

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY
HOSPITAL**

March 31, 2005

*CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT
AUDITORS' REPORT*



**Auditor of State
Betty Montgomery**

Board of Governors
Mercer County Joint Township Community Hospital
800 West Main Street
Coldwater, Ohio 45828-1698

We have reviewed the *Independent Auditors' Report* of the Mercer County Joint Township Community Hospital, prepared by VonLehman and Company Inc., for the audit period April 1, 2004 through March 31, 2005. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Mercer County Joint Township Community Hospital is responsible for compliance with these laws and regulations.

A handwritten signature in cursive script that reads "Betty Montgomery".

BETTY MONTGOMERY
Auditor of State

December 15, 2005

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MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Mercer County Joint Township Community Hospital

We have audited the accompanying basic consolidated financial statements of Mercer County Joint Township Community Hospital as of March 31, 2005 and 2004, as listed in the table of contents. These basic 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 U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 Mercer County Joint Township Community Hospital as of March 31, 2005 and 2004, and the results of its operations, and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The Management's Discussion and Analysis is not a required part of the basic financial statements, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with Government Auditing Standards, we have also issued a report dated July 22, 2005, on our consideration of Mercer County Joint Township Community Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audits.

VonLehman and Company Inc.

Fort Mitchell, Kentucky
July 22, 2005

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED MARCH 31, 2005
(UNAUDITED)**

This section of Mercer County Joint Township Community Hospital's (the Hospital) annual financial statements presents background information and management's discussion and analysis (MD&A) of the Hospital's financial performance during the year ended March 31, 2005. This MD&A includes a discussion and analysis of the activities and results of the Hospital.

This MD&A should be read together with the financial statements included in this report.

FINANCIAL HIGHLIGHTS

- The Hospital's net assets increased by \$1.0 million and includes non-operating income of \$72,000 in 2005.
- During the year, the Hospital's net operating revenues increased 8.7% to \$33.9 million while expenses increased 7.0% to \$33.0 million. The result is income from operations of \$979,000, an increase of \$570,000 when compared to 2004 operations.
- During the year, the Hospital made the following significant capital acquisitions and improvements:
 - X-Ray CT Scanner
 - Echocardiography Machine
 - Time and Attendance Software
 - New Signage

The source of funding for these projects was cash flows from operations and long-term debt.

FINANCIAL STATEMENTS

The financial statements of the Hospital present information about the Hospital using financial reporting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information. The statements of net assets include all of the Hospital's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to Hospital creditors (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of the Hospital, and assessing the liquidity and financial flexibility of the Hospital. All of the current year's revenues and expenses are accounted for in the Statements of Revenues, Expenses and Changes in Net Assets. These statements measure the financial results of the Hospital's operations and present revenues earned and expenses incurred. The final financial statement is the Statement of Cash Flows. The primary purpose of this statement is to provide information about the Hospital's cash flows from operating activities, capital and related financing activities, and investing activities, and to provide information on the sources and uses of cash during the year. The notes to the financial statements provide additional information that is essential to a full understanding of the data provided. The notes to the financial statements can be found on pages 8 through 15 of this report.

MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL

FINANCIAL ANALYSIS

The Statements of Net Assets and Revenues, Expenses and Changes in Net Assets report information about the Hospital's net assets and the Hospital's changes in net assets. Increases or decreases in the Hospital's net assets are one indicator of whether the Hospital's financial health is improving or deteriorating. However, other non-financial factors, such as changes in economic conditions, population growth (including uninsured and medically indigent individuals and families), new or changed government legislation and the Hospital's strategic plan should also be considered.

A summary of the Hospital's Statements of Net Assets as of March 31, 2005 and 2004 is presented below (in thousands):

	<u>2005</u>	<u>2004</u>	<u>\$ Change</u>	<u>% Change</u>
Cash and Cash Equivalents	\$ 5,121	\$ 4,818	\$ 303	6.3%
Property, Plant and Equipment, Net	12,505	11,745	760	6.5
Patient Accounts Receivable, Net	6,638	5,552	1,086	19.6
Other Assets	<u>1,363</u>	<u>1,225</u>	<u>138</u>	11.3
Total Assets	<u>\$ 25,627</u>	<u>\$ 23,340</u>	<u>\$ 2,287</u>	
Current Liabilities	\$ 4,326	\$ 3,530	\$ 796	22.5%
Long-Term Debt	<u>596</u>	<u>151</u>	<u>445</u>	294.7
Total Liabilities	4,922	3,681	1241	
Net Assets	<u>20,705</u>	<u>19,659</u>	<u>1,046</u>	5.3%
Total Liabilities and Net Assets	<u>\$ 25,627</u>	<u>\$ 23,340</u>	<u>\$ 2,287</u>	

As can be seen in the above, net assets increased to \$20.7 million in 2005, up from \$19.7 million in 2004.

