>
Cash flows from noncapital financing activities		
Other nonoperating	401,566	387,560
Net cash flows from noncapital financing activities	<u>401,566</u>	<u>387,560</u>
Cash flows from capital and related financing activities		
Acquisition and construction of capital assets	(2,691,846)	(1,633,136)
Interest expense on long-term debt	(1,172,637)	(1,201,519)
Proceeds from issuance of long-term debt	5,908,091	-0-
Principal payments on long-term debt, net	(7,501,105)	(1,840,898)
Net cash flows from capital and related financing activities	<u>(5,457,497)</u>	<u>(4,675,553)</u>
Cash flows from investing activities		
Investment income	(7,268,246)	1,996,507
Other assets	(60,393)	(24,488)
Change in assets whose use is limited, net	604,853	(656,006)
Change in investments, net	4,404,700	(1,646,865)
Net cash flows from investing activities	<u>(2,319,086)</u>	<u>(330,852)</u>
Net change in cash and cash equivalents	3,907,015	2,822,562
Cash and cash equivalents		
Beginning of year	6,461,922	3,639,360
End of year	<u>\$ 10,368,937</u>	<u>\$ 6,461,922</u>

See accompanying notes to combined financial statements.

HENRY COUNTY HOSPITAL

COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
Reconciliation of operating income to net cash flows from operating activities		
Operating income	\$ 4,748,478	\$ 196,803
Adjustment to reconcile operating income to net cash flows from operating activities		
Depreciation and amortization	5,551,546	5,706,952
(Gain)/loss on disposal of assets	300	25,720
Bad debts	3,331,450	4,289,252
Changes in assets and liabilities		
Patient accounts receivable	(2,449,810)	(4,875,140)
Supplies and other current assets	(285,977)	1,285,256
Accounts payable and accrued expenses	35,995	737,051
Accrued salaries and related liabilities	351,204	234,445
Other long-term liabilities	51,145	(80,000)
Estimated third-party settlements	(52,299)	(78,932)
Net cash flows from operating activities	<u>\$ 11,282,032</u>	<u>\$ 7,441,407</u>
Reconciliation of cash and cash equivalents to the balance sheets		
Cash and cash equivalents		
In current assets	\$ 10,323,442	\$ 5,704,460
In investments and assets whose use is limited	45,495	757,462
Total cash and cash equivalents	<u>\$ 10,368,937</u>	<u>\$ 6,461,922</u>

See accompanying notes to combined financial statements.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

1. SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Henry County Memorial Hospital d/b/a Henry County Hospital (the Hospital) is a county owned facility and operates under the Indiana County Hospital Law, Indiana Code 16-22. The Hospital provides short-term inpatient and outpatient healthcare.

The Board of County Commissioners of Henry County appoints the Governing Board of the Hospital (Board) and a financial benefit/burden relationship exists between the County and the Hospital. For these reasons, the Hospital is considered a component unit of Henry County.

On June 7, 1976, the Board of County Commissioners of Henry County, upon written request of the Henry County Hospital Board of Trustees created the Henry County Hospital Association. The Association was created pursuant to the provisions of Indiana Code 16-22-6 for the exclusive purpose of financing and constructing hospital facilities for the Hospital.

The component units discussed below are included in the Hospital's reporting entity because of the significance of their operational or financial relationships with the Hospital.

Blended Component Units

Henry County Hospital Foundation, Inc. (the Foundation), is a significant component unit of the Hospital. The Hospital appoints a voting majority of the Foundation's Board of Directors and a financial benefit/burden relationship exists between the Hospital and the Foundation. Although it is legally separate from the Hospital, the Foundation is reported as if it were a part of the Hospital because it provides services entirely or almost entirely to the Hospital.

The activities of the Foundation may include capital improvements, educational programs, medical related research and initial capital for experimental health services related to the principal purpose of the Hospital. The Foundation also manages investments and rental property, provides equipment, grants scholarships for health careers, conducts physician recruitment and other medical programs as directed under the terms of a contract with the Hospital. The Foundation's separate audited financial statements can be obtained by contacting the Foundation.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

HCMH Diversified Management Corporation (DMC) is a significant component unit of the Hospital. The Hospital is the sole shareholder and appoints DMC's Board of Directors and is able to impose its will. Although it is legally separate from the Hospital, DMC is reported as if it were a part of the Hospital because the two Boards of Directors/Trustees are substantially the same.

DMC provides laboratory services to the patients of New Castle Family Physicians, nursing homes, employees of the Hospital, physicians and veterinarians in the surrounding area. The performance of tests on the specimens collected by DMC is purchased from the Hospital. DMC also provides pharmacy services to the surrounding communities. DMC's separate audited financial statements can be obtained by directly contacting DMC.

DMC owns Henry County Urgent Care, LLC. Urgent Care, LLC operates an emergency care physician office located in a shopping center in New Castle.

DMC owns New Castle Clinic, Inc., which operates a physician group practice. DMC's results within these financials include those of the Clinic for the years ended December 31, 2008 and 2007.

All intercompany accounts and transactions have been eliminated.

Use of Estimates

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

Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Because the Hospital does not collect amounts deemed to be charity care, they are not reported as revenue.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Enterprise Fund Accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits and investments in highly liquid debt instruments with an original maturity of three months or less.

Restricted Cash Equivalents

The restricted cash equivalents consist of money market investments accumulated from monthly deposits the Hospital and Foundation are required to make to the Trustee for long-term bonds for payment of interest and bond principal that matures each April.

Patient Accounts Receivable, Net and Net Patient Service Revenues

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

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. At the Hospital's year-end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients. The difference between computed reimbursement and interim reimbursement is reflected as a receivable from or payable to the third-party program. These programs have audited the year-end cost report filed with the Medicare program through December 31, 2006, with differences reflected as deductions from revenue in 2008. Amounts for the unresolved cost reports as well as other allowances are reflected in estimated third-party settlements on the balance sheets.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Revenue from Medicare and Medicaid programs accounted for approximately 36 percent and 6 percent for the year ended 2008 and 37 percent and 6 percent for the year ended 2007.

Combined Statements of Cash Flows

For purposes of the combined statements of cash flows, cash consists of cash that is readily available for use in operations. Cash paid for interest was approximately \$1,172,000 and \$1,201,000 for 2008 and 2007, respectively.

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.

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 long-term debt also approximates the carrying value.

Assets Whose Use Is Limited

Assets whose use is limited consists of investments and includes assets that are trustee-held funds for the retirement of debt obligations and assets internally designated by the Board for acquisition of property and equipment and debt service.

Bond Issue Costs

The Hospital provides for the amortization of costs incurred for the issuance of bonds over the life of the debt. Amortization expense for 2008 and 2007 was \$39,914 and \$62,172, respectively.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Capital Assets

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. Contributed capital assets are reported at their estimated fair market value at the time of their donation. Maintenance, repairs and minor renewals are expensed as incurred.

