



**COMBINED FINANCIAL STATEMENTS**

**DECEMBER 31, 2016 AND 2015**

*CPAs / ADVISORS*



# HANCOCK REGIONAL HOSPITAL

## TABLE OF CONTENTS DECEMBER 31, 2016 AND 2015

---

	Page
<b>Report of Independent Auditors</b> .....	1
<b>Required Supplementary Information</b>	
Management’s Discussion and Analysis (Unaudited).....	i
<b>Combined Financial Statements</b>	
Combined Balance Sheets .....	3
Combined Statements of Operations and Changes in Net Position.....	5
Combined Statements of Cash Flows.....	6
Notes to Combined Financial Statements.....	8

---



Blue & Co., LLC / 500 N. Meridian Street, Suite 200 / Indianapolis, IN 46204  
main 317.633.4705 fax 317.633.4889 email blue@blueandco.com

## REPORT OF INDEPENDENT AUDITORS

Board of Trustees  
Hancock Regional Hospital  
Greenfield, Indiana

### Report on the Combined Financial Statements

We have audited the accompanying combined financial statements of Hancock Regional Hospital and component units (the "Hospital"), a component unit of Hancock County, which comprise the combined balance sheets as of December 31, 2016 and 2015, and the related combined statements of operations and changes in net position, and cash flows for the years then ended, and the related notes to the combined financial statements.

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

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the *Uniform Compliance Guidelines for Audits of Hospitals and State and Local Governments by Authorized Independent Public Accountants*, issued by the Indiana State Board of Accounts. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined financial statements.

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

Board of Trustees  
Hancock Regional Hospital  
Greenfield, Indiana

### Opinion

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

### Change in Accounting Principles

As discussed in Note 2 to the consolidated financial statements, in 2016, the Hospital adopted new accounting guidance, Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application* and GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. Our opinion is not modified with respect to this matter.

### Report on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis 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.

**Blue & Co., LLC**

Indianapolis, Indiana  
June 12, 2017

**REQUIRED SUPPLEMENTARY INFORMATION**

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

---

This section of Hancock Regional Hospital's (Hospital) annual combined financial statements presents background information and management's discussion and analysis of the Hospital's financial performance during the years ended December 31, 2016 and 2015. Please read it in conjunction with the Hospital's combined financial statements, which begin on page 3. Unless otherwise indicated, amounts are in thousands and are approximates.

### FINANCIAL HIGHLIGHTS

- The Hospital reported an increase in net position of approximately \$30,468 or 18% for the year ended 2016.
- Operating income in 2016 compared to 2015 increased by \$920 or 4%.
- Nonoperating income increased from 2016 to 2015 by \$7,410 or 476%.

### USING THIS ANNUAL REPORT

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

### THE BALANCE SHEET AND STATEMENT OF OPERATIONS AND CHANGES IN NET POSITION

Our analysis of the Hospital finances begins on page ii. One of the most important questions asked about the Hospital's finances is, "Is the Hospital as a whole better or worse off as a result of the year's activities?" The Balance Sheet and the Statement of Operations and Changes in Net 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. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

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

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED)

DECEMBER 31, 2016 AND 2015

---

### THE STATEMENT OF CASH FLOWS

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

### THE HOSPITAL'S NET POSITION

The Hospital's net position is the difference between its assets and liabilities reported in the Balance Sheet on page 3. The Hospital's net position increased in 2016 by \$30,468 (18%) as you can see from Table 1.

Table 1: Assets, Liabilities, and Net Position

	2016	2015	2016 - 2015 \$ Change	2014
<b>Assets</b>				
Current assets	\$ 116,630	\$ 112,839	\$ 3,791	\$ 78,492
Capital assets, net	79,711	78,025	1,686	65,752
Restricted and limited use assets	67,265	41,709	25,556	48,473
Other noncurrent assets	4,763	4,080	683	4,304
Total assets	<u>268,369</u>	<u>236,653</u>	<u>31,716</u>	<u>197,021</u>
<b>Liabilities</b>				
Current liabilities	68,175	66,927	1,248	49,437
Total liabilities	<u>68,175</u>	<u>66,927</u>	<u>1,248</u>	<u>49,437</u>
<b>Net Position</b>				
Net investment in capital assets	79,711	78,025	1,686	65,752
Donor restricted - expendable	5,196	4,685	511	2,413
Restricted nonexpendable	2,344	2,231	113	2,346
Unrestricted	112,943	84,785	28,158	77,073
Total net position	200,194	169,726	30,468	147,584
Total liabilities and net position	<u>\$ 268,369</u>	<u>\$ 236,653</u>	<u>\$ 31,716</u>	<u>\$ 197,021</u>

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

A significant component in the Hospital's assets is the increase in Restricted and Limited Use Assets which increased significantly by \$25,556 or 63% due primarily to funding investments with cash and market performance. Capital assets increase is attributable to the completion of a wellness center and various other projects.

### OPERATING RESULTS AND CHANGES IN THE HOSPITAL'S NET POSITION

In 2016, the Hospital's change in net position increased by \$8,326 compared to 2015 as shown in Table 2.

Table 2: Operating Results and Changes in Net Position

	2016	2015	2016 - 2015 \$ Change	2014
Operating Revenue				
Net patient service revenue	\$ 469,317	\$ 429,127	\$ 40,190	\$ 311,855
Other	7,660	7,711	(51)	9,570
Total operating revenue	476,977	436,838	40,139	321,425
Operating expenses				
Salaries and benefits	54,450	49,047	5,403	47,659
Medical supplies and drugs	48,161	37,433	10,728	24,824
Purchased services and medical fees	321,183	300,316	20,867	199,963
Depreciation and amortization	10,228	9,214	1,014	8,127
Hospital assessment fee	2,164	2,475	(311)	3,574
Other operating expense	15,003	13,485	1,518	13,966
Total operating expense	451,189	411,970	39,219	298,113
Operating income	25,788	24,868	920	23,312
Nonoperating income (expense)				
Noncapital contributions	1,310	1,529	(219)	923
Other nonoperating expense	(972)	(739)	(233)	(667)
Interest expense	-0-	-0-	-0-	(1,363)
Investment income	5,514	(2,348)	7,862	3,624
Total nonoperating income (expense)	5,852	(1,558)	7,410	2,517
Change in net position before capital distributions	31,640	23,310	8,330	25,829
Capital distributions	(1,172)	(1,168)	(4)	(1,283)
Change in net position	30,468	22,142	8,326	24,546
Net position				
Beginning of year	169,726	147,584	22,142	123,038
End of year	\$ 200,194	\$ 169,726	\$ 30,468	\$ 147,584

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

---

### SOURCES OF REVENUE

During 2016, the Hospital derived substantially all of its revenue from patient service and other related activities. Revenue includes, among other items, revenue from the Medicare and Medicaid programs, patients, insurance carriers, preferred provider organizations, and managed care programs.