A summary of the Hospital's Changes in Net Assets for the years ended March 31, 2005 and 2004 is presented below (in thousands):

	<u>2005</u>	<u>2004</u>	<u>\$ Change</u>	<u>% Change</u>
Revenues				
Net Patient Service Revenues	\$ 32,505	\$ 29,977	\$ 2,528	
Other Operating Revenues	<u>1,427</u>	<u>1,235</u>	<u>192</u>	
Total Revenues	<u>33,932</u>	<u>31,212</u>	<u>2,720</u>	8.7%
Expenses				
Nursing Services	7,620	7,291	329	
Medical Professional Services	7,702	7,875	(175)	
General Services	3,056	2,978	78	
Administrative Services	11,938	10,336	1,602	
Provision for Bad Debts	1,279	1,033	246	
Depreciation	<u>1,358</u>	<u>1,289</u>	<u>69</u>	
Total Expenses	<u>32,953</u>	<u>30,802</u>	<u>2,151</u>	7.0%
Income from Operations	979	410	569	
Non-Operating Revenues	72	48	24	
Extraordinary Item	<u>(6)</u>	<u>(474)</u>	<u>468</u>	
Changes in Net Assets	<u>\$ 1,045</u>	<u>\$ (16)</u>	<u>\$ 1,061</u>	

FINANCIAL ANALYSIS (Continued)

Sources of Revenues

During 2005, the Hospital derived substantially all of its revenues from patient services and other related activities. Revenues include, among other items, revenues from the Medicare and Medicaid programs, patients, insurance carriers, preferred provider organizations, and managed care programs.

Payer Mix

The Hospital provides care to patients under payment arrangements with Medicare, Medicaid, and various commercial 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.

OPERATING AND FINANCIAL PERFORMANCE

The Hospital generated significantly more gross revenues from patients in 2005 and the result was a change in net assets of \$1.0 million. This section will discuss highlights of 2005 operations and changes in activity.

Revenues

Net patient service revenues increased \$2.5 million in 2005 primarily due to a 'charge-per-episode' increase, a volume increase and an increase in ancillary services.

Expenses

Total operating expenses increased \$2.2 million in 2005 which was attributed to an increase in personnel costs, costs for other services, costs for supplies and drugs, utilities and bad debt expense.

PROPERTY, PLANT AND EQUIPMENT

During 2005, the Hospital invested \$2.2 million in a broad range of property, plant and equipment which is included in the table below (in thousands):

	<u>2005</u>	<u>2004</u>	<u>\$ Change</u>	<u>% Change</u>
Land	\$ 44	\$ 44	\$ -	
Buildings and Improvements	19,749	19,829	(80)	
Major Movable and Leased Equipment	11,425	10,482	943	
Other	<u>1,246</u>	<u>836</u>	<u>410</u>	
Total Property, Plant and Equipment	32,464	31,191	1,273	4.1%
Less Accumulated Depreciation	<u>19,959</u>	<u>19,446</u>	<u>513</u>	
Property, Plant and Equipment, Net	<u>\$ 12,505</u>	<u>\$ 11,745</u>	<u>\$ 760</u>	6.5%

Property, plant and equipment have increased due to the fact that the Hospital has expanded its patient service capacity to meet the needs of the community. Additionally, the Hospital continues to replace equipment as it becomes obsolete as well as upgrade the capabilities of its information systems.

LONG TERM DEBT

During the year, the Hospital incurred a note payable for the purchase of an X-ray CT Scanner in the amount of \$782,160. Also, the Hospital paid \$145,254 in principal on all outstanding debt during the year.

