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July 6, 2017

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

We have reviewed the audit report prepared by BKD, LLP, Independent Public Accountants, for the period January 1, 2016 to December 31, 2016. In our opinion, the audit report was prepared in accordance with the guidelines established by the State Board of Accounts. Per the Independent Auditor's Report, the financial statements included in the report present fairly the financial condition of the Daviness Community Hospital, as of December 31, 2016 and the results of its operations for the period then ended, on the basis of accounting described in the report.

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

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

Paul D. Joyce, CPA  
State Examiner

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

Independent Auditor's Report and Financial Statements

December 31, 2016 and 2015

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**December 31, 2016 and 2015**

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## Independent Auditor's Report

Board of Governors  
Daviness Community Hospital  
Washington, Indiana

### Report on the Financial Statements

We have audited the accompanying financial statements of Daviness Community Hospital (Hospital), a component unit of Daviness County, Indiana, as of and for the years ended December 31, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements as listed in the table of contents.

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

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

#### *Auditor's Responsibility*

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

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

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

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Daviess Community Hospital as of December 31, 2016 and 2015, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Other Matters***

#### ***Required Supplementary Information***

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

#### ***Other Information***

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Hospital's basic financial statements. The combining schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining schedule information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated June 19, 2017, on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control over financial reporting and compliance.

*BKD, LLP*

Indianapolis, Indiana  
June 19, 2017

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Management's Discussion and Analysis**  
**December 31, 2016 and 2015**

***Introduction***

This management's discussion and analysis of the financial performance of Daviess Community Hospital, a component unit of Daviess County, Indiana (Hospital), provides an overview of the Hospital's financial activities for the years ended December 31, 2016 and 2015. It should be read in conjunction with the accompanying financial statements of the Hospital.

***Financial Highlights***

- Cash and investments increased in 2016 by \$5,127,079 or 60.4% and increased in 2015 by \$2,177,850 or 34.5%.
- The Hospital's net position decreased in 2016 and 2015 by \$428,146 or 1.8% and \$642,956 or 2.7%, respectively.
- The Hospital reported operating income in 2016 and 2015 of \$390,337 and \$384,509, respectively. The operating results in 2016 improved by \$5,828 or 1.5% over the operating income reported in 2015.
- Net nonoperating expenses decreased by \$254,095 or 23.7% in 2016 compared to the decrease of \$33,404 or 3.0% in 2015.

***Using This Annual Report***

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

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

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

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

### **Statements of Cash Flows**

The statements of cash flows reports cash receipts, cash payments and net changes in cash resulting from our defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for and what was the change in cash and cash equivalents during the reporting period.

### **Hospital's Net Position**

The Hospital's net position is the difference between its assets, deferred outflows of resources and liabilities reported in the balance sheets. The Hospital's net position decreased by \$428,146 or 1.8% in 2016 over 2015 compared to the \$642,956 or 2.7% decrease in 2015 over 2014, as shown in Table 1.

	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Assets and Deferred Outflows of Resources</b>			
Patient accounts receivable, net	\$ 17,797,363	\$ 11,846,541	\$ 6,882,550
Other current assets	21,928,960	14,207,247	6,060,183
Capital assets, net	28,364,596	28,573,304	28,294,541
Other noncurrent assets and deferred outflows of resources	6,558,362	6,730,938	8,550,682
	<u>74,649,281</u>	<u>61,358,030</u>	<u>49,787,956</u>
Total assets and deferred outflows of resources	<u>\$ 74,649,281</u>	<u>\$ 61,358,030</u>	<u>\$ 49,787,956</u>
<b>Liabilities</b>			
Long-term debt (including current portion)	\$ 17,936,647	\$ 19,211,224	\$ 19,048,257
Other current and noncurrent liabilities	33,556,852	18,562,878	6,512,815
Total liabilities	<u>51,493,499</u>	<u>37,774,102</u>	<u>25,561,072</u>
<b>Net Position</b>			
Net investment in capital assets	10,427,949	9,362,080	9,246,284
Restricted for debt service	3,197,128	3,167,413	3,142,988
Unrestricted	9,530,705	11,054,435	11,837,612
Total net position	<u>23,155,782</u>	<u>23,583,928</u>	<u>24,226,884</u>
Total liabilities and net position	<u>\$ 74,649,281</u>	<u>\$ 61,358,030</u>	<u>\$ 49,787,956</u>

The most significant change in assets during 2016 were current assets. Current assets increased by approximately \$13.7 million (52.5%) in 2016 primarily as a result of the lease agreements related to the operations of eight additional long-term care facilities. The most significant changes in assets during 2015 were current assets, which increased by approximately \$13.1 million (101.5%) primarily as a result of the lease agreements related to the operations of six long-term care facilities.

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

In 2016, the Hospital's net position decreased by \$428,146 or 1.8% as shown in Table 2. This decrease is made up of several components and represents an improvement of 37.8% compared with the decrease in net position for 2015 of \$642,956 (2.7)%. Of note, during 2016, the Hospital recognized revenue approximating \$12.4 million related to its participation in the Indiana Medicaid Upper Payment Limit (UPL) program with its expanded nursing home operations. These amounts are recorded in other operating revenues. Also, during 2015 and 2014, the Hospital received approximately \$476,000 and \$1.1 million of revenue, respectively, from electronic health records incentive funding, which is included in other operating revenues.

	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Operating Revenues</b>			
Net patient service revenue	\$ 143,445,639	\$ 95,923,449	\$ 53,837,586
Other operating revenues	15,434,547	6,765,112	2,007,031
Total operating revenues	<u>158,880,186</u>	<u>102,688,561</u>	<u>55,844,617</u>
<b>Operating Expenses</b>			
Salaries, wages, contract labor and employee benefits	78,565,667	52,056,098	28,895,523
Purchased services and professional fees	19,726,627	14,509,023	8,368,612
Depreciation and amortization	3,168,910	3,014,084	3,088,725
Provider hospital assessment fee	2,277,328	2,010,528	3,598,202
Other operating expenses	54,751,317	30,714,319	12,816,515
Total operating expenses	<u>158,489,849</u>	<u>102,304,052</u>	<u>56,767,577</u>
<b>Operating Income (Loss)</b>	<u>390,337</u>	<u>384,509</u>	<u>(922,960)</u>
<b>Nonoperating Revenues (Expenses)</b>			
Investment income	71,696	51,331	39,078
Interest expense	(1,140,572)	(1,131,657)	(1,165,777)
Noncapital grants and contributions	65,815	-	-
Other nonoperating revenues and expenses, net	184,578	7,748	20,717
Total nonoperating expenses	<u>(818,483)</u>	<u>(1,072,578)</u>	<u>(1,105,982)</u>
<b>Capital Grants and Contributions</b>	<u>-</u>	<u>45,113</u>	<u>47,620</u>
<b>Decrease in Net Position</b>	<u>\$ (428,146)</u>	<u>\$ (642,956)</u>	<u>\$ (1,981,322)</u>

## Operating Losses

The first component of the overall change in the Hospital's net position is its operating income or loss—generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. In each of the past three years, the Hospital has reported improved operating results, with an operating loss in 2014 and operating income in 2015 and 2016.