All capital assets, other than land, are depreciated using the straight-line method of depreciation using these asset lives:

<u>Description</u>	<u>Range of Useful Lives</u>
Land improvements	5 - 30 years
Buildings and fixed equipment	3 - 50 years
Major movable equipment	3 - 20 years

Goodwill and Intangible Assets

Goodwill totaling \$8,966,112 was recognized when DMC purchased a physician clinic during 2005. A portion of the goodwill was subsequently sold to the Hospital for a \$2,340,000, seven year, 7% note receivable to compensate DMC for the transfer of the clinic radiology department profit. The radiology department equipment was sold to the Hospital and the Hospital operates the radiology department. DMC analyzed the expected future earnings of the clinic and determined the remaining goodwill had been entirely impaired and a goodwill impairment expense of \$6,626,112 was recognized during 2005. The Hospital evaluates goodwill on an annual basis, or sooner if necessary, for potential impairment in accordance with Statement of Financial Accounts Standards (SFAS) No. 142.

Grants and Contributions

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

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

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.

Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures and internally designated by the board of directors. 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—the Hospital's principal activity. Nonoperating revenues include contributions received for purposes other than capital asset acquisition, and other nonoperating activities and are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Compensated Absences

Regular employees of the Hospital earn paid days off (PDO) at rates of twenty-three days to thirty-nine days per year, based on the length of continuous employment and regular hours worked. PDO is adjusted proportionately to hours worked for employees working less than full time. No limit exists on the amount of PDO that may be accumulated. Accrued PDO is paid to employees who resign, giving a two-week notice or in the event of death. All employees may elect to be paid for PDO accumulated in excess of ten days. This option is available twice during the calendar year. The Hospital tracks the PDO accrual on a bi-weekly basis computed on the hourly rate and PDO balance per employee, and the financial statements recognize this liability. Accumulated PDO is reported as a current liability in the amount of \$1,934,860 and \$1,853,534 for 2008 and 2007, respectively.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

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. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Costs of Borrowing

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. There was no interest capitalized during either 2008 or 2007.

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 under Section 115 of the Internal Revenue Code of 1986 as a not-for-profit organization under Section 501(c)(3). Henry County Hospital Foundation, Inc. is a 501(c)(3) not-for-profit organization. HCMH Diversified Management Corporation is a for-profit organization incorporated in 1985 and the sole shareholder is the Hospital.

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.

Reclassifications

Certain amounts from 2007 have been reclassified in order to conform to the 2008 presentation.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

2. ACCOUNTS RECEIVABLE AND PAYABLE

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the Hospital at December 31 are as follows:

	<u>2008</u>	<u>2007</u>
Patient accounts receivable		
Receivable from patients and their insurance carriers	\$ 14,681,976	\$ 15,154,163
Receivable from Medicare	4,479,360	5,493,417
Receivable from Medicaid	<u>2,080,248</u>	<u>1,803,494</u>
Total patient accounts receivable	21,241,584	22,451,074
Less contractual allowances	(7,587,137)	(7,508,658)
Less allowance for uncollectible amounts	<u>(3,643,609)</u>	<u>(4,049,938)</u>
Patient accounts receivable, net	<u>\$ 10,010,838</u>	<u>\$ 10,892,478</u>
Accounts payable and accrued expenses		
Payable to employees (including payroll taxes)	\$ 2,933,164	\$ 2,624,228
Payable to suppliers	4,677,113	4,641,118
Accrued employee health benefit claims	641,353	599,085
Total accounts payable and accrued expenses	<u>\$ 8,251,630</u>	<u>\$ 7,864,431</u>

3. CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy. The charity care provided during 2008 and 2007 was approximately \$7,236,232 and \$5,296,468, respectively.

4. 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 is left to accumulate as an addition to the funds.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Trustee Held Assets

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

Assets that are required for obligations classified as current liabilities are reported in current assets. The composition of assets whose use is limited at December 31 is as follows:

	<u>2008</u>	<u>2007</u>
Board designated		
Funded depreciation		
Investments	\$ 2,079,697	\$ 8,558,746
Certificate of deposit	5,994,048	-0-
Trustee held assets		
Short-term investments	<u>157,261</u>	<u>277,113</u>
Total assets limited to use	<u>\$ 8,231,006</u>	<u>\$ 8,835,859</u>

5. 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 Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

Net realized gains and losses on security transactions are determined on the specific identification cost basis. Funded depreciation investments consist of cash equivalents, mutual funds and U.S. Government securities.

The Hospital's investments generally are reported at fair value, as discussed in Note 1. As of December 31, 2008 and 2007, 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.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

December 31, 2008

	Carrying Amount	Investment Maturities (in years)			
		Less than 1	1-5	6-10	More than 10
US Government Securities	\$ 157,261	\$ 157,261	\$ -0-	\$ -0-	\$ -0-
Mutual funds	14,992,747	14,992,747	-0-	-0-	-0-
Certificate of Deposit	5,994,048	5,994,048	-0-	-0-	-0-
	<u>\$ 21,144,056</u>	<u>\$ 21,144,056</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

December 31, 2007

	Carrying Amount	Investment Maturities (in years)			
		Less than 1	1-5	6-10	More than 10
US Government Securities	\$ 526,488	\$ 277,113	\$ 249,375	\$ -0-	\$ -0-
Mutual funds	26,417,335	26,417,335	-0-	-0-	-0-
	<u>\$ 26,943,823</u>	<u>\$ 26,694,448</u>	<u>\$ 249,375</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

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

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.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Deposits and investments consist of the following as of December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Carrying amount		
Deposits	\$ 10,323,442	\$ 5,704,460
Investments	21,144,056	26,943,823
	<u>\$ 31,467,498</u>	<u>\$ 32,648,283</u>
Included in the balance sheet captions		
Cash and cash equivalents	\$ 10,013,119	\$ 5,441,917
Restricted cash equivalents	310,323	262,543
Investments	12,913,050	18,107,964
Internally designated	8,073,745	8,558,746
Held by trustee for debt service	157,261	277,113
	<u>\$ 31,467,498</u>	<u>\$ 32,648,283</u>

Investment income for 2008 and 2007 is summarized as follows:

	<u>2008</u>	<u>2007</u>
Unrealized losses	\$ (1,673,310)	\$ (257,501)
Realized gains (losses)	(6,181,810)	708,726
Interest and dividends	586,874	1,545,282
	<u>\$ (7,268,246)</u>	<u>\$ 1,996,507</u>

6. FAIR VALUE MEASUREMENTS

Statement on Financial Accounting Standards No. 157, Fair Value Measurements (as amended), requires certain disclosures regarding the fair value of financial instruments. Financial instruments held by the Hospital impacted by this pronouncement include the Hospital's investments and assets whose use is limited which are measured using quoted prices in active markets and other significant observable inputs.