The table below presents the percentages of gross revenue for patient services by payor for the Hospital's acute care operations.

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Medicare	53%	56%	51%
Medicaid	10%	6%	8%
Commercial	33%	34%	35%
Self-pay	4%	4%	6%
	<u>100%</u>	<u>100%</u>	<u>100%</u>

The Hospital provides care to patients under payment arrangement with Medicare, Medicaid, and various managed care programs. Services provided under those arrangements are paid at predetermined rates and/or reimbursable costs as defined. Provisions have been made in the financial statements for contractual adjustments, which represent the difference between the standard charges for services and the actual or estimated payment. Total operating revenue increased \$40,139 or 9% in 2016 compared to 2015. This increase was primarily the result of an increase in volumes and the addition of one long-term care facility during 2016 compared to 2015. Disproportionate Share Hospital Payment (DSH) for years 2016 and 2015 were \$1,826 and \$1,141, respectively. The Hospital recognized Electronic Health Record Incentive revenue in 2016 and 2015 of \$292 and \$374, respectively, by meeting Meaningful Use requirements. This revenue is included in other operating revenue.

### OPERATING INCOME

The first component of the overall change in the Hospital's net position is its operating income, generally the difference between net patient service and the expenses incurred to perform those services. In each of the past two years, the Hospital has reported an operating gain. This is consistent with the Hospital's entire operating history. The Hospital's operations were begun in 1951 as a county owned and operated hospital under Indiana Code 16-22.

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

---

The increase in the Hospital's operating income in 2016 of \$920 or 4% from 2015 was the result of a rate increase and volume in oncology and other volume increases in 2016. The Hospital increased gross charge rates by 5% for both years ended December 31, 2016 and 2015, respectively. More importantly, as noted previously, the Hospital's volumes increased. Total operating expenses increased \$39,219 or 10% in 2016 compared to 2015. The increase in operating expenses was the result of supplies and drugs, salaries and benefits and purchased services and medical fees. Supplies and drugs increased due to an increase in pharmaceutical costs as well as services provided for oncology services. The increase in purchased services and medical fees was primarily due to long-term care operations.

The Hospital experienced statistical changes in the following areas:

Statistical Growth	2016	2015	2016 - 2015	
			% Increase / <Decrease>	2014
Patient Days	15,257	14,965	1.95%	14,712
Diagnostic Imaging Procedures	60,482	60,443	0.06%	57,137
Laboratory Procedures	309,233	323,363	-4.37%	312,016
Pharmaceutical Medication Units	426,792	420,137	1.58%	413,698
Rehab Procedures	65,880	61,104	7.82%	61,915
Home Health Units of Service	39,840	27,162	46.68%	24,228
Outpatient Clinic Procedures	5,529	6,232	-11.28%	7,600

Excluded from net patient service revenue are charges for patient service waived under the Hospital's uncompensated care policy. Uncompensated care represents unreimbursed charges, both charity care and bad debt, incurred by the Hospital in providing uncompensated care to patients. Based on established rates, gross charges of \$4,384 were waived during 2016. This is a decrease compared to the previous year.

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

### NONOPERATING INCOME AND EXPENSES

Nonoperating income and expenses are the result of changes in the Hospital's investment income and other non-capital grants and contributions. The Hospital's investment income significantly increased primarily due to market conditions during 2016. The Hospital's nonoperating income and expenses increased in 2016 by \$7,410 from 2015.

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

---

### GRANTS AND CONTRIBUTIONS

The Hospital receives operating grants from various state and federal agencies for specific programs. Operating grants received in 2016 totaled \$843 compared to \$707 in 2015.

Some of the significant grants received by the Hospital are:

- Tobacco Cessation – From Indiana State Department of Health for prevention of tobacco use
- Rural Health Clinic – Knightstown from Indiana State Department of Health – for rural health clinic operations in Knightstown
- Critical Needs Expansion – From Hancock Regional Hospital Foundation
- Women’s Health Center
- New Cancer Center Service line – from Hancock Regional Hospital Foundation

### THE HOSPITAL’S CASH FLOWS

Changes in the Hospital’s cash flows are consistent with changes in operating income and nonoperating income and expenses as discussed earlier. The following is a summary of cash flows:

Table 3: Statements of Cash Flow

	2016	2015	Change	2014
Net cash flows from				
Operating activities	\$ 30,972	\$ 34,700	\$ (3,729)	\$ 16,901
Noncapital financing activities	337	790	(453)	40
Capital and related financing	(13,038)	(22,599)	9,560	(8,883)
Investing	(9,458)	6,042	(15,500)	(81)
Change in cash and cash equivalents	<u>\$ 8,812</u>	<u>\$ 18,934</u>	<u>\$ (10,121)</u>	<u>\$ 7,977</u>

### CAPITAL ASSETS AND DEBT ADMINISTRATION

#### CAPITAL ASSETS

During 2016, the Hospital’s net capital assets increased by approximately \$1,686. This compares to an increase of approximately \$12,273 for 2015 compared to 2014. The increase from 2015 to 2014 was due primarily to projects for oncology and the wellness center.

# HANCOCK REGIONAL HOSPITAL

## MANAGEMENT DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

---

The change in capital assets is outlined in the following table:

	2016	2015	Change	2014
Land	\$ 1,241	\$ 1,241	\$ -0-	\$ 1,241
Land improvements	8,457	6,845	1,612	5,776
Buildings and fixed equipment	123,267	113,252	10,015	107,425
Major movable equipment	82,953	76,966	5,987	65,505
Construction in progress	277	6,024	(5,747)	3,102
Total capital assets	<u>216,195</u>	<u>204,328</u>	<u>11,867</u>	<u>183,049</u>
Less accumulated depreciation	<u>136,484</u>	<u>126,303</u>	<u>10,181</u>	<u>117,297</u>
Capital assets, net	<u>\$ 79,711</u>	<u>\$ 78,025</u>	<u>\$ 1,686</u>	<u>\$ 65,752</u>

Capital assets, net increased as additions exceeded depreciation. More detailed information about the Hospital's capital assets is presented in the notes to the combined financial statements.

### DEBT

During 2014, the Hospital had retired its revenue notes, mortgage loans, and capital lease obligations outstanding.

### CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

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

# HANCOCK REGIONAL HOSPITAL

## COMBINED BALANCE SHEETS DECEMBER 31, 2016 AND 2015

---

### ASSETS

	2016	2015
<b>Current assets</b>		
Cash and cash equivalents	\$ 48,564,972	\$ 51,162,965
Investments	1,638,634	1,542,655
Patient accounts receivable, net	42,618,303	41,293,926
Inventories and other current assets	23,808,429	18,839,761
Total current assets	<u>116,630,338</u>	<u>112,839,307</u>
<b>Assets whose use is limited</b>		
Board designated funds	62,069,515	37,024,241
Donor restricted funds	5,195,803	4,685,059
Total assets whose use is limited	<u>67,265,318</u>	<u>41,709,300</u>
<b>Capital assets</b>		
Land and land improvements	9,698,502	8,086,584
Buildings and fixed equipment	123,267,332	113,252,238
Major movable equipment	82,952,827	76,965,791
Construction in progress	276,302	6,023,237
Total capital assets	<u>216,194,963</u>	<u>204,327,850</u>
Less accumulated depreciation	136,484,228	126,303,130
Capital assets, net	<u>79,710,735</u>	<u>78,024,720</u>
<b>Other assets</b>	<u>4,762,784</u>	<u>4,080,061</u>
Total assets	<u>\$ 268,369,175</u>	<u>\$ 236,653,388</u>

---

See accompanying notes to combined financial statements

# HANCOCK REGIONAL HOSPITAL

COMBINED BALANCE SHEETS  
DECEMBER 31, 2016 AND 2015

---

## LIABILITIES AND NET POSITION

	2016	2015
<b>Current liabilities</b>		
Accounts payable and other liabilities	\$ 60,035,239	\$ 57,358,545
Accrued salaries and related liabilities	4,948,401	4,378,121
Estimated third-party settlements	3,191,808	5,190,094
Total current liabilities	<u>68,175,448</u>	<u>66,926,760</u>
Total liabilities	68,175,448	66,926,760
<b>Net position</b>		
Net investment in capital assets	79,710,735	78,024,720
Donor restricted expendable	5,195,803	4,685,059
Restricted nonexpendable	2,344,144	2,231,678
Unrestricted	<u>112,943,045</u>	<u>84,785,171</u>
Total net position	<u>200,193,727</u>	<u>169,726,628</u>
Total liabilities and net position	<u>\$ 268,369,175</u>	<u>\$ 236,653,388</u>

---

See accompanying notes to combined financial statements

# HANCOCK REGIONAL HOSPITAL

## COMBINED STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
<b>Operating revenue</b>		
Net patient service revenue	\$ 469,316,873	\$ 429,127,337
Other operating revenue	7,660,267	7,711,117
Total operating revenue	476,977,140	436,838,454
<b>Operating expenses</b>		
Salaries and wages	43,224,257	39,738,133
Employee benefits	11,225,878	9,308,776
Professional medical fees	2,457,324	2,704,663
Supplies and drugs	48,160,665	37,432,821
Purchased services	318,725,231	297,611,060
Utilities and insurance	10,114,616	8,790,802
Depreciation and amortization	10,228,366	9,214,446
Hospital assessment fee	2,164,473	2,474,784
Other	4,888,823	4,694,573
Total operating expenses	451,189,633	411,970,058
Operating income	25,787,507	24,868,396
<b>Nonoperating income (expense), net</b>		
Noncapital contributions	1,310,342	1,529,340
Other nonoperating expense	(973,172)	(739,051)
Investment income	5,514,148	(2,348,153)
Total non-operating income (expense), net	5,851,318	(1,557,864)
Change in net position before capital distributions	31,638,825	23,310,532
<b>Capital distributions - noncontrolling interest</b>	(1,171,726)	(1,167,744)
Change in net position	30,467,099	22,142,788
<b>Net position</b>		
Beginning of year	169,726,628	147,583,840
End of year	\$ 200,193,727	\$ 169,726,628

See accompanying notes to combined financial statements

# HANCOCK REGIONAL HOSPITAL

## COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
<b>Operating activities</b>		
Cash received from patients and third party payors	\$ 465,994,210	\$ 409,202,344
Cash paid to employees for wages and benefits	(53,879,855)	(50,169,631)
Cash paid to vendors for goods and services	(388,803,106)	(332,043,395)
Other operating receipts	7,660,267	7,711,117
Net cash from operating activities	30,971,516	34,700,435
<b>Noncapital financing activities</b>		
Noncapital contributions	1,310,342	1,529,340
Other nonoperating	(973,172)	(739,051)
Net cash from noncapital financing activities	337,170	790,289
<b>Capital and related financing activities</b>		
Acquisition and construction of capital assets	(11,880,993)	(21,557,060)
Loss on disposal of capital assets	14,285	126,012
Capital distributions - noncontrolling interest	(1,171,726)	(1,167,744)
Net cash from capital and related financing activities	(13,038,434)	(22,598,792)
<b>Investing activities</b>		
Other assets	(682,723)	224,106
Investment income	5,514,148	(2,348,153)
Other changes in assets whose use is limited, net	(14,289,286)	8,165,705
Net cash from investing activities	(9,457,861)	6,041,658
Net change in cash and cash equivalents	8,812,391	18,933,590
<b>Cash and cash equivalents</b>		
Beginning of year	52,613,197	33,679,607
End of year	\$ 61,425,588	\$ 52,613,197

See accompanying notes to combined financial statements

# HANCOCK REGIONAL HOSPITAL

## COMBINED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2016 AND 2015

---

	<u>2016</u>	<u>2015</u>
<b>Reconciliation of operating income to net cash from operating activities</b>		
Operating income	\$ 25,787,507	\$ 24,868,396
Adjustment to reconcile operating income to net cash from operating activities		
Depreciation and amortization	10,228,366	9,214,446
Bad debts	11,862,680	12,810,713
Changes in assets and liabilities		
Patient accounts receivable	(13,187,057)	(20,239,685)
Other current assets	(4,968,668)	(9,442,750)
Accounts payable and other liabilities	2,676,694	16,267,111
Accrued salaries and related liabilities	570,280	(1,122,722)
Estimated third-party settlements	(1,998,286)	2,344,926
Net cash from operating activities	<u>\$ 30,971,516</u>	<u>\$ 34,700,435</u>
 <b>Reconciliation of cash and cash equivalents to the balance sheets</b>		
Cash and cash equivalents:		
In current assets	\$ 48,564,972	\$ 51,162,965
In investments and assets whose use is limited	12,860,616	1,450,232
Total cash and cash equivalents	<u>\$ 61,425,588</u>	<u>\$ 52,613,197</u>

---

See accompanying notes to combined financial statements

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### 1. SIGNIFICANT ACCOUNTING POLICIES

#### Organization and Reporting Entity

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

Pursuant to the provision of long-term care, HRH owns the operations of several long-term care facilities by way of an arrangement with the managers of the facilities. These facilities provide inpatient and therapy services. Generally, gross revenues from the operations of the long-term care facilities are the property of HRH and HRH is responsible for the associated operating expenses and working capital requirements. While the management and related lease agreements are in effect, the performance of all activities of the managers shall be on behalf of HRH and HRH retains the authority and legal responsibility for the operations of the facilities.

Specifically, HRH entered into lease agreements with the long-term care facilities to lease the facilities managed by the managers. Concurrently, HRH entered into agreements with the managers to manage the leased facilities. As part of the agreements, HRH will pay the managers a management fee to continue managing the facilities on behalf of HRH in accordance with the terms of the agreements. The agreements expire at various times and are generally automatically extended for successive terms unless appropriately terminated. All parties involved can terminate the agreement without cause with a written notice.

