



# **MARGARET MARY COMMUNITY HOSPITAL, INC.**

**FINANCIAL STATEMENTS**

**DECEMBER 31, 2007 AND 2006**

# MARGARET MARY COMMUNITY HOSPITAL, INC.

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## REPORT OF INDEPENDENT AUDITORS

Board of Directors  
Margaret Mary Community Hospital, Inc.  
Batesville, Indiana

We have audited the accompanying balance sheets of Margaret Mary Community Hospital, Inc. (Hospital) as of December 31, 2007 and 2006, and the related statements of operations, changes in net assets and cash flows for the years then ended. These 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 conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of December 31, 2007 and 2006, 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.

*Blue & Co., LLC*

March 6, 2008

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## BALANCE SHEETS DECEMBER 31, 2007 AND 2006

<b>ASSETS</b>		
	2007	2006
<b>Current assets</b>		
Cash and cash equivalents	\$ 2,516,960	\$ 2,105,244
Investments	17,307	16,366
Patient accounts receivable, net of uncollectible allowance of \$1,892,759 in 2007 and \$1,799,668 in 2006	8,341,442	7,717,876
Other receivables	177,343	318,770
Inventories	718,460	566,113
Prepaid expenses	342,232	353,750
Current portion of assets whose use is limited	625,000	605,000
Total current assets	12,738,744	11,683,119
<b>Assets whose use is limited</b>		
Board designated for capital improvements	20,651,017	16,093,677
Board designated for retirement plan	484,831	482,838
	21,135,848	16,576,515
Less current portion	625,000	605,000
Assets whose use is limited - noncurrent	20,510,848	15,971,515
<b>Property and equipment, net</b>	42,821,206	43,521,220
<b>Derivative asset</b>	-0-	207,548
<b>Bond issue costs, net</b>	280,340	293,532
Total assets	\$ 76,351,138	\$ 71,676,934
<b>LIABILITIES AND NET ASSETS</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 1,131,314	\$ 1,243,493
Accrued wages and related liabilities	2,410,323	2,107,953
Estimated third-party settlements	975,998	605,198
Current portion of long-term debt	625,000	605,000
Total current liabilities	5,142,635	4,561,644
<b>Derivative liability</b>	355,397	-0-
<b>Long-term debt, less current portion</b>	19,620,000	20,245,000
Total liabilities	25,118,032	24,806,644
<b>Net assets</b>		
Unrestricted	51,125,637	46,750,439
Temporarily restricted	107,469	119,851
Total net assets	51,233,106	46,870,290
Total liabilities and net assets	\$ 76,351,138	\$ 71,676,934

See accompanying notes to financial statements.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## STATEMENTS OF OPERATIONS YEARS ENDED DECEMBER 31, 2007 AND 2006

	2007	2006
<b>Unrestricted revenue, gains and other support</b>		
Patient service revenue	\$ 54,178,172	\$ 48,890,050
Gains, primarily investment income	1,707,606	1,318,507
Other revenue	485,746	428,527
Net assets released from restrictions	61,762	37,300
Total revenue, gains and other support	56,433,286	50,674,384
<b>Expenses</b>		
Salaries and wages	18,379,352	16,994,565
Employee benefits	7,027,258	6,911,896
Physician fees	2,024,839	1,766,985
Medical and surgical supplies	6,196,666	5,839,123
Other supplies	382,993	356,814
Purchased services	3,945,297	3,513,140
Equipment rentals	85,620	73,395
Food	319,413	358,573
Utilities	1,028,116	1,123,216
Bad debts	3,875,764	3,316,310
Insurance	498,360	496,824
Depreciation and amortization	4,076,669	3,953,828
Interest	857,902	883,905
Other	961,033	984,258
Total expenses	49,659,282	46,572,832
Excess revenues over expenses from continuing operations	6,774,004	4,101,552
<b>Other changes in unrestricted net assets</b>		
Unrealized gain (loss) on investments	(1,034,552)	293,790
Unrealized gain (loss) on derivative	(562,945)	314,477
Total other changes in unrestricted net assets	(1,597,497)	608,267
Change in unrestricted net assets before discontinued operations	5,176,507	4,709,819
<b>Loss from operations of discontinued component</b>	801,309	585,071
Change in unrestricted net assets	\$ 4,375,198	\$ 4,124,748