ECONOMIC FACTORS AND 2005 BUDGET

The Hospital's Board and management considered many factors when setting the 2006 budget. Of primary importance in setting the budget was the status of the economy, which takes into account market focus and other environmental factors such as the following:

- Demographics and impact areas of population growth and the expanding need for services
- Continuously increasing expectations for quality improvement
- Advances in medical equipment technology and the need to replace obsolete equipment
- Privacy legislation – Health Insurance Portability and Accountability Act (HIPAA)
- Increasing emphasis on the integrity of financial information
- Increasing number of uninsured patients
- Increasing cost of medical supplies
- Access to additional capital
- Increasing drug costs

The focus of management is to implement a multi-year plan that will emphasize expanded services to all areas of Mercer County, continuous quality improvement, cost control, capital requirements, and financing in support of net asset improvement.

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
STATEMENTS OF NET ASSETS**

ASSETS

	March 31,	
	2005	2004
Current Assets		
Cash and Cash Equivalents	\$ 459,783	\$ 854,681
Patient Accounts Receivable, Net of Estimated Uncollectibles (2005 - \$745,904; 2004 - \$704,636)	6,638,492	5,552,147
Inventories	754,483	743,846
Prepaid Expenses	262,713	257,512
 Total Current Assets	 8,115,471	 7,408,186
Cash and Cash Equivalents Whose Use is Limited		
Board Designated for Future Capital Purposes	4,661,506	3,963,348
Property, Plant and Equipment, Net	12,505,151	11,745,330
Other Assets	344,757	223,366
 Total Assets	 \$ 25,626,885	 \$ 23,340,230

See accompanying notes.

LIABILITIES AND NET ASSETS

	March 31,	
	<u>2005</u>	<u>2004</u>
Current Liabilities		
Accounts Payable	\$ 1,608,182	\$ 1,152,034
Accrued Expenses	2,523,314	2,334,124
Note Payable - Current	150,941	-
Capital Lease Obligation - Current Portion	<u>44,052</u>	<u>44,052</u>
Total Current Liabilities	4,326,489	3,530,210
Long-Term Liabilities		
Note Payable - Long Term Portion	485,965	-
Capital Lease Obligation - Long Term Portion	<u>109,727</u>	<u>150,535</u>
Total Long-Term Liabilities	595,692	150,535
Total Liabilities	<u>4,922,181</u>	<u>3,680,745</u>
Net Assets		
Unrestricted	8,965,238	8,083,742
Invested in Capital Assets - Net of Related Debt	11,714,466	11,550,743
Temporarily Restricted	<u>25,000</u>	<u>25,000</u>
Total Net Assets	<u>20,704,704</u>	<u>19,659,485</u>
Total Liabilities and Net Assets	<u>\$ 25,626,885</u>	<u>\$ 23,340,230</u>

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**

	Years Ended March 31,			
	2005		2004	
	Amount	Percent	Amount	Percent
Net Patient Service Revenues	\$ 32,504,702	95.8 %	\$ 29,976,513	96.0 %
Other Operating Revenues	<u>1,427,061</u>	<u>4.2</u>	<u>1,234,739</u>	<u>4.0</u>
Total Operating Revenues	<u>33,931,763</u>	<u>100.0 %</u>	<u>31,211,252</u>	<u>100.0 %</u>
Operating Expenses				
Nursing Services	7,619,673	22.5	7,291,253	23.4
Medical Professional Services	7,701,617	22.7	7,874,609	25.2
General Services	3,055,641	9.0	2,978,006	9.5
Administrative Services	11,938,054	35.2	10,336,416	33.1
Depreciation	1,358,353	4.0	1,289,023	4.1
Provision for Bad Debts	<u>1,279,470</u>	<u>3.8</u>	<u>1,032,597</u>	<u>3.3</u>
Total Operating Expenses	<u>32,952,808</u>	<u>97.1</u>	<u>30,801,904</u>	<u>98.6</u>
Income from Operations	<u>978,955</u>	2.9	<u>409,348</u>	1.4
Non-Operating Revenues				
Investment Earnings	47,708	-	27,364	-
Unrestricted Gifts	<u>24,275</u>	<u>-</u>	<u>21,017</u>	<u>-</u>
Total Non-Operating Revenues	<u>71,983</u>	<u>-</u>	<u>48,381</u>	<u>-</u>
Change in Net Assets Before Extraordinary Item	1,050,938	2.9 %	457,729	1.4 %
Extraordinary Item - Losses from Flood and Related Damages, Net of Insurance Proceeds	<u>(5,719)</u>	<u>-</u>	<u>(474,305)</u>	<u>(1.4)</u>
Change in Net Assets	1,045,219	<u>2.9 %</u>	(16,576)	<u>- %</u>
Net Assets, Beginning of Year	<u>19,659,485</u>		<u>19,676,061</u>	
Net Assets, End of Year	<u>\$ 20,704,704</u>		<u>\$ 19,659,485</u>	

See accompanying notes.