The Hospital partially adopted the provisions of FAS 157 for fiscal year 2008, but will delay adoption of non-financial assets and non-financial liabilities covered by FASB Staff Position No. FAS 157-2. This Staff Position permits entities to partially defer the effective date of FAS 157 for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis, until fiscal year 2009.

When fully adopted, the Hospital will apply the provisions of FAS 157-2 to certain non-financial assets and liabilities and is currently evaluating the impact of the full adoption of this statement on the activities, changes in net assets and financial position. Using

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

the provisions within SFAS No. 157, the Hospital has characterized its investments in securities, based on the priority of the inputs used to value the investments, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities [Level 1], and the lowest priority to unobservable inputs [Level 3]. If the inputs used to measure the investments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the investment.

Investments recorded in the statement of financial position are categorized based on the inputs to valuation techniques as follows:

Level 1 - These are investments where values are based on unadjusted quoted prices for identical assets in an active market the Hospital has the ability to access. Investments include mutual funds.

Level 2 - These are investments where values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the investments. These investments are comprised of US government securities that trade infrequently and certificates of deposit.

Level 3 - These are investments where values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect assumptions of management about assumptions market participants would use in pricing the investments.

Based upon the levels as defined the Hospital's investments as of December 31, 2008 are classified as follows:

Investment Type	Fair value measurements at reporting date using:			
	December 31, 2008	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
U.S. Government Securities	\$ 157,261	\$ -0-	\$ 157,261	\$ -0-
Certificates of deposit	5,994,048	-0-	5,994,048	-0-
Mutual funds	14,992,747	13,992,747	1,000,000	-0-
	\$ 21,144,056	\$ 13,992,747	\$ 7,151,309	\$ -0-

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

7. CAPITAL ASSETS

A summary of capital asset additions, retirements and balances at and for the years ended December 31 is as follows:

	Balance December 31, 2007	Additions	Retirements	Transfers	Balance December 31, 2008
Land	\$ 2,060,000	\$ 388,234	\$ -0-	\$ -0-	\$ 2,448,234
Land improvements	2,225,429	7,776	-0-	-0-	2,233,205
Buildings and improvements	55,841,696	141,819	-0-	83,560	56,067,075
Fixed equipment	14,825,529	308,606	(38,047)	-0-	15,096,088
Major equipment	25,899,183	1,463,966	(569,001)	85,481	26,879,629
Construction in progress	131,640	450,123	-0-	(169,041)	412,722
Total capital assets	<u>100,983,477</u>	<u>2,760,524</u>	<u>(607,048)</u>	<u>-0-</u>	<u>103,136,953</u>
Less accumulated depreciation:					
Land improvements	(1,782,801)	(64,612)	-0-	-0-	(1,847,413)
Buildings and improvements	(23,254,768)	(2,279,320)	-0-	-0-	(25,534,088)
Fixed equipment	(11,627,830)	(639,900)	37,265	-0-	(12,230,465)
Major equipment	(16,047,413)	(2,485,337)	565,352	-0-	(17,967,398)
Total accumulated depreciation	<u>(52,712,812)</u>	<u>(5,469,169)</u>	<u>602,617</u>	<u>-0-</u>	<u>(57,579,364)</u>
Capital assets, net	<u>\$ 48,270,665</u>	<u>\$ (2,708,645)</u>	<u>\$ (4,431)</u>	<u>\$ -0-</u>	<u>\$ 45,557,589</u>

	Balance December 31, 2006	Additions	Retirements	Transfers	Balance December 31, 2007
Land	\$ 2,060,000	\$ -0-	\$ -0-	\$ -0-	\$ 2,060,000
Land improvements	2,253,964	-0-	(28,535)	-0-	2,225,429
Buildings and improvements	55,954,254	14,627	(179,860)	52,675	55,841,696
Fixed equipment	14,797,558	78,219	(75,730)	25,482	14,825,529
Major equipment	23,903,499	1,231,284	(1,641,329)	2,405,729	25,899,183
Construction in progress	2,173,020	442,506	-0-	(2,483,886)	131,640
Total capital assets	<u>101,142,295</u>	<u>1,766,636</u>	<u>(1,925,454)</u>	<u>-0-</u>	<u>100,983,477</u>
Less accumulated depreciation:					
Land improvements	(1,718,449)	(64,352)	-0-	-0-	(1,782,801)
Buildings and improvements	(21,114,697)	(2,259,931)	119,860	-0-	(23,254,768)
Fixed equipment	(11,043,881)	(652,902)	68,953	-0-	(11,627,830)
Major equipment	(15,054,697)	(2,620,162)	1,627,446	-0-	(16,047,413)
Total accumulated depreciation	<u>(48,931,724)</u>	<u>(5,597,347)</u>	<u>1,816,259</u>	<u>-0-</u>	<u>(52,712,812)</u>
Capital assets, net	<u>\$ 52,210,571</u>	<u>\$ (3,830,711)</u>	<u>\$ (109,195)</u>	<u>\$ -0-</u>	<u>\$ 48,270,665</u>

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

8. LONG-TERM DEBT

The Indiana Health Facility Financing Authority issued its Adjustable Rate Demand Revenue Bonds, Series 2002 for the benefit of the Hospital on June 3, 2002. The 2002 Bonds were issued for the purposes of refunding prior indebtedness of the Hospital and providing funds for the construction of an assisted living facility and making certain renovations and equipment purchases at the Hospital. The 2002 Bonds are payable from funds to be drawn upon an irrevocable direct-pay letter of credit issued for the benefit of the Foundation and the Hospital by Fifth Third Bank. From time to time in 2008, bondholders tendered portions of the 2002 Bonds and the letter of credit was drawn to purchase such tendered bonds. Subsequently all of the 2002 Bonds were successfully remarketed and none of the 2002 Bonds were held by Fifth Third Bank as of December 31, 2008. The Hospital continues to pay annual bond payments ranging from \$620,000 to \$1,540,000 with a variable interest rate. The 2002 bonds have a variable interest rate which is 6.0% and 3.5% at December 31, 2008 and 2007, respectively.

The Foundation financed the purchase of equipment with a 6%, 5 year installment loan. The machine cost \$978,338 and the monthly payments are \$18,912.

Effective March 1, 2005, the Hospital issued \$7,500,000 of Series 1985 A Indiana Health Facility Financing Authority bonds. The proceeds were used for various construction and remodeling projects, including the remodeling of the Progressive Care Unit, Emergency Room and Intensive Care Unit. During May 2008, the Hospital retired these bonds and obtained a loan from Citizens State Bank payable upon demand in the amount of \$5,908,091, 4.5% variable interest, at December 31, 2008, expiring May 30, 2009. The loan is collateralized by a certificate of deposit in the amount of \$5,908,091 held with Citizens State Bank.

The Foundation purchased an MRI machine for \$1,518,000 which was financed with a 5 year, 4.38% loan with monthly payments of \$29,241.