See accompanying notes to financial statements.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

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

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	<u>2007</u>	<u>2006</u>
<b>Unrestricted net assets</b>		
Change in unrestricted net assets	\$ 4,375,198	\$ 4,124,748
<b>Temporarily restricted net assets</b>		
Contributions	49,380	70,938
Net assets released from restrictions	<u>(61,762)</u>	<u>(37,300)</u>
Change in temporarily restricted net assets	<u>(12,382)</u>	<u>33,638</u>
Change in net assets	4,362,816	4,158,386
<b>Net assets</b>		
Beginning of year	<u>46,870,290</u>	<u>42,711,904</u>
End of year	<u><u>\$ 51,233,106</u></u>	<u><u>\$ 46,870,290</u></u>

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See accompanying notes to financial statements.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

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

	2007	2006
<b>Operating activities</b>		
Change in net assets	\$ 4,362,816	\$ 4,158,386
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation and amortization	4,076,669	3,953,828
Depreciation included in discontinued operations	3,800	3,800
Bad debts	3,875,764	3,316,310
Realized and unrealized (gain) loss on investments	1,244,170	(232,288)
Unrealized (gain) loss on derivative	562,945	(314,477)
(Gain) loss on disposal of property and equipment	74,785	(1,278)
Change in operating assets and liabilities		
Patient accounts receivable	(4,499,330)	(4,380,262)
Other receivables	141,427	(110,004)
Inventories	(152,347)	(7,246)
Prepaid expenses	11,518	(19,955)
Accounts payable	(112,179)	(975,505)
Accrued wages and related liabilities	302,370	381,320
Estimated third-party settlements	370,800	455,198
Net cash flows from operating activities	10,263,208	6,227,827
<b>Investing activities</b>		
Proceeds from sale of assets whose use is limited	10,453,778	1,674,916
Purchase of assets whose use is limited	(16,257,281)	(2,576,846)
Proceeds from sale of property and equipment	2,052	1,278
Additions to property and equipment	(3,444,100)	(2,812,538)
Other changes in investing activities	(941)	(613)
Net cash flows from investing activities	(9,246,492)	(3,713,803)
<b>Financing activities</b>		
Repayment of long-term debt	(605,000)	(585,000)
Net change in cash	411,716	1,929,024
<b>Cash and cash equivalents, beginning of year</b>	2,105,244	176,220
<b>Cash and cash equivalents, end of year</b>	\$ 2,516,960	\$ 2,105,244
<b>Supplemental disclosure of cash flows information</b>		
Cash paid for interest	\$ 857,902	\$ 883,905

See accompanying notes to financial statements.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### 1. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies followed by Margaret Mary Community Hospital, Inc. (Hospital) in the preparation of its financial statements are summarized below:

#### Organization

The Hospital, located in Batesville, Indiana, is a not-for-profit acute care hospital also providing long-term care and home health services. The Hospital provides inpatient, outpatient, and other ancillary services to the residents of Ripley and surrounding counties. Admitting physicians are primarily practitioners in the local area.

#### Use of Estimates

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

#### Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts deemed to be charity care, they are not reported as revenue (see Note 2).

#### Patient Accounts Receivable and Revenues

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

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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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). In 2006, The Hospital was granted Critical Access Status by Medicare and is paid for Medicare services based upon a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at an interim rate, with final settlement determined after submission of annual cost reports.