Operating income for 2016 improved by \$5,828 or 1.5% as compared to 2015. The primary changes that caused the operating loss are:

- An increase in net patient service revenue of approximately \$47.5 million or 49.5%.
- An increase in other operating revenue of approximately \$8.7 million or 128.1%.
- An increase in total operating expenses of approximately \$56.2 million or 54.9%.

Net patient service revenue increased during 2016 as a result of the leases related to additional long-term care facilities during the year.

Increases in other operating revenues are attributed to UPL revenue approximating \$12.4 million recognized with the increase in nursing home operations.

Total operating expenses increased in 2016 as a result of the leases related to additional long-term care facilities during the year. Salaries, wages, contract labor and employee benefits increased approximately \$26.5 million or 51.0% while purchased services and professional fees increased approximately \$5.2 million or 36.0%.

Operating income for 2016 of \$390,337 approximated operating income of \$384,509 recognized in 2015.

### ***Nonoperating Revenues and Expenses***

Nonoperating revenues and expenses consist primarily of investment income and interest expense. The Hospital recognized a slight increase in interest expense in 2016 as compared to 2015, resulting primarily from additional draws on the outstanding line of credit.

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

Changes in the Hospital's cash flows are consistent with changes in operating results and net nonoperating revenues and expenses for 2016 and 2015, discussed earlier.

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

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

At the end of 2016 and 2015, the Hospital had \$28,364,596 and \$28,573,304 invested in capital assets, net of accumulated depreciation, respectively, as detailed in Note 6 to the financial statements. The Hospital purchased new capital assets costing approximately \$3.0 million in 2016 and \$3.3 million in 2015. Included in these additions are assets acquired through capital lease obligations totaling approximately \$62,000 and \$1,272,000 in 2016 and 2015, respectively.

#### ***Debt***

At December 31, 2016, the Hospital had \$16,695,000 in revenue bonds outstanding compared to \$17,605,000 at December 31, 2015. The Hospital issued no new debt other than the capital leases described above in 2016. The Hospital's formal revenue bonds are subject to limitations imposed by state law. See Note 10 to the basic financial statements for more information regarding long-term debt.

#### ***Line of Credit***

The Hospital had a \$6,000,000 revolving bank line of credit, which expired in February 2017. This agreement was extended to February 2018 and the total principal available increased to \$20 million (see Note 11). At December 31, 2016, there was \$5,928,502 borrowed against this line. The line is collateralized by certain deposit accounts held with the bank. Interest varies with the bank's prime rate less 1.5%, which was 2.0% on December 31, 2016, and is payable monthly.

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

This financial report is designed to provide our patients, suppliers, taxpayers and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Hospital Business Administration by telephoning 812.254.2760.

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

**Balance Sheets**  
**December 31, 2016 and 2015**

**Assets and Deferred Outflows of Resources**

	<b>2016</b>	<b>2015</b>
<b>Current Assets</b>		
Cash	\$ 9,959,228	\$ 4,848,201
Patient accounts receivable, net of allowance of \$2,594,019 and \$2,180,383 for 2016 and 2015, respectively	17,797,363	11,846,541
Supplies	1,315,680	1,189,481
Prepaid expenses and other	10,111,328	7,829,899
Estimated amounts due from third-party payers	542,724	339,666
Total current assets	39,726,323	26,053,788
<b>Noncurrent Cash and Investments</b>		
Internally designated	452,257	465,920
Held by trustee for debt service	3,197,128	3,167,413
	3,649,385	3,633,333
<b>Capital Assets, net</b>	28,364,596	28,573,304
<b>Other Assets</b>	312,690	286,453
<b>Deferred Outflows of Resources - debt defeasance costs</b>	2,596,287	2,811,152
Total assets and deferred outflows of resources	\$ 74,649,281	\$ 61,358,030

**Liabilities and Net Position**

<b>Current Liabilities</b>		
Current maturities of long-term debt	\$ 1,349,497	\$ 1,305,726
Line of credit	5,928,502	1,944,987
Interest payable	417,912	440,662
Accounts payable	9,335,532	4,633,794
Accrued expenses	17,245,889	11,543,435
Estimated amounts due to third-party payers	629,017	-
Total current liabilities	34,906,349	19,868,604
<b>Long-Term Debt</b>	16,587,150	17,905,498
Total liabilities	51,493,499	37,774,102
<b>Net Position</b>		
Net investment in capital assets	10,427,949	9,362,080
Restricted for debt service	3,197,128	3,167,413
Unrestricted	9,530,705	11,054,435
Total net position	23,155,782	23,583,928
Total liabilities and net position	\$ 74,649,281	\$ 61,358,030

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**Years Ended December 31, 2016 and 2015**

	<b>2016</b>	<b>2015</b>
<b>Operating Revenues</b>		
Net patient service revenue, net of provision for uncollectible accounts of \$3,740,365 and \$4,625,215 for 2016 and 2015, respectively	\$ 143,445,639	\$ 95,923,449
Other	15,434,547	6,765,112
Total operating revenues	158,880,186	102,688,561
<b>Operating Expenses</b>		
Salaries, wages and contract labor	64,976,022	41,257,672
Employee benefits	13,589,645	10,798,426
Purchased services and professional fees	19,726,627	14,509,023
Supplies	15,085,515	9,890,300
Insurance	1,268,701	962,311
Utilities	3,256,218	2,542,281
Rent	12,107,493	6,987,662
Repairs and maintenance	4,141,488	3,366,270
Provider hospital assessment fee	2,277,328	2,010,528
Depreciation and amortization	3,168,910	3,014,084
Other	18,891,902	6,965,495
Total operating expenses	158,489,849	102,304,052
<b>Operating Income</b>	390,337	384,509
<b>Nonoperating Revenues (Expenses)</b>		
Investment income	71,696	51,331
Interest expense	(1,140,572)	(1,131,657)
Noncapital grants and contributions	65,815	-
Other	184,578	7,748
Total nonoperating expenses	(818,483)	(1,072,578)
<b>Deficiency of Revenues Over Expenses Before Capital Grants and Contributions</b>	(428,146)	(688,069)
<b>Capital Grants and Contributions</b>	-	45,113
<b>Decrease in Net Position</b>	(428,146)	(642,956)
<b>Net Position, Beginning of Year</b>	23,583,928	24,226,884
<b>Net Position, End of Year</b>	\$ 23,155,782	\$ 23,583,928