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

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### Blended Component Units

The accompanying combined financial statements include the accounts of Hancock Regional Hospital Foundation, Inc. (Foundation), a separate not-for-profit entity organized to support the operations of HRH. The accompanying combined financial statements also include the accounts of the Blended Component Unit – Hancock Regional Surgery Center, LLC (HRSC) and O3PureMed, LLC (O3PureMed); both are separate limited liability companies. All significant intercompany transactions have been eliminated for financial reporting purposes.

HRSC was formed for the purpose of owning and operating a multi-specialty ambulatory surgery facility that provides the medical, management and administrative support necessary for licensed physicians to perform non-emergency surgical procedures on an outpatient basis. HRH's membership interest in HRSC is 51%. HRH maintains substantial participation in the operations of HRSC in addition to an economic interest in HRSC's financial position.

O3PureMed was formed for the purpose of operating a medical and infectious waste treatment facility. HRH's membership interest in O3PureMed is 100%.

The separate financial statements for each of the entities discussed above may be obtained through contacting management of HRH. All entities contained in the combined financial statements are collectively referred to as the "Hospital".

### Use of Estimates

The preparation of combined financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements.

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

### Measurement Focus and Basis of Accounting

The combined financial statements are reported using the economic resources measurement focus and on the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### Cash and Cash Equivalents

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

### Patient Accounts Receivable and Net Patient Service Revenue

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

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

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

The Hospital is a provider of services to patients entitled to coverage under Titles XVIII and XIX of the Health Insurance Act (Medicare and Medicaid). The Hospital is reimbursed for Medicare and Medicaid inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG).

The Hospital is reimbursed for Medicare and Medicaid outpatient services based on a fixed price per clinical unit of service. Differences between the total program billed charges and the payments received are reflected as deductions from revenue. At HRH's year-end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients.

These programs have audited the year-end cost report filed with the Medicare program through December 31, 2013. There were no significant differences reflected as deductions from revenue during 2016 and 2015. Amounts for unresolved cost reports for 2014 through 2016 are reflected in estimated third-party settlements on the combined balance sheets.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

The Hospital participates in the Indiana Hospital Assessment Fee (HAF) Program. The purpose of the HAF Program is to fund the State share of enhanced Medicaid payments and Medicaid Disproportionate Share (DSH) payments for Indiana hospitals as reflected in the Hospital Assessment Fee reported in the combined statements of operations and changes in net position. Previously, the State's share was funded by governmental entities through intergovernmental transfers.

The Medicaid enhanced payments relate to both fee for service and managed care claims. Under the HAF Program, the enhanced Medicaid payments follow the patients and are realized through increased Medicaid rates. During 2016 and 2015, HRH recognized HAF Program expense of approximately \$2,164,000 and \$2,475,000, respectively. The Medicaid rate increases under the HAF Program are included in patient service revenue in the combined statements of operations and changes in net position.

Net revenue from the Medicare and Medicaid programs accounted for approximately 84 percent of the Hospital's net patient revenue for the year ended 2016, and 79 percent of the Hospital's net patient revenue, for the year ended 2015. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

The Hospital recognized revenue related to the Medicaid Disproportionate Share Hospital and the Upper Payment Limitation programs of approximately \$1,800,000 and \$2,475,000 for the years ended December 31, 2016 and 2015, respectively. These amounts are reimbursements for providing care to the uninsured and underinsured and are included in net patient service revenue within the combined statements of operations and changes in net position.

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

### Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy on a sliding scale on the basis of financial need. Because the Hospital does not pursue collection of approved charity care balances, the charges are not reflected in net revenue. Rather, charges approved for charity are posted to gross revenue and subsequently written off as a charity adjustment before the resulting net patient service revenue.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

Of the Hospital's total expenses (excluding subsidiaries and long-term care operations) reported within the combined statements of operations and changes in net position, an estimated \$1,579,000 and \$1,628,000 arose from providing services to charity patients during 2016 and 2015, respectively. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the Hospital's total expenses divided by gross patient service revenue.

### Inventories

Inventories are valued at the lower of cost (first-in, first-out method) or market. Inventory at year-end consists mainly of pharmaceuticals and medical supplies.

### Assets Whose Use is Limited and Investments

Assets whose use is limited include investments designated by HRH's Board for internal purposes, investments and other assets restricted by donors for a specific purpose and investments held by trustees for debt service and continued construction projects.

Assets whose use is limited and investments consist of money market funds and mutual funds that are reported at fair value. Assets whose use is limited and investments also consist of certificates of deposit which are recorded at contract value. Interest, dividends, and gains and losses, both realized and unrealized, are included in nonoperating income when earned.

### Capital Assets and Depreciation

Capital assets such as property and equipment are stated at cost and include expenditures for new additions and other costs added to existing facilities, which exceed \$1,000 and meet certain useful life thresholds. Maintenance, repairs and minor renewals are expensed as incurred. The Hospital provides for depreciation of property and equipment using annual rates, which are sufficient to depreciate the cost of depreciable assets over their estimated useful lives using the straight-line method.

The ranges of useful lives in computing depreciation include the following:

<u>Description</u>	<u>Range of Useful Lives</u>
Land improvements	8-15 years
Buildings and fixed equipment	5-40 years
Major movable equipment	3-20 years

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### Costs of Borrowing

Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. No amounts were capitalized as of December 31, 2016 and 2015.

### Income Taxes

HRH is a governmental instrumentality organized under Title 16, Article 22, of the Indiana statutes. The Hospital is exempt from federal income tax under Section 115 of the Internal Revenue Code of 1986. As such, HRH is exempt from federal income tax as a unit of local government. No income tax filings are required of the Hospital as it is a governmental instrumentality.

The Foundation is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (Code) and is exempt from federal and state income taxes on related income pursuant to Section 501(a) of the Code. However, the Foundation is required to file Federal Form 990 – Return of Organization Exempt from Income Tax which is an informational return only.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Hospital and recognize a tax liability if the Hospital has taken an uncertain position that more likely than not would not be sustained upon examination by various federal and state taxing authorities.

Management has analyzed the tax positions taken by the Hospital and has concluded that as of December 31, 2016 and 2015, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying combined financial statements. The Hospital is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

HRSC and O3PureMed are organized as a limited liability company, whereby net taxable income is taxed directly to the members of the limited liability company. Thus, the combined financial statements do not include any provision for federal or state income taxes related to HRSC or O3PureMed.

These entities have filed their federal and state income tax returns for periods through their most recent fiscal year ends. These income tax returns are generally open to examination by the relevant taxing authorities for a period of three years from the later of the date the return was filed or its due date (including approved extensions).

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### Advertising and Community Relations

The Hospital records advertising and promotion expense in the period incurred. Total expense for advertising and promotion was approximately \$635,000 and \$713,000 for 2016 and 2015, respectively.