DMC financed various equipment purchases with 4-13% installment loans payable in monthly or annual installments with maturity dates ranging from 2006 to 2012.

The Hospital has capital lease obligations, at varying interest rates of imputed interest of 2.5% to 7.49%, collateralized by leased equipment with cost of \$205,968 and \$140,290 as of December 31, 2008 and 2007, respectively. Accumulated depreciation on capital leases was \$109,609 and \$63,434 December 31, 2008 and 2007, respectively.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

A summary of long-term debt borrowings, payments and balances at and for the years ended December 31 are as follows:

	Balance December 31, 2007	Additional borrowings	Payments	Balance December 31, 2008	Current portion	Long-term portion
Demand Revenue Bonds, Series 2002	\$ 16,885,000	\$ -0-	\$ 790,000	\$ 16,095,000	\$ 825,000	\$ 15,270,000
Demand Revenue Bonds, Series 1985 A	6,089,906	-0-	6,089,906	-0-	-0-	-0-
Note Payable	-0-	5,908,091	-0-	5,908,091	5,908,091	-0-
Installment loan payable	237,466	-0-	218,648	18,818	18,818	-0-
Equipment loan Installment loans payable	934,096	-0-	302,569	631,527	320,748	310,779
Capital leases	18,320	-0-	3,378	14,942	3,526	11,416
	119,047	68,678	96,605	91,120	45,488	45,632
	<u>\$ 24,283,835</u>	<u>\$ 5,976,769</u>	<u>\$ 7,501,106</u>	<u>\$ 22,759,498</u>	<u>\$ 7,121,671</u>	<u>\$ 15,637,827</u>

	Balance December 31, 2006	Additional borrowings	Payments	Balance December 31, 2007	Current portion	Long-term portion
Demand Revenue Bonds, Series 2002	\$ 17,635,000	\$ -0-	\$ 750,000	\$ 16,885,000	\$ 790,000	\$ 16,095,000
Demand Revenue Bonds, Series 1985 A	6,722,446	-0-	632,540	6,089,906	678,266	5,411,640
Installment loan payable	443,422	-0-	205,956	237,466	218,649	18,817
Equipment loan	1,219,516	-0-	285,420	934,096	302,569	631,527
Installment loans payable	21,566	-0-	3,246	18,320	1,133	17,187
Capital leases	82,783	134,880	98,616	119,047	94,897	24,150
	<u>\$ 26,124,733</u>	<u>\$ 134,880</u>	<u>\$ 1,975,778</u>	<u>\$ 24,283,835</u>	<u>\$ 2,085,514</u>	<u>\$ 22,198,321</u>

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Scheduled principal repayments on long-term debt following December 31, 2008 are as follows:

<u>Years Ending December 31,</u>	Long-term debt		Capital leases	
	Principal	Interest	Principal	Interest
2009	\$ 7,076,183	\$ 610,218	\$ 45,488	\$ 4,638
2010	1,184,725	451,185	22,993	2,639
2011	913,736	410,022	22,639	857
2012	958,734	378,285	-0-	-0-
2013	1,000,000	344,982	-0-	-0-
2013-2017	5,790,000	1,165,307	-0-	-0-
2018-2022	5,745,000	181,439	-0-	-0-
	<u>\$ 22,668,378</u>	<u>\$ 3,541,438</u>	<u>\$ 91,120</u>	<u>\$ 8,134</u>

9. LETTERS OF CREDIT

The Hospital and the Foundation have acquired an irrevocable direct pay letter of credit issued on their behalf by Fifth Third Bank to provide credit and liquidity support for the 2002 Bonds. Both the Hospital and the Foundation are obligated to reimburse Fifth Third Bank for draws made on the letter of credit pursuant to a Reimbursement and Pledge Agreement by and between the Hospital and the Foundation and Fifth Third Bank, each dated as of June 1, 2002. In addition, the Foundation is a guarantor of the Hospital's obligations under the Hospital's Reimbursement and Pledge Agreement. The letter of credit expires June 1, 2011. In the event the letter of credit is drawn to purchase tendered 2002 Bonds, the Hospital and the Foundation are obligated to reimburse Fifth Third Bank for such Remarketing Draw on or before the fifth day following such Remarketing Draw.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

10. NET PATIENT SERVICE REVENUE

Patient service revenue for 2008 and 2007 consists of the following:

	<u>2008</u>	<u>2007</u>
Inpatient services	\$ 56,308,411	\$ 49,931,796
Outpatient services	110,906,271	99,766,078
Gross patient service revenue	<u>167,214,682</u>	<u>149,697,874</u>
Contractual allowances	68,764,201	60,858,001
Bad debts	3,331,450	4,289,252
Charity care	7,236,232	5,296,468
Deductions from revenue	<u>79,331,883</u>	<u>70,443,721</u>
Net patient service revenue	<u>\$ 87,882,799</u>	<u>\$ 79,254,153</u>

The Hospital participates in the Indiana Medicaid Disproportionate Share Hospital (DSH) reimbursement program. The Hospital had net revenue of approximately \$5,660,415 and \$1,845,000 for DSH in 2008 and 2007, respectively. This program is a Federal program administered by the state.

11. PENSION PLANS

Plan Description

The Hospital has a defined contribution pension plan as authorized by IC 16-22-3-11. The plan provides retirement, disability and death benefits to plan members and beneficiaries. The plan was established by written agreement between the Hospital Board of Trustees and the Plan Administrator. The Plan Administrator issues a publicly available financial report that includes the financial statements and required supplementary information of the plan.

Funding Policy

The contribution requirements of plan members are established by the written agreement between the Hospital Board of Trustees and the Plan Administrator. Members make no contributions to the Plan; all contributions are made by the Hospital. The Hospital is required to contribute at the Board approved rate. For employees hired before July 1, 2003 the rate is 7% on the first \$9,998 of covered wages and 12.7% on the amount over \$9,998 and for employees hired on or after July 1, 2003, their pension rate is 6% on all earnings. Hospital contributions to the plan for 2008 and 2007 were approximately \$2,656,000 and \$2,515,000, respectively.

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

The Hospital funded \$2,000,000 in premiums towards a Split-Dollar Life Insurance Agreement for a key employee that is recorded in Other Assets. The Hospital is the sole and absolute owner of the related Life Insurance Policy. The Agreement was used to fund a supplemental retirement benefit plan. In the event the employee remains employed by the Hospital at least until reaching sixty five years of age, or as is otherwise provided in the Agreement, beginning with the Retirement Date, the Hospital will pay an annual benefit, as is stipulated in the Agreement until the death of the employee. An annual expense is recorded for the death benefit and the salary continuation components of the agreement.

12. EMPLOYEE HEALTH PLAN

The Hospital participates in a self-funded health plan covering substantially all employees. Covered services include medical benefits. The plan has annual reinsurance coverage at a specific level of \$175,000. The financial statements include an estimated provision for claims that have been incurred but not reported. Total health claims expense was approximately \$4,374,000 and \$5,046,000 for the years ended December 31, 2008 and 2007, respectively.