Prior to 2006, the Hospital was reimbursed for Medicare inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG). The Hospital was reimbursed for Medicare 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. The year end cost reports filed with the Medicare and Medicaid programs through December 31, 2005 have been audited by these programs and any resulting differences are reflected in the financial statements. During 2007 and 2006, the Hospital recognized approximately \$-0- and \$200,000, respectively, of income due to the differences between original estimates and subsequent revisions for the final settlement of cost reports.

Management estimates an allowance for uncollectible accounts receivable based on an evaluation of historical losses, current economic conditions, and other factors unique to the Hospital's customer base.

A summary of patient service revenue for 2007 and 2006 follows:

	<u>2007</u>	<u>2006</u>
Inpatient routine	\$ 5,686,495	\$ 4,997,672
Inpatient ancillary	13,462,241	11,155,891
Outpatient services	<u>68,523,939</u>	<u>60,170,826</u>
	87,672,675	76,324,389
Less provisions for		
Contractual adjustments under third-party reimbursement programs	32,594,943	26,823,171
Charity care	<u>899,560</u>	<u>611,168</u>
Total provisions	<u>33,494,503</u>	<u>27,434,339</u>
Patient service revenue	<u>\$ 54,178,172</u>	<u>\$ 48,890,050</u>

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# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### Investments

Investments consist of fixed income mutual funds recorded at fair market value.

### Inventories

Inventories are valued at the lower of cost or market with cost being determined on an average cost method.

### Property and Equipment and Provision for Depreciation

Property and equipment are recorded at historical cost except for donations, which are recorded at fair market value at the date of the donation.

Property and equipment include expenditures for additions and repairs that substantially increase the useful lives of existing property and equipment. Maintenance, repairs and minor renewals are expensed as incurred.

The property and equipment of the Hospital are being depreciated over their estimated useful lives using the straight-line method. The ranges of useful lives used in computing depreciation are as follows:

<u>Description</u>	<u>Range of Useful Lives</u>
Land improvements	12-24 years
Buildings and improvements	10-40 years
Equipment	3-20 years

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor restrictions about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service. During 2007 and 2006, there were no gifts of long-lived assets with restrictions.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### Assets Whose Use is Limited

Assets whose use is limited by internal board designation includes cash and cash equivalents, accrued interest receivable, and marketable securities. Marketable securities include investments in or backed by the United States Government, corporate debt instruments and common stock. Such securities are stated at fair market value. Donated securities are recorded at fair market value at the date of the donation.

Assets held by trustee include cash and investments from Hospital deposits for debt service payments in compliance with the Indiana Health Facility Financing Authority bond issues described in the debt note.

### Bond Issue Costs

Unamortized bond issue costs as of December 31, 2007 and 2006 were \$280,340 and \$293,532. Bond issue costs are amortized over the life of the bonds. Accumulated amortization as of December 31, 2007 and 2006 was \$39,577 and \$26,385, respectively. Amortization expense for the years ending December 31, 2008 through 2012 is approximately \$13,000 per year.

### Temporarily Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital has been limited by external sources for a specific time period or purpose. When a restriction expires, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statements of operations and changes in net assets as net assets released from restrictions. Restrictions that are met within the year of receipt are reflected with unrestricted net assets. As of December 31, 2007 and 2006, temporarily restricted net assets were \$107,469 and \$119,851, respectively. These assets are restricted for scholarships and other Hospital programs.

### Excess Revenues Over Expenses

The statement of operations includes excess revenues over expenses. Changes in unrestricted net assets that are excluded from excess revenues over expenses include unrealized gain and loss on investments other than trading securities, derivative gain and loss and contributions of long-lived assets.

### Federal and State Income Taxes

The Hospital qualifies as a tax-exempt organization under Section 501(c)(3) of the U.S. Internal Revenue Code and is exempt from Federal and state income taxes.

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# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### Advertising Costs

The Hospital's policy is to expense advertising costs when the advertising first takes place. Advertising expenses were \$177,574 and \$161,972 in 2007 and 2006, respectively.