### Compensated Absences

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

### Net Position

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

### Donor Restricted Net Position

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

### Operating Revenues and Expenses

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

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### Electronic Health Records (EHR) Incentive Payments

HRH receives EHR incentive payments under the Medicare and Medicaid programs. To qualify for the EHR incentive payments, HRH must meet "meaningful use" criteria that become more stringent over time. HRH periodically submits and attests to its use of certified EHR technology, satisfaction of meaningful use objectives, and various patient data.

These submissions generally include performance measures for each annual EHR reporting period (Federal fiscal year ending September 30th). The related EHR incentive payments are paid out over a four year transition schedule and are based upon data that is captured in HRH's cost reports.

The payment calculation is based upon an initial amount as adjusted for discharges, Medicare and Medicaid utilization using inpatient days multiplied by a factor of total charges excluding charity care to total charges, and a transitional factor that ranges from 100% in first payment year and thereby decreasing by 25% each payment year until it is completely phased out in the fifth year.

HRH recognizes EHR incentive revenues as income when there is reasonable assurance that HRH will comply with the conditions of the meaningful use objectives and any other specific requirements. In addition, the financial statement effects of the income must be both recognizable and measurable. During 2016 and 2015, HRH recognized approximately \$292,000 and \$374,000, respectively, in EHR incentive revenue. Under the ratable recognition method, HRH recognizes revenue ratably over the entire EHR reporting period when it is reasonably assured at the outset of the EHR reporting period that it will comply with the minimum requirements of the program.

EHR incentive income is included in other operating revenue in the combined statements of operations and changes in net position. EHR incentive income recognized is based on management's estimate and amounts are subject to change, with such changes impacting operations in the period the changes occur.

Receipt of these funds is subject to the fulfillment of certain obligations by HRH as prescribed by the programs, subject to future audits and may be subject to repayment upon a determination of noncompliance.

### Contributions

From time to time, the Hospital receives contributions from individuals and private organizations. Revenues from contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Contributions may be restricted either for specific operating purposes or for capital purposes.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

### Restricted Resources

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

### Litigation

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

### Risk Management

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

### Accounting for Noncontrolling Interest

The Hospital has classified the noncontrolling interest as a component of restricted nonexpendable net position in the combined balance sheets. Noncontrolling interests represent the portion of the net position that is attributable to investors that are external to and not included in the Hospital's combined financial statements.

### Reclassification

Certain amounts in the prior year combined financial statements have been reclassified for comparative purposes to conform to the current year presentation. The reclassifications had no effect on the previously reported net position and change in net position.

### Subsequent Events

The Hospital evaluated events or transactions occurring subsequent to the combined balance sheet date for recognition and disclosure in the accompanying combined financial statements through the date the combined financial statements are available to be issued which is June 12, 2017.

---

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### **2. CHANGE IN ACCOUNTING PRINCIPLES**

During 2016, the Hospital implemented GASB Statement No. 72 *Fair Value Measurement and Application*. This statement addressed accounting and financial reporting issues related to fair value measurements. This statement provides guidance for determining a fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. There was no impact to these combined financial statement disclosures as a result of adoption of this standard as these disclosures have been provided historically.

During 2016, the Hospital implemented GASB Statement No. 76 *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addressed the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. There was no impact to these combined financial statement disclosures as a result of adoption of this standard.

### **3. INVESTMENTS AND ASSETS WHOSE USE IS LIMITED**

#### Board Designated Funds

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

#### Donor Restricted Funds

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

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

The following represents assets whose use is limited and investments as of December 31, 2016 and 2015:

	2016	2015
Board designated funds	\$ 62,069,515	\$ 37,024,241
Donor restricted funds	5,195,803	4,685,059
Total assets whose use is limited	67,265,318	41,709,300
Investments	1,638,634	1,542,655
	<u>\$ 68,903,952</u>	<u>\$ 43,251,955</u>
	2016	2015
Mutual funds - equities	\$ 34,037,945	\$ 26,883,358
Mutual funds - fixed income	20,266,930	14,668,580
Certificates of deposit	250,041	249,785
Common stocks	1,488,420	-0-
Money market funds	12,860,616	1,450,232
	<u>\$ 68,903,952</u>	<u>\$ 43,251,955</u>

The common stocks are held by the Foundation.

#### 4. DEPOSITS AND INVESTMENTS

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

Investments are carried at fair market value. Net realized gains and losses on security transactions are determined on the specific identification cost basis. Assets whose use is limited investments consist of cash equivalents, certificates of deposit and mutual funds.

## HANCOCK REGIONAL HOSPITAL

### NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

The Hospital's investments generally are reported at fair value. As of December 31, 2016 and 2015, the Hospital had the following investments and maturities, all of which were held in the Hospital's name by custodial financial institutions that are agents of the Hospital.

December 31, 2016					
	Carrying Amount	Investment Maturities (in years)			
		Less than 1	1-5	6-10	More than 10
Money market funds	\$12,860,616	\$12,860,616	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit	250,041	250,041	-0-	-0-	-0-
Common stocks	1,488,420	1,488,420	-0-	-0-	-0-
Mutual funds - equities	34,037,945	34,037,945	-0-	-0-	-0-
Mutual funds - fixed income	20,266,930	20,266,930	-0-	-0-	-0-
	\$68,903,952	\$68,903,952	\$ -0-	-0-	\$ -0-

December 31, 2015					
	Carrying Amount	Investment Maturities (in years)			
		Less than 1	1-5	6-10	More than 10
Money market funds	\$ 1,450,232	\$ 1,450,232	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit	249,785	249,785	-0-	-0-	-0-
Mutual funds - equities	26,883,358	26,883,358	-0-	-0-	-0-
Mutual funds - fixed income	14,668,580	14,668,580	-0-	-0-	-0-
	\$43,251,955	\$43,251,955	\$ -0-	\$ -0-	\$ -0-

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

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

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

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

Deposits and investments consist of the following as of December 31, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Carrying amount		
Deposits	\$ 48,564,972	\$ 51,162,965
Investments	68,903,952	43,251,955
	<u>\$ 117,468,924</u>	<u>\$ 94,414,920</u>
Included in the balance sheet captions		
Cash and cash equivalents	\$ 48,564,972	\$ 51,162,965
Investments	1,638,634	1,542,655
Board designated funds	62,069,515	37,024,241
Donor restricted funds	5,195,803	4,685,059
	<u>\$ 117,468,924</u>	<u>\$ 94,414,920</u>

### 5. FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1) and the lowest priority to unobservable inputs (level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Hospital has the ability to access.
- Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.
- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

---

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

The Hospital's policy is to recognize transfers between levels as of the end of the reporting period. There were no significant transfers between levels during 2016 and 2015.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2016 and 2015.