13. NET ASSETS RESTRICTED BY DONOR

Net assets restricted by donor of \$782,635 and \$896,034 at December 31, 2008 and 2007, respectively, consist of donor-restricted funds held by the Foundation primarily for Hospital construction projects.

14. MALPRACTICE INSURANCE

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

HENRY COUNTY HOSPITAL

NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

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.

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

15. CONCENTRATIONS OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party arrangements as follows:

	<u>2008</u>	<u>2007</u>
Medicare and Medicaid	38%	38%
Commercial and other payors	42%	44%
Self-pay	20%	18%
	<u>100%</u>	<u>100%</u>

SUPPLEMENTARY INFORMATION

HENRY COUNTY HOSPITAL

COMBINING BALANCE SHEETS DECEMBER 31, 2008

ASSETS

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Current assets					
Cash and cash equivalents	\$ 8,123,975	\$ 506,848	\$ 1,382,296	\$ -0-	\$ 10,013,119
Restricted cash equivalents	-0-	310,323	-0-	-0-	310,323
Patient accounts receivable, net	7,177,347	-0-	2,833,491	-0-	10,010,838
Supplies and other current assets	1,012,791	110,688	361,353	(20,984)	1,463,848
Due from related parties	4,367,015	22,485	679,730	(5,069,230)	-0-
Current portion of assets whose use is limited	6,376,338	-0-	-0-	-0-	6,376,338
Total current assets	<u>27,057,466</u>	<u>950,344</u>	<u>5,256,870</u>	<u>(5,090,214)</u>	<u>28,174,466</u>
Investments					
Internally designated	3,334,767	9,578,283	-0-	-0-	12,913,050
Held by trustee	8,073,745	-0-	-0-	-0-	8,073,745
	157,261	-0-	-0-	-0-	157,261
Less current portion	8,231,006	-0-	-0-	-0-	8,231,006
Total assets whose use is limited	6,376,338	-0-	-0-	-0-	6,376,338
	<u>1,854,668</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>1,854,668</u>
Capital assets, net	26,847,607	18,506,609	203,373	-0-	45,557,589
Other assets					
Total assets	<u>6,255,199</u>	<u>204,410</u>	<u>1,287,635</u>	<u>(2,595,877)</u>	<u>5,151,367</u>
	<u>\$ 65,349,707</u>	<u>\$ 29,239,646</u>	<u>\$ 6,747,878</u>	<u>\$ (7,686,091)</u>	<u>\$ 93,651,140</u>

HENRY COUNTY HOSPITAL

COMBINING BALANCE SHEETS
DECEMBER 31, 2008

LIABILITIES AND NET ASSETS

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Current liabilities					
Current portion of long-term debt	\$ 6,376,338	\$ 741,807	\$ 19,862	\$ (16,336)	\$ 7,121,671
Accounts payable and accrued expenses	2,708,662	282,853	1,994,844	(309,246)	4,677,113
Accrued wages and related liabilities	3,574,517	-0-	-0-	-0-	3,574,517
Estimated third-party settlements	382,187	-0-	-0-	-0-	382,187
Due to related parties	331,245	146,813	5,717,987	(6,196,045)	-0-
Total current liabilities	<u>13,372,949</u>	<u>1,171,473</u>	<u>7,732,693</u>	<u>(6,521,627)</u>	<u>15,755,488</u>
Other long-term liabilities					
	1,270,609	-0-	-0-	(1,139,464)	131,145
Long-term debt, net of current portion					
	7,870,519	7,755,891	11,417	-0-	15,637,827
Total liabilities	<u>22,514,077</u>	<u>8,927,364</u>	<u>7,744,110</u>	<u>(7,661,091)</u>	<u>31,524,460</u>
Net assets					
Unrestricted					
Invested in capital assets, net of related debt	22,003,874	9,520,736	(1,168,326)	(41,336)	30,314,948
Restricted	12,600,750	10,008,911	172,094	16,336	22,798,091
Expendable - debt service	157,261	-0-	-0-	-0-	157,261
Expendable - funded depreciation	8,073,745	-0-	-0-	-0-	8,073,745
By donor - expendable - for capital acquisition	-0-	782,635	-0-	-0-	782,635
Total net assets	<u>42,835,630</u>	<u>20,312,282</u>	<u>(996,232)</u>	<u>(25,000)</u>	<u>62,126,680</u>
Total liabilities and net assets	<u>\$ 65,349,707</u>	<u>\$ 29,239,646</u>	<u>\$ 6,747,878</u>	<u>\$ (7,686,091)</u>	<u>\$ 93,651,140</u>

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HENRY COUNTY HOSPITAL

COMBINING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED DECEMBER 31, 2008

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Operating revenue					
Net patient service revenue	\$ 67,321,002	\$ 1,360,690	\$ 21,716,788	\$ (2,515,681)	\$ 87,882,799
Other revenue	3,117,832	4,082,013	-0-	(3,082,105)	4,117,740
Total revenue	<u>70,438,834</u>	<u>5,442,703</u>	<u>21,716,788</u>	<u>(5,597,786)</u>	<u>92,000,539</u>
Operating expenses					
Salaries and benefits	39,301,790	-0-	11,537,784	(946,928)	49,892,646
Medical professional fees	1,474,499	-0-	1,553,978	-0-	3,028,477
Other professional fees	3,810,530	-0-	1,720,210	(94,402)	5,436,338
Medical supplies and drugs	7,736,814	-0-	7,351,092	(1,649,824)	13,438,082
Other supplies	863,072	-0-	300,177	-0-	1,163,249
Depreciation and amortization	4,227,594	1,198,417	125,535	-0-	5,551,546
Utilities	1,465,464	-0-	41,674	-0-	1,507,138
Rent	1,960,355	-0-	439,728	(1,522,933)	877,150
Other	3,532,481	3,291,617	917,036	(1,383,699)	6,357,435
Total expenses	<u>64,372,599</u>	<u>4,490,034</u>	<u>23,987,214</u>	<u>(5,597,786)</u>	<u>87,252,061</u>
Operating income (loss)	6,066,235	952,669	(2,270,426)	-0-	4,748,478
Nonoperating income (expense)					
Investment income	(2,221,785)	(5,007,627)	134,908	(173,742)	(7,268,246)
Interest expense	(891,094)	(406,138)	(49,147)	173,742	(1,172,637)
Other nonoperating	148,087	174,011	79,468	-0-	401,566
Total nonoperating income (expense)	<u>(2,964,792)</u>	<u>(5,239,754)</u>	<u>165,229</u>	<u>-0-</u>	<u>(8,039,317)</u>
Change in net assets	3,101,443	(4,287,085)	(2,105,197)	-0-	(3,290,839)
Net assets beginning of year	39,734,187	24,599,367	1,108,965	(25,000)	65,417,519
Net assets end of year	<u>\$ 42,835,630</u>	<u>\$ 20,312,282</u>	<u>\$ (996,232)</u>	<u>\$ (25,000)</u>	<u>\$ 62,126,680</u>