### Statements of Cash Flows

For the purposes of reporting cash flows, cash and cash equivalents include all cash held in checking and money market accounts available for operating purposes with original maturities of 90 days or less. Cash paid for interest for 2007 and 2006 was \$857,902 and \$883,905, respectively.

### Accounting Pronouncement

In November 2005, the FASB issued FASB Staff Position No. 45-3, "Application of FASB Interpretation No. 45 to Minimum Revenue Guarantees Granted to a Business or Its Owners" ("FIN 45-3"). It served as an amendment to FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others" ("FIN 45") by adding minimum revenue guarantees to the list of examples of contracts to which FIN 45 applies.

Under FIN 45, a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. One example cited in FIN 45-3 involves a guarantee provided by a healthcare entity to a non-employed physician in order to recruit such physician to move to the entity's geographical area and establish a private practice, which is the approach the Hospital uses in recruiting physicians to the community. FIN 45 is effective for new minimum revenue guarantees issued or modified on or after January 1, 2006.

The Hospital adopted this amendment to FIN 45 effective January 1, 2006. For periods ending before January 1, 2006, the Hospital did not report the fair value of its obligations under physician revenue guarantee agreements. However, under FIN 45 as amended, the Hospital is required to report the liability for these physician revenue guarantees on its balance sheets at fair value and amortize the related prepaid physician recruitment expense over the period of the physician's contractual commitment to practice in the local community, which is typically three years. As of December 31, 2007 and 2006, the Hospital had not entered or modified any physician revenue guarantee agreements on or after January 1, 2006; accordingly, the adoption of this amendment had no effect on the accompanying financial statements.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### Reclassification

Certain items in the 2006 financial statements have been reclassified herein to conform to the current year presentation.

## 2. CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy based on established rates. Charity care charges foregone during 2007 and 2006 were \$899,560 and \$611,168, respectively.

## 3. INVESTMENTS

Investments are recorded at fair market value and consist of the following as of December 31, 2007 and 2006:

	<u>2007</u>	<u>2006</u>
Mutual funds - fixed income	<u>\$ 17,307</u>	<u>\$ 16,366</u>

## 4. PROPERTY AND EQUIPMENT

Property and equipment consist of the following as of December 31:

	<u>2007</u>	<u>2006</u>
Land	\$ 2,371,158	\$ 2,371,158
Land improvements	375,610	375,610
Buildings and improvements	47,611,294	47,345,405
Fixed equipment	5,691,265	5,662,686
Movable and minor equipment	<u>22,414,684</u>	<u>20,425,691</u>
	78,464,011	76,180,550
Less accumulated depreciation	<u>36,734,052</u>	<u>34,079,537</u>
	41,729,959	42,101,013
Construction in progress	<u>1,091,247</u>	<u>1,420,207</u>
	<u>\$ 42,821,206</u>	<u>\$ 43,521,220</u>

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# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

### 5. ASSETS WHOSE USE IS LIMITED

Assets whose use is limited includes board designated funds as of December 31:

	2007	2006
Cash and cash equivalents	\$ 1,384,104	\$ 801,742
Accrued interest receivable	49,073	77,768
Marketable securities	19,702,671	15,697,005
	\$ 21,135,848	\$ 16,576,515

The following is a summary of market value and cost for board designated marketable securities as of December 31:

	2007		2006	
	Market Value	Cost	Market Value	Cost
Fixed income obligations	\$ 9,283,460	\$ 9,115,097	\$ 8,346,676	\$ 8,630,661
Mutual funds - equities	9,631,858	10,924,497	6,546,022	6,393,988
Equity securities	787,353	396,069	804,307	396,069
	\$ 19,702,671	\$ 20,435,663	\$ 15,697,005	\$ 15,420,718

The following is a reconciliation of gains and losses and investment income for 2007 and 2006:

	2007	2006
Interest and dividends	\$ 1,917,224	1,380,009
Realized loss on investments	(209,618)	(61,502)
	\$ 1,707,606	\$ 1,318,507
Unrealized gain (loss) on investments	\$ (1,034,552)	\$ 293,790