- *Mutual funds*: Valued at the daily closing price as reported by the fund. Mutual funds held by the Hospital are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value and to transact at that price. The mutual funds held by the Hospital are deemed to be actively traded.
- *Common stocks*: Valued at the closing price reported on the active market on which the individual securities are traded.
- *Money market funds*: Generally transact subscription and redemption activity at a \$1 stable net asset value (NAV) however, on a daily basis the funds are valued at their daily NAV calculated using the amortized cost of the securities held in the fund.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

The following table sets forth by level, within the hierarchy, the Hospital's assets and liabilities measured at fair value on a recurring basis as of December 31, 2016 and 2015.

	December 31, 2016			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Investments and assets whose use is limited				
Mutual funds - equities				
Large blend	\$ 11,836,602	\$ 11,836,602	\$ -0-	\$ -0-
Large growth	4,839,908	4,839,908	-0-	-0-
Large value	7,850,757	7,850,757	-0-	-0-
Medium growth	1,603,596	1,603,596	-0-	-0-
Small value	2,293,691	2,293,691	-0-	-0-
Small blend	888,808	888,808	-0-	-0-
Other (global, commodities, and index)	4,724,583	4,724,583	-0-	-0-
Total mutual funds - equities	34,037,945	34,037,945	-0-	-0-
Mutual funds - fixed income				
Intermediate term bond	18,870,107	18,870,107	-0-	-0-
Short-term bond	1,396,823	1,396,823	-0-	-0-
Total mutual funds - fixed income	20,266,930	20,266,930	-0-	-0-
Common stocks				
Consumer goods	410,527	410,527	-0-	-0-
Energy	59,446	59,446	-0-	-0-
Financial	236,999	236,999	-0-	-0-
Healthcare	212,112	212,112	-0-	-0-
Industrials	66,077	66,077	-0-	-0-
Services	79,276	79,276	-0-	-0-
Technology	350,908	350,908	-0-	-0-
Utilities	73,075	73,075	-0-	-0-
Total common stocks	1,488,420	1,488,420	-0-	-0-
Money market funds	12,860,616	-0-	12,860,616	-0-
		\$ 54,304,875	\$ 12,860,616	\$ -0-
Certificates of deposit *	250,041			
	<u>\$ 68,903,952</u>			
<b>December 31, 2015</b>				
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Investments and assets whose use is limited				
Mutual funds - equities				
Large blend	\$ 11,772,705	\$ 11,772,705	\$ -0-	\$ -0-
Large growth	4,921,194	4,921,194	-0-	-0-
Large value	3,358,713	3,358,713	-0-	-0-
Medium growth	3,617,953	3,617,953	-0-	-0-
Small blend	969,104	969,104	-0-	-0-
Other (global, commodities, and index)	2,243,689	2,243,689	-0-	-0-
Total mutual funds - equities	26,883,358	26,883,358	-0-	-0-
Mutual funds - fixed income				
Intermediate term bond	11,096,208	11,096,208	-0-	-0-
Short-term bond	1,069,420	1,069,420	-0-	-0-
World bond	2,502,952	2,502,952	-0-	-0-
Total mutual funds - fixed income	14,668,580	14,668,580	-0-	-0-
Money market fund	1,450,232	-0-	1,450,232	-0-
		\$ 41,551,938	\$ 1,450,232	\$ -0-
Certificates of deposit *	249,785			
	<u>\$ 43,251,955</u>			

\* Certificates of deposit are reported at contract value

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

The following methods and assumptions were used by the Hospital in estimating the fair value of its financial instruments:

Cash and cash equivalents, patient accounts receivable, assets whose use is limited, accounts payable, other current liabilities, salaries, wages and related liabilities and estimated third-party settlements: The carrying amount reported in the combined balance sheet for cash and cash equivalents, patient accounts receivable, accounts payable, other current liabilities, salaries, wages and related liabilities and estimated third-party settlements approximate fair value based on short-term maturities.

### 6. ACCOUNTS RECEIVABLE AND PAYABLE

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities as of December 31, 2016 and 2015 is as follows:

	2016	2015
Patient accounts receivable		
Receivable from patients and their insurance carriers	\$ 46,515,919	\$ 28,665,810
Receivable from Medicare	13,058,896	13,058,896
Receivable from Medicaid	3,726,404	3,726,404
Receivable from long-term care operations	27,493,259	28,673,549
Total patient accounts receivable	90,794,478	74,124,659
Less contractual allowances	(31,882,602)	(22,557,005)
Less allowance for uncollectible amounts	(16,293,573)	(10,273,728)
Patient accounts receivable, net	<u>\$ 42,618,303</u>	<u>\$ 41,293,926</u>
Accounts payable and accrued expenses		
Payable to employees (including payroll taxes and benefits)	\$ 4,948,401	\$ 4,378,121
Payable to suppliers and other accrued expenses	60,035,239	57,358,545
Total accounts payable and accrued expenses	<u>\$ 64,983,640</u>	<u>\$ 61,736,666</u>

### 7. INVESTMENTS IN AFFILIATES

HRH owns 50% of Hancock Physician Network, LLC (Network) and has recorded the investment on the equity method of accounting in the amount of \$1,019,093 and \$1,222,100 as of December 31, 2016 and 2015, respectively. This investment is included within other assets in the combined financial statements. HRH paid the Network approximately \$3,362,000 and \$2,896,000 during 2016 and 2015, respectively for management and other operating expenses.

## HANCOCK REGIONAL HOSPITAL

### NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

HRH received approximately \$3,574,000 and \$2,769,000 for 2016 and 2015, respectively from the Network for rental, housecleaning and related income. HRH contributed capital of approximately \$5,479,000 and \$3,986,000 to the Network during 2016 and 2015, respectively.

HRH has a receivable from the Network of approximately \$1,872,000 and \$401,000 as of December 31, 2016 and 2015, respectively. The Hospital has a payable to the Network of approximately \$788,000 and \$505,000 as of December 31, 2016 and 2015, respectively. HRH expects to continue providing capital contributions to the Network at a commensurate level with its past experience.

HRH also owns 50% of a Physician Hospital Organization (PHO), 50% of Suburban Home Health (SHH) and approximately 37% of Parkway, LLC. HRH has recorded these investments in affiliates on the equity method of accounting within other assets in the combined financial statements.