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Statements of Cash Flows**  
**Years Ended December 31, 2016 and 2015**

	<b>2016</b>	<b>2015</b>
<b>Operating Activities</b>		
Receipts from and on behalf of patients	\$ 145,970,253	\$ 93,977,309
Payments to suppliers and contractors	(43,585,862)	(31,378,616)
Payments to employees	(78,251,169)	(52,146,573)
Other payments, net	(18,132,359)	(6,263,214)
Net cash provided by operating activities	6,000,863	4,188,906
<b>Noncapital Financing Activity - Noncapital grants and contributions</b>	65,815	-
<b>Capital and Related Financing Activities</b>		
Capital grants and gifts	-	45,113
Principal paid on capital leases	(422,235)	(234,032)
Principal paid on long-term debt	(910,000)	(870,000)
Borrowings on line of credit	3,983,515	1,944,987
Interest paid on long-term debt and capital leases	(953,128)	(938,542)
Purchase of capital assets	(2,910,815)	(2,027,358)
Other capital and related financing activities	16,790	9,697
Net cash used in capital and related financing activities	(1,195,873)	(2,070,135)
<b>Investing Activities</b>		
Interest and dividends on investments	71,696	51,331
Proceeds from sale of investments	84,393	1,533,067
Other investing activities	184,578	7,748
Net cash provided by investing activities	340,667	1,592,146
<b>Increase in Cash</b>	5,211,472	3,710,917
<b>Cash, Beginning of Year</b>	4,848,201	1,137,284
<b>Cash, End of Year</b>	\$ 10,059,673	\$ 4,848,201
<b>Reconciliation of Cash to the Balance Sheets</b>		
Cash	\$ 9,959,228	\$ 4,848,201
Noncurrent cash and investments - internally designated	100,445	-
	\$ 10,059,673	\$ 4,848,201

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Statements of Cash Flows (Continued)**  
**Years Ended December 31, 2016 and 2015**

	<b>2016</b>	<b>2015</b>
<b>Reconciliation of Net Operating Income to</b>		
<b>Net Cash Provided by Operating Activities</b>		
Operating income	\$ 390,337	\$ 384,509
Depreciation and amortization	3,168,910	3,014,084
Provision for uncollectible accounts	3,740,365	4,625,215
Changes in operating assets and liabilities:		
Patient accounts receivable	(9,691,187)	(9,589,206)
Estimated amounts due to/from third-party payers	425,959	214,456
Accounts payable and accrued expenses	10,404,192	10,126,826
Other assets and liabilities	(2,437,713)	(4,586,978)
	\$ 6,000,863	\$ 4,188,906
<b>Supplemental Cash Flows Information</b>		
Capital lease obligations incurred for capital assets	\$ 62,329	\$ 1,271,671

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Notes to Financial Statements**  
**December 31, 2016 and 2015**

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

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

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

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

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

During 2014, the Hospital invested in a 51% ownership in Daviess Community Hospital Pain Management, LLC (Pain Management), which is organized to offer pain management services in the Hospital's primary service area. The Hospital's ownership interest is accounted for under the equity method. Separate audited financial statements are not issued for Pain Management.

***Basis of Accounting and Presentation***

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally state grants and county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses.

# **Daviess Community Hospital**

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

### **Notes to Financial Statements** **December 31, 2016 and 2015**

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

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

#### ***Risk Management***

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

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

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

Investments in nonnegotiable certificates of deposit are carried at amortized cost. The investment in equity investee is reported on the equity method of accounting. All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income.

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

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

#### ***Supplies***

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

# **Daviess Community Hospital**

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

### **Notes to Financial Statements** **December 31, 2016 and 2015**

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

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

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

#### ***Deferred Outflows of Resources***

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

#### ***Compensated Absences***

Hospital policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as vacation benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Expense and the related liability for sick leave benefits are recognized when earned to the extent the employee is expected to realize the benefit in cash determined using the termination payment method. Sick leave benefits expected to be realized as paid time off are recognized as expense when the time off occurs and no liability is accrued for such benefits employees have earned but not yet realized. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at that date. The estimated compensated absences liability is expected to be paid within one year of the balance sheet date, and is therefore included in current liabilities.

# **Daviess Community Hospital**

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

### **Notes to Financial Statements**

#### **December 31, 2016 and 2015**

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

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

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

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

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

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue. Charges excluded from revenue under the Hospital's charity care policy were \$676,765 for 2016 and \$1,131,233 for 2015.

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

As an essential government function of the County, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. In addition, the Hospital is exempt from taxes under Section 501(c)(3) of the Internal Revenue Code. However, the Hospital is subject to federal income tax on any unrelated business taxable income.

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

# **Daviess Community Hospital**

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

### **Notes to Financial Statements** **December 31, 2016 and 2015**

#### ***Foundation***

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

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

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

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

The Hospital began recognizing incentive payment revenues earned for qualified EHR technology expenditures during 2012, which was the period when it first finished attestation for year one. In 2015, the Hospital recorded revenue of approximately \$476,000 for the Medicare and Medicaid incentive programs, which is included in other operating revenues in the statements of revenues, expenses and changes in net position. No amounts were recorded in 2016.

#### ***Reclassifications***

Certain reclassifications have been made to the 2015 financial statements to conform to the 2016 financial statement presentation. The reclassifications had no effect on the changes in net position.

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Notes to Financial Statements**  
**December 31, 2016 and 2015**

**Note 2: Net Patient Service Revenue**

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

*Medicare.* Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient skilled nursing services are paid at prospectively determined per diem rates that are based on the patients' acuity. Certain inpatient nonacute services are paid based on a cost reimbursement methodology. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary.