The following schedules summarize the fair value of securities included in assets whose use is limited that have gross unrealized losses (the amount by which historical cost exceeds the fair value) as of December 31, 2007 and 2006. The schedules further segregate the securities that have been in a gross unrealized position as of December 31, 2007 and 2006, for less than twelve months and those for twelve months or more. The gross unrealized losses of less than twelve months are a reflection of the normal fluctuations of the market and are therefore considered temporary. The gross unrealized losses of twelve months or longer are reflective of current market fluctuations. The majority of the decline is attributable to securities which industry experts expect recovery in the short-term future. These individual investments have projected recoveries in value in 2008.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

The decline in value is determined by management to be temporary, and unrealized losses have not been reclassified to realized losses as of December 31, 2007 and 2006:

Description of securities	December 31, 2007					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mutual funds	<u>\$ 862,626</u>	<u>\$ 274,769</u>	<u>\$ 2,666,891</u>	<u>\$ 915,193</u>	<u>\$ 3,529,517</u>	<u>\$ (1,189,962)</u>

  

Description of securities	December 31, 2006					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mutual funds	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ 1,154,889</u>	<u>\$ 464,718</u>	<u>\$ 1,154,889</u>	<u>\$ (464,718)</u>

## 6. DERIVATIVE AGREEMENT

In 2004, the Hospital entered into a "cash flow hedge interest rate swap" agreement with a financial institution. The Hospital pays a fixed interest rate (3.48% at December 31, 2007 and 2006) and the financial institution pays a variable interest rate (3.51% and 3.80% as of December 31, 2007 and 2006, respectively) over the term of the agreement.

The Hospital's objective is to provide protection against market driven increases in variable interest rates. The fair value of the agreement was determined by the financial institution using the present value of the estimated projected cash flows. The Hospital is in a liability position as of December 31, 2007 due to the present value of its estimated projected cash flows being more than the financial institution's present value of estimated projected cash flows.

The swap agreement matures on December 1, 2029, and contains an outstanding notional amount of \$20,000,000 with a 3.48% fixed rate of interest. The Hospital recorded a derivative liability of \$355,397 and a derivative asset \$207,548 as of December 31, 2007 and 2006, respectively. The total derivative gain/(loss) recognized on the financial statements was an unrealized loss of \$562,945 for 2007 and an unrealized gain of \$314,477 for 2006.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

### 7. LONG-TERM DEBT

The following is the summary of long-term debt as of December 31:

	<u>2007</u>	<u>2006</u>
Indiana Health Facility Financing Authority; dated March 1, 2004, due 2029; Variable Rate Demand Revenue Bonds; Series 2004A-1	\$ 20,245,000	\$ 20,850,000
Less current portion	<u>625,000</u>	<u>605,000</u>
	<u>\$ 19,620,000</u>	<u>\$ 20,245,000</u>

Annual maturities of long-term debt for the years succeeding December 31, 2007 are as follows:

<u>Year Ending December 31,</u>	
2008	\$ 625,000
2009	650,000
2010	670,000
2011	695,000
2012	715,000
Thereafter	<u>16,890,000</u>
	<u>\$ 20,245,000</u>

In 2004, the Hospital borrowed from the Indiana Health Facility Financing Authority (the Authority) \$22,000,000 for the construction of an addition to the Hospital facilities. The Authority, created under Indiana Code 5-1-16, provides funds to eligible health facilities for financing capital expenditures. Interest expense is determined monthly based on the actual rate of interest paid by the Authority to its bondholders. The Authority's rate of interest is determined by the Remarketing Agent with due regard to prevailing financial market conditions. The variable rate on the Series 2004 bonds was 3.51% and 3.80% as of December 31, 2007 and 2006, respectively. The Series 2004 bonds are secured by a letter of credit in the amount of \$20,478,000 as of December 31, 2007 that expires March 15, 2012. The letter of credit is secured by the assignment of the Authority note, which is secured by a pledge of gross revenues. The loan agreement and letter of credit require the Hospital to comply with certain restrictive covenants. Management believes the Hospital is in compliance with the covenants as of December 31, 2007.