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HENRY COUNTY HOSPITAL

COMBINING STATEMENTS OF CASH FLOWS YEAR ENDED DECEMBER 31, 2008

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Cash flows from operating activities					
Cash received from patients and third party payors	\$ 68,668,249	\$ 1,360,690	\$ 21,198,882	\$ (2,515,681)	\$ 88,712,140
Cash paid to employees for wages and benefits	(38,950,586)	-	(11,537,784)	946,928	(49,541,442)
Cash paid to vendors for goods and services	(20,762,323)	(3,201,803)	(10,243,349)	4,783,613	(29,423,862)
Other operating receipts, net	146,373	4,303,505	-	(2,914,682)	1,535,196
Net cash flows from operating activities	9,101,713	2,462,392	(582,251)	300,178	11,282,032
Cash flows from noncapital financing activities					
Other nonoperating	148,087	174,011	79,468	-	401,566
Net cash flows from noncapital financing activities	148,087	174,011	79,468	-	401,566
Cash flows from capital and related financing activities					
Acquisition and construction of capital assets	(1,965,658)	(637,780)	(88,408)	-	(2,691,846)
Interest expense on long-term debt	(891,094)	(406,138)	(49,147)	173,742	(1,172,637)
Proceeds received from loan	5,908,091	-	-	-	5,908,091
Principal payments on long-term debt, net	(6,591,334)	(906,394)	(34,444)	31,067	(7,501,105)
Net cash flows from capital and related financing activities	(3,539,995)	(1,950,312)	(171,999)	204,809	(5,457,497)
Cash flows from investing activities					
Investment income	(2,221,785)	(5,007,627)	134,908	(173,742)	(7,268,246)
Other assets	(98,264)	10,539	358,577	(331,245)	(60,393)
Change in assets whose use is limited, net	604,853	-	-	-	604,853
Change in investments, net	205,922	4,225,332	(26,554)	-	4,404,700
Net cash flows from investing activities	(1,509,274)	(771,756)	466,931	(504,987)	(2,319,086)
Net change in cash and cash equivalents	4,200,531	(85,665)	(207,851)	-	3,907,015
Cash and cash equivalents					
Beginning of year	3,968,939	902,836	1,590,147	-	6,461,922
End of year	<u>\$ 8,169,470</u>	<u>\$ 817,171</u>	<u>\$ 1,382,296</u>	<u>\$ -</u>	<u>\$ 10,368,937</u>

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HENRY COUNTY HOSPITAL

COMBINING STATEMENTS OF CASH FLOWS YEAR ENDED DECEMBER 31, 2008

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Reconciliation of operating income to net cash flows from operating activities					
Operating income	\$ 6,066,235	\$ 952,669	\$ (2,270,426)	\$ -0-	\$ 4,748,478
Adjustment to reconcile operating income to net cash flows from operating activities:					
Depreciation and amortization	4,227,594	1,198,417	125,535	-0-	5,551,546
Bad debts	3,331,450	-0-	-0-	-0-	3,331,450
(Gain)/Loss on disposal	300	-0-	-0-	-0-	300
Changes in assets and liabilities:					
Patient accounts receivable	(1,931,904)	-0-	(517,906)	-0-	(2,449,810)
Supplies and other current assets	(135,796)	(23,908)	(144,862)	18,589	(285,977)
Accounts payable and accrued expenses	416,788	113,722	(277,436)	(217,079)	35,995
Accrued salaries and related liabilities	351,204	-0-	-0-	-0-	351,204
Other long-term liabilities	(200,100)	-0-	(80,000)	331,245	51,145
Due from (to) related parties	(2,971,759)	221,492	2,582,844	167,423	-0-
Estimated third-party settlements	(52,299)	-0-	-0-	-0-	(52,299)
Net cash flows from operating activities	<u>\$ 9,101,713</u>	<u>\$ 2,462,392</u>	<u>\$ (582,251)</u>	<u>\$ 300,178</u>	<u>\$ 11,282,032</u>

Reconciliation of cash and cash equivalents to the balance sheets

Cash and cash equivalents	\$ 8,123,975	\$ 817,171	\$ 1,382,296	\$ -0-	\$ 10,323,442
In current assets	45,495	-0-	-0-	-0-	45,495
In investments	<u>\$ 8,169,470</u>	<u>\$ 817,171</u>	<u>\$ 1,382,296</u>	<u>\$ -0-</u>	<u>\$ 10,368,937</u>
Total cash and cash equivalents					

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HENRY COUNTY HOSPITAL

SUPPLEMENTAL SCHEDULE OF HOSPITAL OPERATIONS YEARS ENDED DECEMBER 31, 2008 AND 2007

	Hospital 2008	NCFP 2008	NCP 2008	Total 2008	Total 2007	Change
Operating revenue						
Net patient service revenue	\$ 63,932,165	\$ 2,021,766	\$ 1,367,071	\$ 67,321,002	\$ 59,220,465	\$ 8,100,537
Other revenue	2,210,953	292,266	614,613	3,117,832	2,713,131	404,701
Total revenue	<u>66,143,118</u>	<u>2,314,032</u>	<u>1,981,684</u>	<u>70,438,834</u>	<u>61,933,596</u>	<u>8,505,238</u>
Operating expenses						
Salaries and benefits	35,064,232	2,526,419	1,711,139	39,301,790	38,526,435	775,355
Medical professional fees	1,454,916	19,583	-0-	1,474,499	1,107,890	366,609
Other professional fees	3,687,785	15,522	107,223	3,810,530	3,307,087	503,443
Medical supplies and drugs	7,516,717	105,860	114,237	7,736,814	6,737,903	998,911
Other supplies	841,205	19,449	2,418	863,072	752,823	110,249
Depreciation and amortization	4,137,537	90,057	-0-	4,227,594	4,481,348	(253,754)
Utilities	1,437,708	8,115	19,641	1,465,464	1,400,549	64,915
Rent	1,498,114	389,512	72,729	1,960,355	1,719,099	241,256
Other	3,417,012	45,115	70,354	3,532,481	3,361,488	170,993
Total expenses	<u>59,055,226</u>	<u>3,219,632</u>	<u>2,097,741</u>	<u>64,372,599</u>	<u>61,394,622</u>	<u>2,977,977</u>
Operating income (loss)	7,087,892	(905,600)	(116,057)	6,066,235	538,974	5,527,261
Nonoperating income (expense)						
Investment income	(2,222,581)	-0-	796	(2,221,785)	997,562	(3,219,347)
Interest expense	(891,094)	-0-	-0-	(891,094)	(874,292)	(16,802)
Other nonoperating	148,241	910	(1,064)	148,087	129,141	18,946
Total nonoperating income (expense)	<u>(2,965,434)</u>	<u>910</u>	<u>(268)</u>	<u>(2,964,792)</u>	<u>252,411</u>	<u>(3,217,203)</u>
Change in net assets	<u>\$ 4,122,458</u>	<u>\$ (904,690)</u>	<u>\$ (116,325)</u>	<u>\$ 3,101,443</u>	<u>\$ 791,385</u>	<u>\$ 2,310,058</u>