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

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

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

Approximately 59% and 53% of net patient service revenue are from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2016 and 2015, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital qualifies as a Medicaid Disproportionate Share Hospital (DSH) provider under Indiana law and, as such, is eligible to receive supplemental Medicaid payments. The amounts of these supplemental payments are dependent on regulatory approval by agencies of the federal and state governments and is determined by level, extent and cost of uncompensated care and various other factors. Supplemental payments have been made by the State of Indiana, and the Hospital records such amounts as revenue when it has been reasonably determined that the funds will be received. The Hospital recognized approximately \$624,000 and \$770,000 within patient service revenue related to this supplemental payment program for each of the years ended December 31, 2016 and 2015, respectively. At December 31, 2016 and 2015, \$936,000 is accrued as a receivable in other current assets. This represents management's best estimate of DSH funds due to the Hospital, which are typically paid in arrears.

# **Daviess Community Hospital**

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

### **Notes to Financial Statements** **December 31, 2016 and 2015**

The Hospital participates in a state-specific provider assessment program to increase Medicaid payments to hospitals. The Hospital paid approximately \$2.3 million and \$2.0 million for 2016 and 2015, respectively, into this Medicaid program, which is recorded as an operating expense in the statements of revenues, expenses and changes in net position. In January 2017, the Hospital received notice that its Medicaid Inpatient Utilization Rate (MIUR) continued to exceed state wide thresholds, as defined by state regulation. A benefit of having a MIUR exceeding the threshold includes a 25% reduction in the provider assessment fee. The provider assessment fee program is subject to further retroactive rate setting by the state of Indiana and its Medicaid program and the amounts expensed represent the current fees that have been assessed to the Hospital, including the 25% benefit. The program is scheduled to sunset on June 30, 2017. There is no assurance this program will continue to be implemented in the future.

The long-term care operations of the Hospital qualify for supplemental Medicaid payments through the Upper Payment Limit (UPL) program. The UPL is established to pay qualifying providers the difference between what Medicare would have paid and what Medicaid actually paid. The UPL is distributed through an intergovernmental transfer (IGT) arrangement. The Hospital is responsible for funding the IGT long-term care operations. Revenue associated with the UPL program is recorded net of IGT payments made to the program and are included in other operating revenue. The Hospital recognized approximately \$12,398,000 and \$4,048,000 related to this supplemental payment program for the years ended December 31, 2016 and 2015, respectively. At December 31, 2016 and 2015, respectively, approximately \$5,635,000 and \$1,287,000 is accrued and included in other current assets.

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

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

#### ***Deposits***

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

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

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Notes to Financial Statements**  
**December 31, 2016 and 2015**

**Investments**

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

At December 31, 2016 and 2015, the Hospital had the following investments and maturities:

Type	December 31, 2016				
	Fair Value	Maturities in Years			More Than 10
		Less Than 1	1-5	6-10	
Money market mutual funds	\$ 3,297,196	\$ 3,297,196	\$ -	\$ -	\$ -

  

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

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

**Credit Risk** - Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The Hospital does not have a formal investment policy for credit risk. At December 31, 2016 and 2015, the Hospital's investments were not rated.

**Custodial Credit Risk** - For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Hospital will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Hospital's investment policy does not address how securities underlying repurchase agreements are to be held.

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

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

**Notes to Financial Statements**  
**December 31, 2016 and 2015**

**Summary of Carrying Values**

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

	<b>2016</b>	<b>2015</b>
Carrying value:		
Deposits	\$ 10,311,417	\$ 5,213,079
Investments	3,297,196	3,268,455
	<b>\$ 13,608,613</b>	<b>\$ 8,481,534</b>
 Included in the following balance sheets captions:		
Cash	\$ 9,959,228	\$ 4,848,201
Noncurrent cash and investments	3,649,385	3,633,333
	<b>\$ 13,608,613</b>	<b>\$ 8,481,534</b>

Nonnegotiable certificates of deposit totaling \$251,744 are included in deposit balances at December 31, 2016. There were no material certificate of deposit balances at December 31, 2015.

**Investment Income**

Investment income for the years ended December 31 consisted of:

	<b>2016</b>	<b>2015</b>
Interest and dividend income	\$ 71,696	\$ 51,331

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

**Notes to Financial Statements**  
**December 31, 2016 and 2015**

**Note 4: Patient Accounts Receivable**

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

	<u>2016</u>	<u>2015</u>
Medicare	\$ 6,406,154	\$ 4,568,296
Medicaid	6,160,799	3,195,442
Other third-party payers	4,240,784	3,172,801
Patients	<u>3,583,645</u>	<u>3,090,385</u>
	20,391,382	14,026,924
Less allowance for uncollectible accounts	<u>2,594,019</u>	<u>2,180,383</u>
	<u>\$ 17,797,363</u>	<u>\$ 11,846,541</u>

**Note 5: Investment in Equity Investee**

The investment in equity investee relate to a 51% ownership of Daviess Community Hospital Pain Management, LLC (Pain Management). The Hospital's investment at December 31, 2016 and 2015 was \$79,626 and \$21,956, respectively, and is recorded in other noncurrent assets. The Hospital provides support to the joint venture through labor and supply costs which are billed to Pain Management on a monthly basis. The Hospital also provides billing and collections services for Pain Management and remits patient collections to the joint venture to satisfy operating expenses. Financial positions and results of operations of the investee are summarized below:

	<u>2016</u>	<u>2015</u>
Current and total assets	\$ 272,630	\$ 156,224
Current and total liabilities	<u>116,501</u>	<u>113,173</u>
Members' equity	<u>\$ 156,129</u>	<u>\$ 43,051</u>
Revenues	\$ 609,177	\$ 316,822
Excess (deficiency) of revenues over expenses	\$ 198,714	\$ (56,950)