The Hospital has entered into an interest rate swap agreement related to the Series 2004 bonds (Note 6).

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### 8. RETIREMENT PLANS

The Hospital has a defined contribution pension plan which covers all eligible employees. Allocations of plan contributions are made based upon the earnings of qualified employees. Contribution percentages are at the discretion of the Hospital.

In 2003, the Hospital adopted a 457(b) deferred compensation plan that provides for non-elective employer deferrals covering a select group of management or highly compensated individuals.

Pension expense was \$497,091 and \$498,155 for 2007 and 2006, respectively.

### 9. CONCENTRATIONS OF CREDIT RISK

The Hospital is located in Batesville, Indiana. The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. Percentages of receivables from self pay patients and third-party payors were as follows:

	<u>2007</u>	<u>2006</u>
Medicare	24%	21%
Medicaid	7%	10%
Blue Cross	16%	11%
Other third-party payors	22%	18%
Self pay	<u>31%</u>	<u>40%</u>
	<u>100%</u>	<u>100%</u>

The Hospital maintains its cash in accounts, which at times may exceed federally insured limits. The Hospital has not experienced any losses in such accounts. The Hospital believes that it is not exposed to any significant credit risk on cash and cash equivalents.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### 10. COMMITMENTS AND CONTINGENCIES

#### Self-Funded Health Plan

The Hospital is committed to pay for employees' health care costs. A third-party administrator has been retained to process and present all benefit claims to the Hospital for payment. Under a stop loss agreement, the Hospital is responsible for the funding of all claims and related administrative costs up to \$150,000 per individual per policy year. There is no aggregate limit for the Plan under the stop loss agreement. Group health insurance expense for the years ended December 31, 2007 and 2006 totaled \$4,755,561 and \$4,958,081, respectively.

#### Estimated Malpractice Costs

Previously, the Hospital was insured for malpractice through PHICO Insurance Company. PHICO was placed into liquidation by the Pennsylvania Department of Insurance. Due to the financial circumstances of PHICO, the Hospital obtained malpractice coverage through another carrier. The Hospital may be liable for the first \$250,000 of any pending PHICO claims. Amounts in excess of \$250,000 are covered by the Indiana Patient's Compensation Fund.

#### Litigation

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

#### Construction Commitments

The Hospital has committed to construction projects to renovate the ESD and Radiology departments. The estimated amount to complete the projects is approximately \$12,000,000.

#### Other

The Financial Accounting Standards Board (FASB) issued Interpretation No. 47, Accounting for Condition and Retirement Obligations, an interpretation of FASB Statement 143. This interpretation elaborates on the disclosures to be made by an organization in its financial statements about its obligations related to asset retirements. The interpretation is effective for fiscal years ending after December 15, 2005. Management has evaluated the Interpretation and determined the impact to be immaterial to the financial statements.

# MARGARET MARY COMMUNITY HOSPITAL, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2007 AND 2006

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### 11. FUNCTIONAL EXPENSES

The Hospital is an acute care hospital also providing long-term care and home health services. The Hospital has provided inpatient, outpatient and other ancillary services to the residents within its geographical region. Expenses related to providing these services for 2007 and 2006 approximate the following:

	<u>2007</u>	<u>2006</u>
Health care services	\$ 43,513,661	\$ 40,809,177
General and administrative	<u>6,145,621</u>	<u>5,763,655</u>
	<u>\$ 49,659,282</u>	<u>\$ 46,572,832</u>

### 12. DISCONTINUED OPERATIONS

In 2007, the Hospital discontinued its long-term care unit. Operating results are included in the loss from operations of the discontinued component line of the statement of operations of \$801,309 and \$585,071 for 2007 and 2006, respectively.