The separate financial statements for each of the entities above may be obtained through contacting management of HRH.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

### 8. CAPITAL ASSETS

Capital assets consist of the following as of December 31, 2016 and 2015:

	Balance December 31, 2015				Balance December 31, 2016
	Additions	Retirements	Transfers		
Land	\$ 1,241,194	\$ -0-	\$ -0-	\$ -0-	\$ 1,241,194
Land improvements	6,845,390	36,900	-0-	1,575,018	8,457,308
Buildings and fixed equipment	113,252,238	3,053,383	-0-	6,961,711	123,267,332
Major movable equipment	76,965,791	4,535,703	(13,880)	1,465,213	82,952,827
Construction in progress	6,023,237	4,255,007	-0-	(10,001,942)	276,302
Total capital assets	204,327,850	11,880,993	(13,880)	-0-	216,194,963
Less accumulated depreciation					
Land improvements	(4,653,992)	(402,779)	-0-	-0-	(5,056,771)
Buildings and fixed equipment	(68,986,825)	(4,083,250)	-0-	-0-	(73,070,075)
Major movable equipment	(52,662,313)	(5,694,664)	(405)	-0-	(58,357,382)
Total accumulated depreciation	(126,303,130)	(10,180,693)	(405)	-0-	(136,484,228)
Capital assets, net	\$ 78,024,720	\$ 1,700,300	\$ (14,285)	\$ -0-	\$ 79,710,735

  

	Balance December 31, 2014				Balance December 31, 2015
	Additions	Retirements	Transfers		
Land	\$ 1,241,194	\$ -0-	\$ -0-	\$ -0-	\$ 1,241,194
Land improvements	5,775,926	-0-	-0-	1,069,464	6,845,390
Buildings and fixed equipment	107,425,114	1,433,395	(152,952)	4,546,681	113,252,238
Major movable equipment	65,504,760	8,401,526	(125,199)	3,184,704	76,965,791
Construction in progress	3,101,947	11,722,139	-0-	(8,800,849)	6,023,237
Total capital assets	183,048,941	21,557,060	(278,151)	-0-	204,327,850
Less accumulated depreciation					
Land improvements	(4,367,125)	(286,867)	-0-	-0-	(4,653,992)
Buildings and fixed equipment	(65,016,154)	(4,071,676)	101,005	-0-	(68,986,825)
Major movable equipment	(47,913,301)	(4,800,146)	51,134	-0-	(52,662,313)
Total accumulated depreciation	(117,296,580)	(9,158,689)	152,139	-0-	(126,303,130)
Capital assets, net	\$ 65,752,361	\$ 12,398,371	\$ (126,012)	\$ -0-	\$ 78,024,720

At December 31, 2016, the Hospital did not have any significant commitments related to capital assets.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### 9. PATIENT SERVICE REVENUE

Patient service revenue for 2016 and 2015 consists of the following:

	2016	2015
Inpatient	\$ 70,243,247	\$ 62,975,243
Outpatient	249,149,722	210,923,621
Long-Term Care	353,474,422	323,163,073
Geriatric Psychiatric	5,330,176	4,679,101
Patient service revenue	<u>678,197,567</u>	<u>601,741,038</u>
Contractual allowance	192,634,328	158,704,808
Bad debts	11,862,680	9,655,240
Charity care	4,383,686	4,253,653
Deductions from revenue	<u>208,880,694</u>	<u>172,613,701</u>
Net patient service revenue	<u>\$ 469,316,873</u>	<u>\$ 429,127,337</u>

### 10. PENSION PLAN

The Hospital offers a defined contribution plan that covers all employees who meet eligibility requirements as to age and length of service and who elect to participate. The name of Plan is the Hancock Regional Hospital 403(b) Plan and is administered by MetLife. The plan was established by written agreement between the Board of Trustees and the plan administrator. The contribution requirements of participants of the plan are established and can be amended by written agreement. The Hospital matches 50% of the employee contribution up to 4% of the eligible wages. Pension expense related to this plan was approximately \$1,355,000 and \$1,236,000 in 2016 and 2015, respectively.

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

### 11. CONCENTRATION OF CREDIT RISK

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

	Receivables		Revenue	
	2016	2015	2016	2015
Medicare	35%	36%	53%	56%
Medicaid	10%	10%	10%	6%
Commercial	29%	33%	33%	34%
Self pay and other	26%	21%	4%	4%
	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

The majority of the patient accounts receivable and related revenues from long-term care operations are concentrated in Medicare and Medicaid.

### 12. ACCOUNTING FOR NONCONTROLLING INTEREST

The following depicts the changes in combined net position attributable to the controlling financial interest of the Hospital and the noncontrolling interest as of December 31, 2016 and 2015:

	Controlling interest	Noncontrolling interest	Total
Net position			
December 31, 2014	\$ 145,237,698	\$ 2,346,142	\$ 147,583,840
Change in net position before capital distributions	22,257,252	1,053,280	23,310,532
Capital distributions	-0-	(1,167,744)	(1,167,744)
Change in net position	<u>22,257,252</u>	<u>(114,464)</u>	<u>22,142,788</u>
December 31, 2015	167,494,950	2,231,678	169,726,628
Change in net position before capital distributions	30,354,633	1,284,192	31,638,825
Capital distributions	-0-	(1,171,726)	(1,171,726)
Change in net position	<u>30,354,633</u>	<u>112,466</u>	<u>30,467,099</u>
December 31, 2016	<u>\$ 197,849,583</u>	<u>\$ 2,344,144</u>	<u>\$ 200,193,727</u>

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

### 13. SELF-INSURED HEALTH CLAIMS

The Hospital is self-insured for employee health claims. A third party administrator processes the claims for the Hospital. The Hospital maintains an estimated liability for the amount of claims incurred but not reported.

The Hospital maintains reinsurance including a stop loss for specific incident claims generally over \$300,000. Substantially all employees are covered for major medical benefits. The total health claims expense was approximately \$7,827,000 and \$6,090,000 for 2016 and 2015, respectively.

Claim expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. The Hospital has recorded the accrual for the unpaid claims estimate within accrued salaries and related liabilities on the combined financial statements.

Changes in the accrual for unpaid claims for 2016 and 2015 are as follows:

	2016	2015
Unpaid claims estimate, beginning of year	\$ 497,652	\$ 619,058
Incurred claims and changes in estimates	7,826,812	6,090,012
Claims payments	(7,739,785)	(6,211,418)
Unpaid claims estimate, end of year	<u>\$ 584,679</u>	<u>\$ 497,652</u>

### 14. COMMITMENTS AND CONTINGENCIES

#### Malpractice Insurance

The Indiana Medical Malpractice Act, IC 27-12 (the Act), provides a recovery for an occurrence of malpractice and for any injury or death of a patient due to an act of malpractice in excess of certain thresholds. The Act requires the Hospital to maintain medical malpractice liability insurance on a per individual basis and in the annual aggregate for amounts below the thresholds of the Act. During 2001, the Hospital's malpractice carrier filed bankruptcy. The Hospital has obtained malpractice coverage through another carrier.

## HANCOCK REGIONAL HOSPITAL

### NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

---

The Hospital may be liable for certain pending claims incurred while with the former carrier. Management is not aware of any related material adverse effects to its financial position, results of operations, and cash flows. Prior to July 1, 1999, the Indiana Medical Malpractice Act provided for a maximum recovery of \$750,000 per individual (\$3,000,000 annual aggregate) for professional liability, \$100,000 of which would be paid through the Hospital's malpractice insurance coverage and the balance would be paid by the State of Indiana Patient Compensation Fund (Fund). For claims on or after July 1, 1999, the Indiana Medical Malpractice Act provides for a maximum recovery of \$1,250,000 per individual (\$7,500,000 annual aggregate) with the first \$250,000 covered by the Hospital's insurance and the remainder by the Fund. Changes to the Act have been made and will be effective for claims commencing July 1, 2017. The changes increase the maximum recovery to \$1,650,000 with the healthcare provider responsible for the first \$400,000.