# Daviness Community Hospital

## A Component Unit of Daviness County, Indiana

### Notes to Financial Statements December 31, 2016 and 2015

#### Note 6: Capital Assets

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

	2016				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 1,280,955	\$ -	\$ -	\$ -	\$ 1,280,955
Land improvements	687,865	-	-	-	687,865
Buildings and leasehold improvements	39,385,620	1,260,275	-	614,086	41,259,981
Equipment	32,688,757	266,203	(171,523)	734,049	33,517,486
Construction in progress	780,626	1,446,666	-	(1,348,135)	879,157
	74,823,823	2,973,144	(171,523)	-	77,625,444
Less accumulated depreciation:					
Land improvements	668,921	7,650	-	-	676,571
Buildings and leasehold improvements	18,711,182	1,232,130	-	-	19,943,312
Equipment	26,870,416	1,925,282	(154,733)	-	28,640,965
	46,250,519	3,165,062	(154,733)	-	49,260,848
Capital assets, net	\$ 28,573,304	\$ (191,918)	\$ (16,790)	\$ -	\$ 28,364,596
	2015				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 1,280,955	\$ -	\$ -	\$ -	\$ 1,280,955
Land improvements	687,865	-	-	-	687,865
Buildings and leasehold improvements	38,741,531	578,914	-	65,175	39,385,620
Equipment	31,025,790	1,635,221	(315,654)	343,400	32,688,757
Construction in progress	104,307	1,084,894	-	(408,575)	780,626
	71,840,448	3,299,029	(315,654)	-	74,823,823
Less accumulated depreciation:					
Land improvements	659,074	9,847	-	-	668,921
Buildings and leasehold improvements	17,624,500	1,086,682	-	-	18,711,182
Equipment	25,262,333	1,914,040	(305,957)	-	26,870,416
	43,545,907	3,010,569	(305,957)	-	46,250,519
Capital assets, net	\$ 28,294,541	\$ 288,460	\$ (9,697)	\$ -	\$ 28,573,304

# Daviness Community Hospital

## A Component Unit of Daviness County, Indiana

### Notes to Financial Statements December 31, 2016 and 2015

#### Note 7: Medical Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claims experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

#### Note 8: Employee Health Claims

Substantially all of the Hospital's employees and their dependents are eligible to participate in the Hospital's employee health insurance plan. The Hospital is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$90,000 per enrollee. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Hospital's estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability, which is included in accrued expenses in the balance sheets, during 2016 and 2015, is summarized as follows:

	2016	2015
Balance, beginning of year	\$ 400,000	\$ 521,000
Current year claims incurred and changes in estimate	3,533,057	3,823,959
Claims and expenses paid	(3,458,057)	(3,944,959)
Balance, end of year	\$ 475,000	\$ 400,000

#### Note 9: Operating Leases

The Hospital has operating leases for long-term care nursing facilities (see Note 16) and equipment that expire at various dates through 2026. In addition to base monthly rent, certain agreements require the Hospital to pay its proportionate share of excess operating costs associated with the facilities.

# Daviness Community Hospital

## A Component Unit of Daviness County, Indiana

### Notes to Financial Statements December 31, 2016 and 2015

Future minimum lease payments at December 31, 2016 were:

2017	\$ 13,155,255
2018	6,914,196
2019	1,153,557
2020	1,188,163
2021	1,223,808
Thereafter	<u>6,337,602</u>
Future minimum lease payments	<u><u>\$ 29,972,581</u></u>

Rental expense for all operating leases amounted to \$12,107,493 and \$6,987,662 for the years ended December 31, 2016 and 2015, respectively.

#### Note 10: Long-Term Debt

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

	2016				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt:					
Series 2011 refunding revenue bonds	\$ 17,605,000	\$ -	\$ (910,000)	\$ 16,695,000	\$ 955,000
Unamortized bond premium	61,122	-	(4,671)	56,451	-
Capital lease obligations	<u>1,545,102</u>	<u>62,329</u>	<u>(422,235)</u>	<u>1,185,196</u>	<u>394,497</u>
Total long-term debt	<u><u>\$ 19,211,224</u></u>	<u><u>\$ 62,329</u></u>	<u><u>\$ (1,336,906)</u></u>	<u><u>\$ 17,936,647</u></u>	<u><u>\$ 1,349,497</u></u>
	2015				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt:					
Series 2011 refunding revenue bonds	\$ 18,475,000	\$ -	\$ (870,000)	\$ 17,605,000	\$ 910,000
Unamortized bond premium	65,794	-	(4,672)	61,122	-
Capital lease obligations	<u>507,463</u>	<u>1,271,671</u>	<u>(234,032)</u>	<u>1,545,102</u>	<u>395,726</u>
Total long-term debt	<u><u>\$ 19,048,257</u></u>	<u><u>\$ 1,271,671</u></u>	<u><u>\$ (1,108,704)</u></u>	<u><u>\$ 19,211,224</u></u>	<u><u>\$ 1,305,726</u></u>

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

**Notes to Financial Statements**  
**December 31, 2016 and 2015**

**Series 2011 Revenue Refunding Bonds Payable**

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

The debt service requirements as of December 31, 2016 are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2017	\$ 1,775,306	\$ 955,000	\$ 820,306
2018	1,779,788	1,000,000	779,788
2019	1,768,788	1,040,000	728,788
2020	1,770,988	1,090,000	680,988
2021	1,765,813	1,135,000	630,813
2022-2026	8,794,406	6,615,000	2,179,406
2027-2029	5,251,650	4,860,000	391,650
	<u>\$ 22,906,739</u>	<u>\$ 16,695,000</u>	<u>\$ 6,211,739</u>

**Capital Lease Obligations**

The Hospital is obligated under leases for equipment that are accounted for as capital leases. The following is a schedule by year of future minimum lease payments under the capital lease including interest at rates ranging from 3.42% to 4.25% together with the present value of the future minimum lease payments as of December 31, 2016:

2017	\$ 431,630
2018	351,294
2019	287,702
2020	189,132
2021	1,156
Total minimum lease payments	1,260,914
Less amount representing interest	75,718
Present value of future minimum lease payments	\$ 1,185,196

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

**Notes to Financial Statements**  
**December 31, 2016 and 2015**

Assets under capital leases at December 31, totaled:

	<b>2016</b>	<b>2015</b>
Machinery and equipment	\$ 2,066,788	\$ 2,024,450
Accumulated depreciation	(916,378)	(513,830)
	\$ 1,150,410	\$ 1,510,620

**Note 11: Line of Credit**

In 2015, the Hospital entered into a \$6,000,000 revolving bank line of credit. The original agreement has been subsequently amended to extend the maturity, which expired in February 2017. At December 31, 2016 and 2015, respectively, there was \$5,928,502 and \$1,944,987 borrowed against this line. The line is collateralized by certain deposit accounts held with the bank. Interest varies with the bank's prime rate less 1.5%, which was 2.0% on December 31, 2016, and is payable monthly. Subsequent to December 31, 2016, the agreement was amended to extend the maturity date to February 2018 and increase the principal available to \$20 million.