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HENRY COUNTY HOSPITAL

SUPPLEMENTAL SCHEDULE OF HOSPITAL OPERATIONS YEARS ENDED DECEMBER 31, 2007 AND 2006

	Hospital 2007	NCFP 2007	NCP 2007	Total 2007	Total 2006	Change
Operating revenue						
Net patient service revenue	\$ 56,401,170	\$ 1,621,724	\$ 1,197,571	\$ 59,220,465	\$ 59,986,919	\$ (766,454)
Other revenue	1,974,631	236,255	502,245	2,713,131	2,199,815	513,316
Total revenue	<u>58,375,801</u>	<u>1,857,979</u>	<u>1,699,816</u>	<u>61,933,596</u>	<u>62,186,734</u>	<u>(253,138)</u>
Operating expenses						
Salaries and benefits	34,678,370	2,235,115	1,612,950	38,526,435	41,555,057	(3,028,622)
Medical professional fees	1,091,672	16,218	-	1,107,890	1,395,655	(287,765)
Other professional fees	3,115,236	91,654	100,197	3,307,087	2,607,621	699,466
Medical supplies and drugs	6,551,767	74,100	112,036	6,737,903	6,290,232	447,671
Other supplies	732,188	18,331	2,304	752,823	794,485	(41,662)
Depreciation and amortization	4,397,214	84,134	-	4,481,348	4,396,986	84,362
Utilities	1,376,601	6,904	17,044	1,400,549	1,531,038	(130,489)
Rent	1,271,210	375,673	72,216	1,719,099	1,699,699	19,400
Other	3,232,930	61,329	67,229	3,361,488	3,280,108	81,380
Total expenses	<u>56,447,188</u>	<u>2,963,458</u>	<u>1,983,976</u>	<u>61,394,622</u>	<u>63,550,881</u>	<u>(2,156,259)</u>
Operating income (loss)	1,928,613	(1,105,479)	(284,160)	538,974	(1,364,147)	1,903,121
Nonoperating income (expense)						
Investment income	996,923	-	639	997,562	1,505,496	(507,934)
Interest expense	(874,292)	-	-	(874,292)	(842,504)	(31,788)
Other nonoperating	129,190	562	(611)	129,141	6,368	122,773
Total nonoperating income (expense)	<u>251,821</u>	<u>562</u>	<u>28</u>	<u>252,411</u>	<u>669,360</u>	<u>(416,949)</u>
Change in net assets	<u>\$ 2,180,434</u>	<u>\$ (1,104,917)</u>	<u>\$ (284,132)</u>	<u>\$ 791,385</u>	<u>\$ (694,787)</u>	<u>\$ 1,486,172</u>

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HENRY COUNTY HOSPITAL

COMBINING BALANCE SHEETS DECEMBER 31, 2007

ASSETS

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Current assets					
Cash and cash equivalents	\$ 3,211,477	\$ 640,293	\$ 1,590,147	\$ -0-	\$ 5,441,917
Restricted cash equivalents	-0-	262,543	-0-	-0-	262,543
Patient accounts receivable, net	8,576,893	-0-	2,315,585	-0-	10,892,478
Supplies and other current assets	876,995	86,780	216,491	(2,395)	1,177,871
Due from related parties	1,748,372	255,238	612,325	(2,615,935)	-0-
Current portion of assets whose use is limited	1,177,988	-0-	-0-	-0-	1,177,988
Total current assets	15,591,725	1,244,854	4,734,548	(2,618,330)	18,952,797
Investments					
	4,293,812	13,814,152	-0-	-0-	18,107,964
Assets whose use is limited					
Internally designated	8,558,746	-0-	-0-	-0-	8,558,746
Held by trustee	277,113	-0-	-0-	-0-	277,113
Less current portion	8,835,859	-0-	-0-	-0-	8,835,859
Total assets whose use is limited	1,177,988	-0-	-0-	-0-	1,177,988
	7,657,871	-0-	-0-	-0-	7,657,871
Capital assets, net	29,000,010	19,056,709	213,946	-0-	48,270,665
Other assets					
Total assets	6,156,935	214,949	1,646,212	(2,927,122)	5,090,974
	\$ 62,700,353	\$ 34,330,664	\$ 6,594,706	\$ (5,545,452)	\$ 98,080,271

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HENRY COUNTY HOSPITAL

COMBINING BALANCE SHEETS
DECEMBER 31, 2007

LIABILITIES AND NET ASSETS

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Current liabilities					
Current portion of long-term debt	\$ 1,177,988	\$ 906,394	\$ 34,444	\$ (33,312)	\$ 2,085,514
Accounts payable and accrued expenses	2,291,874	169,131	2,272,280	(92,167)	4,641,118
Accrued wages and related liabilities	3,223,313	-0-	-0-	-0-	3,223,313
Estimated third-party settlements	434,486	-0-	-0-	-0-	434,486
Due to related parties	684,361	158,074	3,067,738	(3,910,173)	-0-
Total current liabilities	<u>7,812,022</u>	<u>1,233,599</u>	<u>5,374,462</u>	<u>(4,035,652)</u>	<u>10,384,431</u>
Other long-term liabilities					
	1,470,709	-0-	80,000	(1,470,709)	80,000
Long-term debt, net of current portion	<u>13,683,435</u>	<u>8,497,698</u>	<u>31,279</u>	<u>(14,091)</u>	<u>22,198,321</u>
Total liabilities	<u>22,966,166</u>	<u>9,731,297</u>	<u>5,485,741</u>	<u>(5,520,452)</u>	<u>32,662,752</u>
Net assets					
Unrestricted	16,759,741	14,050,716	960,742	(72,403)	31,698,796
Invested in capital assets, net of related debt	14,138,587	9,652,617	148,223	47,403	23,986,830
Restricted					
Expendable - debt service	277,113	-0-	-0-	-0-	277,113
Expendable - funded depreciation	8,558,746	-0-	-0-	-0-	8,558,746
By donor - expendable - for capital acquisition	-0-	896,034	-0-	-0-	896,034
Total net assets	<u>39,734,187</u>	<u>24,599,367</u>	<u>1,108,965</u>	<u>(25,000)</u>	<u>65,417,519</u>
Total liabilities and net assets	<u>\$ 62,700,353</u>	<u>\$ 34,330,664</u>	<u>\$ 6,594,706</u>	<u>\$ (5,545,452)</u>	<u>\$ 98,080,271</u>