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

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

### 15. BLENDED COMPONENT UNITS

Below is condensed, combining financial information of the blended component units.

	2016			
	Foundation	HRSC	O3PureMed	Total
<b>Assets</b>				
Current assets	\$ 1,783,688	\$ 5,065,337	\$ 113,374	\$ 6,962,399
Capital assets	9,495	873,524	1,309,088	2,192,107
Assets whose use is limited	5,195,803	-0-	-0-	5,195,803
Total assets	<u>\$ 6,988,986</u>	<u>\$ 5,938,861</u>	<u>\$ 1,422,462</u>	<u>\$ 14,350,309</u>
<b>Liabilities</b>				
Accounts payable and other liabilities	122,453	1,020,013	99,287	1,241,753
Total liabilities	<u>122,453</u>	<u>1,020,013</u>	<u>99,287</u>	<u>1,241,753</u>
<b>Net position</b>				
Unrestricted	1,661,235	4,045,324	14,087	5,720,646
Net investment in capital assets	9,495	873,524	1,309,088	2,192,107
Donor restricted-expendable	5,195,803	-0-	-0-	5,195,803
Total net position	<u>6,866,533</u>	<u>4,918,848</u>	<u>1,323,175</u>	<u>13,108,556</u>
Total liabilities and net position	<u>\$ 6,988,986</u>	<u>\$ 5,938,861</u>	<u>\$ 1,422,462</u>	<u>\$ 14,350,309</u>
Operating revenues (patient and other)	\$ -0-	\$ 12,421,100	\$ 112,432	\$ 12,533,532
<b>Expenses</b>				
Depreciation	-0-	356,538	268,599	625,137
Other expenses	-0-	9,411,524	509,714	9,921,238
Total expenses	<u>-0-</u>	<u>9,768,062</u>	<u>778,313</u>	<u>10,546,375</u>
Operating income (loss)	-0-	2,653,038	(665,881)	1,987,157
Nonoperating revenues, net	663,759	-	-0-	663,759
Capital contributions (distributions)	-0-	(2,600,000)	400,000	(2,200,000)
Change in net position	663,759	53,038	(265,881)	450,916
Net position, beginning of year	6,202,774	4,865,810	1,589,056	12,657,640
Net position, end of year	<u>\$ 6,866,533</u>	<u>\$ 4,918,848</u>	<u>\$ 1,323,175</u>	<u>\$ 13,108,556</u>
<b>Net cash flows from</b>				
Operating activities	\$ -0-	\$ 3,009,576	\$ (509,714)	\$ 2,499,862
Noncapital financing activities	202,538	-0-	-0-	202,538
Capital and related financing activities	-0-	(2,937,667)	603,269	(2,334,398)
Investing activities	(375,263)	-	-0-	(375,263)
Total	<u>(172,725)</u>	<u>71,909</u>	<u>93,555</u>	<u>(7,261)</u>
<b>Cash and cash equivalents:</b>				
Beginning of year	856,716	2,862,049	10,012	3,728,777
End of year	<u>\$ 683,991</u>	<u>\$ 2,933,958</u>	<u>\$ 103,567</u>	<u>\$ 3,721,516</u>

# HANCOCK REGIONAL HOSPITAL

## NOTES TO COMBINED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

	2015			
	Foundation	HRSC	O3PureMed	Total
<b>Assets</b>				
Current assets	\$ 1,542,706	\$ 4,688,235	\$ 12,119	\$ 6,243,060
Capital assets	11,605	933,844	1,581,426	2,526,875
Assets whose use is limited	4,685,059	-0-	-0-	4,685,059
Total assets	<u>\$ 6,239,370</u>	<u>\$ 5,622,079</u>	<u>\$ 1,593,545</u>	<u>\$ 13,454,994</u>
<b>Liabilities</b>				
Accounts payable and other liabilities	36,596	756,269	4,489	797,354
Total liabilities	<u>36,596</u>	<u>756,269</u>	<u>4,489</u>	<u>797,354</u>
<b>Net position</b>				
Unrestricted	1,506,110	3,931,966	7,630	5,445,706
Net investment in capital assets	11,605	933,844	1,581,426	2,526,875
Donor restricted-expendable	4,685,059	-0-	-0-	4,685,059
Total net position	<u>6,202,774</u>	<u>4,865,810</u>	<u>1,589,056</u>	<u>12,657,640</u>
Total liabilities and net position	<u>\$ 6,239,370</u>	<u>\$ 5,622,079</u>	<u>\$ 1,593,545</u>	<u>\$ 13,454,994</u>
Operating revenues (patient and other)	\$ -0-	\$ 11,132,124	\$ 2,107	\$ 11,134,231
<b>Expenses</b>				
Depreciation	-0-	336,781	162,900	499,681
Other expenses	-0-	8,643,241	338,614	8,981,855
Total expenses	<u>-0-</u>	<u>8,980,022</u>	<u>501,514</u>	<u>9,481,536</u>
Operating income (loss)	-0-	2,152,102	(499,407)	1,652,695
Nonoperating revenues, net	645,575	1,816	-0-	647,391
Capital contributions (distributions)	<u>-0-</u>	<u>(2,440,000)</u>	<u>375,002</u>	<u>(2,064,998)</u>
Change in net position	645,575	(286,082)	(124,405)	235,088
Net position, beginning of year	<u>5,557,199</u>	<u>5,151,892</u>	<u>1,713,461</u>	<u>12,422,552</u>
Net position, end of year	<u>\$ 6,202,774</u>	<u>\$ 4,865,810</u>	<u>\$ 1,589,056</u>	<u>\$ 12,657,640</u>
<b>Net cash flows from</b>				
Operating activities	\$ -0-	\$ 2,488,883	\$ (338,614)	\$ 2,150,269
Noncapital financing activities	927,238	-0-	-0-	927,238
Capital and related financing activities	-0-	(2,704,164)	331,509	(2,372,655)
Investing activities	(593,290)	1,816	-0-	(591,474)
Total	<u>333,948</u>	<u>(213,465)</u>	<u>(7,105)</u>	<u>113,378</u>
<b>Cash and cash equivalents:</b>				
Beginning of year	<u>522,768</u>	<u>3,075,514</u>	<u>17,117</u>	<u>3,615,399</u>
End of year	<u>\$ 856,716</u>	<u>\$ 2,862,049</u>	<u>\$ 10,012</u>	<u>\$ 3,728,777</u>

The separate financial statements for each of the entities above may be obtained through contacting management of HRH.