**Note 12: Pension Plan**

The Hospital contributes to a defined-contribution 403(b) pension plan covering substantially all employees after one year of service. Pension expense is recorded for the amount of the Hospital's required contributions, determined in accordance with the terms of the plan. The plan is administered by a board of governors. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Hospital's board of governors. The Hospital will match 50% of the employee's contributions into the plan up to a maximum of 6% contribution by the employee. Employees are 100% vested in their own contributions and are vested on an increasing scale from 0% to 100% over 5 years in Hospital contributions. Hospital contributions aggregated \$275,633 and \$184,829 during 2016 and 2015, respectively.

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**

**Notes to Financial Statements**  
**December 31, 2016 and 2015**

**Note 13: Disclosures About Fair Value of Assets and Liabilities**

Fair value is the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities

***Recurring Measurements***

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying financial statements measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2016 and 2015:

	<b>Fair Value</b>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
<b>December 31, 2016</b>				
<b>Investment by fair value level</b>				
Money market mutual funds	\$ 3,297,196	\$ 3,297,196	\$ -	\$ -
<b>December 31, 2015</b>				
<b>Investment by fair value level</b>				
Money market mutual funds	\$ 3,268,455	\$ 3,268,455	\$ -	\$ -

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Notes to Financial Statements**  
**December 31, 2016 and 2015**

***Investments***

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. The Hospital does not have any Level 2 or Level 3 assets at December 31, 2016 and 2015.

**Note 14: Contingencies**

***Litigation***

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

# Daviness Community Hospital

## A Component Unit of Daviness County, Indiana

### Notes to Financial Statements December 31, 2016 and 2015

#### Note 15: Condensed Combining Information

The following tables include condensed combining balance sheet information for the Hospital and its blended component unit as of December 31, 2016 and 2015:

	December 31, 2016		
	Hospital	Foundation	Total
<b>Assets</b>			
Current assets	\$ 39,709,207	\$ 17,116	\$ 39,726,323
Capital assets, net	28,364,596	-	28,364,596
Other assets	3,609,886	352,189	3,962,075
Total assets	<u>71,683,689</u>	<u>369,305</u>	<u>72,052,994</u>
<b>Deferred Outflows of Resources</b>	<u>2,596,287</u>	<u>-</u>	<u>2,596,287</u>
Total assets and deferred outflows of resources	<u>\$ 74,279,976</u>	<u>\$ 369,305</u>	<u>\$ 74,649,281</u>
<b>Liabilities</b>			
Current liabilities	\$ 34,906,349	\$ -	\$ 34,906,349
Noncurrent liabilities	16,587,150	-	16,587,150
Total liabilities	<u>51,493,499</u>	<u>-</u>	<u>51,493,499</u>
<b>Net Position</b>			
Net investment in capital assets	10,427,949	-	10,427,949
Restricted	3,197,128	-	3,197,128
Unrestricted	9,161,400	369,305	9,530,705
Total net position	<u>22,786,477</u>	<u>369,305</u>	<u>23,155,782</u>
Total liabilities and net position	<u>\$ 74,279,976</u>	<u>\$ 369,305</u>	<u>\$ 74,649,281</u>

  

	December 31, 2015		
	Hospital	Foundation	Total
<b>Assets</b>			
Current assets	\$ 26,016,648	\$ 37,140	\$ 26,053,788
Capital assets, net	28,573,304	-	28,573,304
Other assets	3,554,908	364,878	3,919,786
Total assets	<u>58,144,860</u>	<u>402,018</u>	<u>58,546,878</u>
<b>Deferred Outflows of Resources</b>	<u>2,811,152</u>	<u>-</u>	<u>2,811,152</u>
Total assets and deferred outflows of resources	<u>\$ 60,956,012</u>	<u>\$ 402,018</u>	<u>\$ 61,358,030</u>
<b>Liabilities</b>			
Current liabilities	\$ 19,868,604	\$ -	\$ 19,868,604
Noncurrent liabilities	17,905,498	-	17,905,498
Total liabilities	<u>37,774,102</u>	<u>-</u>	<u>37,774,102</u>
<b>Net Position</b>			
Net investment in capital assets	9,362,080	-	9,362,080
Restricted	3,167,413	-	3,167,413
Unrestricted	10,652,417	402,018	11,054,435
Total net position	<u>23,181,910</u>	<u>402,018</u>	<u>23,583,928</u>
Total liabilities and net position	<u>\$ 60,956,012</u>	<u>\$ 402,018</u>	<u>\$ 61,358,030</u>

# Daviess Community Hospital

## A Component Unit of Daviess County, Indiana

### Notes to Financial Statements December 31, 2016 and 2015

The following tables include condensed combining statements of revenues, expenses and changes in net position information for the Hospital and its blended component unit for the years ended December 31, 2016 and 2015.

	December 31, 2016		
	Hospital	Foundation	Total
<b>Operating Revenue</b>			
Net patient service revenue	\$ 143,445,639	\$ -	\$ 143,445,639
Other operating revenue	15,434,547	-	15,434,547
Total operating revenue	<u>158,880,186</u>	<u>-</u>	<u>158,880,186</u>
<b>Operating Expenses</b>			
Salaries, wages, contract labor and employee benefits	78,565,667	-	78,565,667
Purchased services and professional fees	19,726,627	-	19,726,627
Depreciation and amortization	3,168,910	-	3,168,910
Other operating expenses	56,928,803	99,842	57,028,645
Total operating expenses	<u>158,390,007</u>	<u>99,842</u>	<u>158,489,849</u>
<b>Operating Income (Loss)</b>	<u>490,179</u>	<u>(99,842)</u>	<u>390,337</u>
<b>Nonoperating Revenue (Expenses)</b>			
Investment return	70,382	1,314	71,696
Interest expense	(1,140,572)	-	(1,140,572)
Noncapital grants and contributions	-	65,815	65,815
Other	184,578	-	184,578
	<u>(885,612)</u>	<u>67,129</u>	<u>(818,483)</u>
<b>Decrease in Net Position</b>	<u>\$ (395,433)</u>	<u>\$ (32,713)</u>	<u>\$ (428,146)</u>
	December 31, 2015		
	Hospital	Foundation	Total
<b>Operating Revenue</b>			
Net patient service revenue	\$ 95,923,449	\$ -	\$ 95,923,449
Other operating revenue	6,765,112	-	6,765,112
Total operating revenue	<u>102,688,561</u>	<u>-</u>	<u>102,688,561</u>
<b>Operating Expenses</b>			
Salaries, wages, contract labor and employee benefits	52,056,098	-	52,056,098
Purchased services and professional fees	14,509,023	-	14,509,023
Depreciation and amortization	3,014,084	-	3,014,084
Other operating expenses	32,612,102	112,745	32,724,847
Total operating expenses	<u>102,191,307</u>	<u>112,745</u>	<u>102,304,052</u>
<b>Operating Income (Loss)</b>	<u>497,254</u>	<u>(112,745)</u>	<u>384,509</u>
<b>Nonoperating Revenue (Expenses)</b>			
Investment return	48,731	2,600	51,331
Interest expense	(1,131,657)	-	(1,131,657)
Other	7,748	-	7,748
	<u>(1,075,178)</u>	<u>2,600</u>	<u>(1,072,578)</u>
<b>Capital Grants and Contributions</b>	<u>-</u>	<u>45,113</u>	<u>45,113</u>
<b>Decrease in Net Position</b>	<u>\$ (577,924)</u>	<u>\$ (65,032)</u>	<u>\$ (642,956)</u>