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HENRY COUNTY HOSPITAL

COMBINING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED DECEMBER 31, 2007

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Operating revenue					
Net patient service revenue	\$ 59,220,465	\$ 1,220,780	\$ 21,026,891	\$ (2,213,983)	\$ 79,254,153
Other revenue	2,713,131	4,037,238	-	(2,687,196)	4,063,173
Total revenue	<u>61,933,596</u>	<u>5,258,018</u>	<u>21,026,891</u>	<u>(4,901,179)</u>	<u>83,317,326</u>
Operating expenses					
Salaries and benefits	38,526,435	-	10,227,647	(1,165,563)	47,588,519
Medical professional fees	1,107,890	-	1,057,561	-	2,165,451
Other professional fees	3,307,087	-	1,768,482	(94,652)	4,980,917
Medical supplies and drugs	6,737,903	-	7,699,079	(1,121,897)	13,315,085
Other supplies	752,823	-	124,155	-	876,978
Depreciation and amortization	4,481,348	1,094,398	131,206	-	5,706,952
Utilities	1,400,549	-	135,321	-	1,535,870
Rent	1,719,099	-	419,347	(1,275,764)	862,682
Other	3,361,488	2,964,623	1,005,261	(1,243,303)	6,088,069
Total expenses	<u>61,394,622</u>	<u>4,059,021</u>	<u>22,568,059</u>	<u>(4,901,179)</u>	<u>83,120,523</u>
Operating income (loss)	538,974	1,198,997	(1,541,168)	-	196,803
Nonoperating income (expense)					
Investment income	997,562	1,021,235	173,727	(196,017)	1,996,507
Interest expense	(874,292)	(472,099)	(51,145)	196,017	(1,201,519)
Other nonoperating	129,141	107,342	151,077	-	387,560
Total nonoperating income (expense)	<u>252,411</u>	<u>656,478</u>	<u>273,659</u>	<u>-</u>	<u>1,182,548</u>
Change in net assets	791,385	1,855,475	(1,267,509)	-	1,379,351
Net assets beginning of year	38,942,802	22,743,892	2,376,474	(25,000)	64,038,168
Net assets end of year	<u>\$ 39,734,187</u>	<u>\$ 24,599,367</u>	<u>\$ 1,108,965</u>	<u>\$ (25,000)</u>	<u>\$ 65,417,519</u>

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HENRY COUNTY HOSPITAL

COMBINING STATEMENTS OF CASH FLOWS YEAR ENDED DECEMBER 31, 2007

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Cash flows from operating activities					
Cash received from patients and third party payors	\$ 58,744,306	\$ 1,220,780	\$ 20,953,375	\$ (2,329,128)	\$ 78,589,333
Cash paid to employees for wages and benefits	(38,291,990)	-	(10,227,647)	1,165,563	(47,354,074)
Cash paid to vendors for goods and services	(16,743,520)	(3,159,370)	(11,244,472)	4,278,661	(26,868,701)
Other operating receipts, net	1,584,067	4,351,953	(26,504)	(2,834,567)	3,074,849
Net cash flows from operating activities	5,292,863	2,413,363	(545,348)	280,529	7,441,407
Cash flows from noncapital financing activities					
Other nonoperating	129,141	107,342	151,077	-	387,560
Net cash flows from noncapital financing activities	129,141	107,342	151,077	-	387,560
Cash flows from capital and related financing activities					
Acquisition and construction of capital assets	(1,060,288)	(551,430)	(21,418)	-	(1,633,136)
Interest expense on long-term debt	(874,292)	(472,099)	(51,145)	196,017	(1,201,519)
Principal payments on long-term debt, net	(980,603)	(857,049)	(32,291)	29,045	(1,840,898)
Net cash flows from capital and related financing activities	(2,915,183)	(1,880,578)	(104,854)	225,062	(4,675,553)
Cash flows from investing activities					
Investment income	997,562	1,021,235	173,727	(196,017)	1,996,507
Other assets	(62,857)	11,035	336,908	(309,574)	(24,488)
Change in assets whose use is limited, net	(656,006)	-	-	-	(656,006)
Change in investments, net	340,178	(1,987,043)	-	-	(1,646,865)
Net cash flows from investing activities	618,877	(954,773)	510,635	(505,591)	(330,852)
Net change in cash and cash equivalents	3,125,698	(314,646)	11,510	-	2,822,562
Cash and cash equivalents					
Beginning of year	843,241	1,217,482	1,578,637	-	3,639,360
End of year	<u>\$ 3,968,939</u>	<u>\$ 902,836</u>	<u>\$ 1,590,147</u>	<u>\$ -</u>	<u>\$ 6,461,922</u>

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HENRY COUNTY HOSPITAL

COMBINING STATEMENTS OF CASH FLOWS YEAR ENDED DECEMBER 31, 2007

	Hospital	Foundation	Diversified Management Corporation	Eliminations	Total
Reconciliation of operating income to net cash flows from operating activities					
Operating income	\$ 538,974	\$ 1,198,997	\$ (1,541,168)	\$ -0-	\$ 196,803
Adjustment to reconcile operating income to net cash flows from operating activities:					
Depreciation and amortization	4,481,348	1,094,398	131,206	-0-	5,706,952
Bad debts	4,289,252	-0-	-0-	-0-	4,289,252
(Gain)/Loss on disposal	66,360	(14,036)	(26,604)	-0-	25,720
Changes in assets and liabilities:					
Patient accounts receivable	(4,686,479)	-0-	(73,516)	(115,145)	(4,875,140)
Supplies and other current assets	1,307,580	(5,535)	(19,184)	2,395	1,285,256
Accounts payable and accrued expenses	645,313	(189,212)	49,874	231,076	737,051
Accrued salaries and related liabilities	234,445	-0-	-0-	-0-	234,445
Other long-term liabilities	(309,574)	-0-	(80,000)	309,574	(80,000)
Due from (to) related parties	(1,195,424)	328,751	1,014,044	(147,371)	-0-
Estimated third-party settlements	(78,932)	-0-	-0-	-0-	(78,932)
Net cash flows from operating activities	<u>\$ 5,292,863</u>	<u>\$ 2,413,363</u>	<u>\$ (545,348)</u>	<u>\$ 280,529</u>	<u>\$ 7,441,407</u>
Reconciliation of cash and cash equivalents to the balance sheets					
Cash and cash equivalents					
In current assets	\$ 3,211,477	\$ 902,836	\$ 1,590,147	\$ -0-	\$ 5,704,460
In investments	757,462	-0-	-0-	-0-	757,462
In assets whose use is limited	-0-	-0-	-0-	-0-	-0-
Total cash and cash equivalents	<u>\$ 3,968,939</u>	<u>\$ 902,836</u>	<u>\$ 1,590,147</u>	<u>\$ -0-</u>	<u>\$ 6,461,922</u>

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