# **Daviess Community Hospital**

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

### **Notes to Financial Statements** **December 31, 2016 and 2015**

#### **Note 16: Long-Term Care Operating Leases and Management Agreements**

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

The lease agreements call for monthly base rent payments as outlined in the agreements. Certain facilities include annual rent increases of 2% to 5%. Rental expense approximated \$11.6 million and \$5.5 million in 2016 and 2015, respectively. See Note 9 for future minimum lease payments, including those due under these lease agreements.

The management agreements include management fees consisting of base management fees, subordinated management fees and incentive management fees. Base and subordinate management fees are determined on percentages of net patient service revenue of the individual facilities and range from 0.5% to 5.0%. Incentive management fees are to be paid only if sufficient working capital exists. The management agreements also call for quality, royalty and capital improvement fees to be paid to the Managers. Management and other fees approximated \$4.4 million and \$2.7 million in 2016 and 2015, respectively, and included fee reductions as insufficient cash flows existed to fund amounts due. Amounts are included in purchased services and professional fees on the statements of revenues, expenses and changes in net position.

Under the management agreements, the employees necessary to operate the facilities are contracted by the Hospital. The majority of all costs in the ordinary course of business are paid by the Managers who are then reimbursed by the Hospital from operations of the facilities. Similarly, Managers of certain facilities have provided working capital to cover insufficient cash flows from operations. Consequently, the majority of accounts payable and accrued expenses of the long-term care operations approximating \$18.4 million and \$10.7 million at December 31, 2016 and 2015, respectively, reflect amounts due to Managers.

#### **Note 17: Subsequent Events**

Effective January 1, 2017 and April 1, 2017, the Hospital entered into an additional agreement to lease the facilities and equipment for the operation of six nursing homes. The lease and management agreements have similar terms as nursing home arrangements currently in place.

In February 2017, the Hospital entered into a lease amendment for property that was being constructed for use as an off-campus clinic. The lease was amended to establish the effective date and expected payment terms, which call for monthly rent expense approximating \$12,100 from March 1, 2017 through February 2028. The lease also calls for annual capital improvement payments ranging from \$250,000 to \$400,000 beginning in 2017 through 2023.

## **Supplementary Information**

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Combining Balance Sheet Information**  
**December 31, 2016**

**Assets and Deferred Outflows of Resources**

	2016			
	Hospital	LTC	Hospital Foundation	Total
<b>Current Assets</b>				
Cash	\$ 642,920	\$ 9,299,192	\$ 17,116	\$ 9,959,228
Patient accounts receivable, net of allowance of \$2,594,019	6,089,103	11,708,260	-	17,797,363
Supplies	1,315,680	-	-	1,315,680
Prepaid expenses and other	3,017,258	7,094,070	-	10,111,328
Estimated amounts due from third-party payers	542,724	-	-	542,724
Total current assets	<u>11,607,685</u>	<u>28,101,522</u>	<u>17,116</u>	<u>39,726,323</u>
<b>Noncurrent Cash and Investments</b>				
Internally designated	100,068	-	352,189	452,257
Held by trustee for debt service	3,197,128	-	-	3,197,128
	<u>3,297,196</u>	<u>-</u>	<u>352,189</u>	<u>3,649,385</u>
<b>Capital Assets, net</b>				
	<u>26,879,289</u>	<u>1,485,307</u>	<u>-</u>	<u>28,364,596</u>
<b>Other Assets</b>				
	<u>312,690</u>	<u>-</u>	<u>-</u>	<u>312,690</u>
<b>Deferred Outflows of Resources - debt defeasance costs</b>				
	<u>2,596,287</u>	<u>-</u>	<u>-</u>	<u>2,596,287</u>
Total assets and deferred outflows of resources	<u>\$ 44,693,147</u>	<u>\$ 29,586,829</u>	<u>\$ 369,305</u>	<u>\$ 74,649,281</u>

**Liabilities and Net Position**

<b>Current Liabilities</b>				
Current maturities of long-term debt	\$ 1,349,497	\$ -	\$ -	\$ 1,349,497
Line of credit	1,900,000	4,028,502	-	5,928,502
Interest payable	417,912	-	-	417,912
Accounts payable	3,450,452	5,885,080	-	9,335,532
Accrued expenses	4,738,191	12,507,698	-	17,245,889
Estimated amounts due to third-party payers	629,017	-	-	629,017
Total current liabilities	<u>12,485,069</u>	<u>22,421,280</u>	<u>-</u>	<u>34,906,349</u>
<b>Long-Term Debt</b>				
	<u>16,587,150</u>	<u>-</u>	<u>-</u>	<u>16,587,150</u>
Total liabilities	<u>29,072,219</u>	<u>22,421,280</u>	<u>-</u>	<u>51,493,499</u>
<b>Net Position</b>				
Net investment in capital assets	8,942,642	1,485,307	-	10,427,949
Restricted for debt service	3,197,128	-	-	3,197,128
Unrestricted	3,481,158	5,680,242	369,305	9,530,705
Total net position	<u>15,620,928</u>	<u>7,165,549</u>	<u>369,305</u>	<u>23,155,782</u>
Total liabilities and net position	<u>\$ 44,693,147</u>	<u>\$ 29,586,829</u>	<u>\$ 369,305</u>	<u>\$ 74,649,281</u>

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Combining Balance Sheet Information**  
**December 31, 2015**

**Assets and Deferred Outflows of Resources**

	2015			
	Hospital	LTC	Hospital Foundation	Total
<b>Current Assets</b>				
Cash	\$ 266,941	\$ 4,544,120	\$ 37,140	\$ 4,848,201
Patient accounts receivable, net of allowance of \$2,180,383	7,096,446	4,750,095	-	11,846,541
Supplies	1,189,481	-	-	1,189,481
Prepaid expenses and other	3,850,527	3,979,372	-	7,829,899
Estimated amounts due from third-party payers	339,666	-	-	339,666
Total current assets	<u>12,743,061</u>	<u>13,273,587</u>	<u>37,140</u>	<u>26,053,788</u>
<b>Noncurrent Cash and Investments</b>				
Internally designated	101,042	-	364,878	465,920
Held by trustee for debt service	3,167,413	-	-	3,167,413
	<u>3,268,455</u>	<u>-</u>	<u>364,878</u>	<u>3,633,333</u>
<b>Capital Assets, net</b>	<u>28,175,741</u>	<u>397,563</u>	<u>-</u>	<u>28,573,304</u>
<b>Other Assets</b>	<u>286,453</u>	<u>-</u>	<u>-</u>	<u>286,453</u>
<b>Deferred Outflows of Resources - debt defeasance costs</b>	<u>2,811,152</u>	<u>-</u>	<u>-</u>	<u>2,811,152</u>
Total assets and deferred outflows of resources	<u>\$ 47,284,862</u>	<u>\$ 13,671,150</u>	<u>\$ 402,018</u>	<u>\$ 61,358,030</u>
<b>Liabilities and Net Position</b>				
<b>Current Liabilities</b>				
Current maturities of long-term debt	\$ 1,305,726	\$ -	\$ -	\$ 1,305,726
Line of credit	1,944,987	-	-	1,944,987
Interest payable	440,662	-	-	440,662
Accounts payable	2,144,439	2,489,355	-	4,633,794
Accrued expenses	3,310,411	8,233,024	-	11,543,435
Total current liabilities	<u>9,146,225</u>	<u>10,722,379</u>	<u>-</u>	<u>19,868,604</u>
<b>Long-Term Debt</b>	<u>17,905,498</u>	<u>-</u>	<u>-</u>	<u>17,905,498</u>
Total liabilities	<u>27,051,723</u>	<u>10,722,379</u>	<u>-</u>	<u>37,774,102</u>
<b>Net Position</b>				
Net investment in capital assets	8,964,517	397,563	-	9,362,080
Restricted for debt service	3,167,413	-	-	3,167,413
Unrestricted	8,101,209	2,551,208	402,018	11,054,435
Total net position	<u>20,233,139</u>	<u>2,948,771</u>	<u>402,018</u>	<u>23,583,928</u>
Total liabilities and net position	<u>\$ 47,284,862</u>	<u>\$ 13,671,150</u>	<u>\$ 402,018</u>	<u>\$ 61,358,030</u>

**Daviess Community Hospital**  
**A Component Unit of Daviess County, Indiana**  
**Combining Statement of Revenues, Expenses and**  
**Changes in Net Position Information**  
**Year Ended December 31, 2016**

	2016			
	Hospital	LTC	Hospital Foundation	Total
<b>Operating Revenues</b>				
Net patient service revenue, net of provision for uncollectible accounts of \$3,740,365	\$ 53,130,449	\$ 90,315,190	\$ -	\$ 143,445,639
Other	916,405	14,518,142	-	15,434,547
Total operating revenues	<u>54,046,854</u>	<u>104,833,332</u>	<u>-</u>	<u>158,880,186</u>
<b>Operating Expenses</b>				
Salaries, wages and contract labor	24,761,806	40,214,216	-	64,976,022
Employee benefits	6,037,174	7,552,471	-	13,589,645
Purchased services and professional fees	9,862,456	9,864,171	-	19,726,627
Supplies	6,407,639	8,677,876	-	15,085,515
Insurance	389,814	878,887	-	1,268,701
Utilities	932,115	2,324,103	-	3,256,218
Rent	356,810	11,750,683	-	12,107,493
Repairs and maintenance	3,180,667	960,821	-	4,141,488
Provider hospital assessment fee	2,277,328	-	-	2,277,328
Depreciation and amortization	3,030,479	138,431	-	3,168,910
Other	1,834,761	16,957,299	99,842	18,891,902
Total operating expenses	<u>59,071,049</u>	<u>99,318,958</u>	<u>99,842</u>	<u>158,489,849</u>
<b>Operating Income (Loss)</b>	<u>(5,024,195)</u>	<u>5,514,374</u>	<u>(99,842)</u>	<u>390,337</u>
<b>Nonoperating Revenues (Expenses)</b>				
Investment income	70,382	-	1,314	71,696
Interest expense	(1,140,572)	-	-	(1,140,572)
Noncapital grants and contributions	-	-	65,815	65,815
Other	184,578	-	-	184,578
Total nonoperating revenues (expenses)	<u>(885,612)</u>	<u>-</u>	<u>67,129</u>	<u>(818,483)</u>
<b>Excess (Deficiency) of Revenues Over Expenses Before Transfers</b>	<u>(5,909,807)</u>	<u>5,514,374</u>	<u>(32,713)</u>	<u>(428,146)</u>
<b>Transfers</b>	<u>1,297,596</u>	<u>(1,297,596)</u>	<u>-</u>	<u>-</u>
<b>Increase (Decrease) in Net Position</b>	<u>(4,612,211)</u>	<u>4,216,778</u>	<u>(32,713)</u>	<u>(428,146)</u>
<b>Net Position, Beginning of Year</b>	<u>20,233,139</u>	<u>2,948,771</u>	<u>402,018</u>	<u>23,583,928</u>
<b>Net Position, End of Year</b>	<u>\$ 15,620,928</u>	<u>\$ 7,165,549</u>	<u>\$ 369,305</u>	<u>\$ 23,155,782</u>

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

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

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

Board of Governors  
Daviess Community Hospital  
Washington, Indiana

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Daviess Community Hospital (Hospital), a component unit of Daviess County, Indiana, which comprise the balance sheet as of December 31, 2016, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 19, 2017.

### ***Internal Control Over Financial Reporting***

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

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

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

### ***Compliance and Other Matters***

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

We noted certain matters that we reported to the Hospital's management in a separate letter dated June 19, 2017.

### ***Purpose of this Report***

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

**BKD, LLP**

Indianapolis, Indiana  
June 19, 2017