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
STATEMENTS OF CASH FLOWS**

	March 31,	
	<u>2005</u>	<u>2004</u>
Cash Flows from Operating Activities		
Cash Received from Customers	\$ 28,890,168	\$ 29,283,154
Cash Payments to Suppliers for Goods and Services	(15,416,797)	(17,659,093)
Cash Payments to Employees for Services	(13,100,395)	(11,632,953)
Other Operating Revenues	<u>1,427,061</u>	<u>1,234,739</u>
Net Cash Provided by Operating Activities:	<u>1,800,037</u>	<u>1,225,847</u>
Cash Flows from Non-Capital Financing Activities:		
Non-Operating Revenues	71,983	48,381
Extraordinary Item - Losses from Flood and Related Damages, Net of Insurance Proceeds	<u>(5,719)</u>	<u>(474,305)</u>
Net Cash Provided (Used) Provided by Non-Capita Financing Activities:	<u>66,264</u>	<u>(425,924)</u>
Cash Flows from Capital and Related Financing Activities:		
Payments on Notes Payable	(145,254)	-
Payments on Capital Lease Obligation	(40,808)	-
Proceeds from Sale of Property, Plant and Equipment	63,053	4,388
Acquisition of Property, Plant and Equipmen	<u>(1,440,032)</u>	<u>(1,525,189)</u>
Net Cash Used by Capital and Related Financing Activitie	<u>(1,563,041)</u>	<u>(1,520,801)</u>
Net Increase (Decrease) in Cash and Cash Equivalents:	303,260	(720,878)
Cash and Cash Equivalents at Beginning of Year:	<u>4,818,029</u>	<u>5,538,907</u>
Cash and Cash Equivalents at End of Year	<u>\$ 5,121,289</u>	<u>\$ 4,818,029</u>
Recap of Cash and Cash Equivalents		
Undesignated Cash	\$ 434,783	\$ 829,681
Designated Cash	4,661,506	3,963,348
Restricted Cash	<u>25,000</u>	<u>25,000</u>
Total Cash and Cash Equivalents:	<u>5,121,289</u>	<u>4,818,029</u>
Reconciliation of Income from Operations to Net Cash Provided by Operating Activities:		
Income from Operations	\$ 978,955	\$ 409,348
Adjustments to Reconcile Income from Operations to Net Cash Provided by Operating Activities:		
Depreciation	1,358,353	1,289,023
Provision for Bad Debts	1,279,470	1,032,597
Loss on Disposal of Property, Plant and Equipmen	40,965	49,858
Changes in		
Patient Accounts Receivable	(2,365,815)	(1,725,956)
Inventories	(10,637)	(9,431)
Prepaid Expenses and Other Assets	(126,592)	18,965
Accounts Payable	456,148	19,565
Accrued Expenses	<u>189,190</u>	<u>141,878</u>
Total Adjustments	<u>821,082</u>	<u>816,499</u>
Net Cash Provided by Operating Activities:	<u>\$ 1,800,037</u>	<u>\$ 1,225,847</u>
Supplemental Disclosure of Cash Flow Information		
Assets Acquired Under Capital Lease or Note Payable	<u>\$ 782,160</u>	<u>\$ 220,284</u>
Cash Paid for Interest	<u>\$ 25,669</u>	<u>\$ -</u>

See accompanying notes.

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

NOTE 1 – ACCOUNTING POLICIES

Mercer County Joint Township Community Hospital (the Hospital) is a 76-bed facility, located in Mercer County, Ohio and operates under the direction of an eleven member board of governors pursuant to the authority of the Joint Township Hospital Board of Trustees with representatives from Butler, Franklin, Gibson, Granville, Marion, Recovery, Washington and Jefferson Townships. The Medical and Educational Development Foundation (MEDF) Physician Corporation is a not for profit, non-governmental entity. MEDF manages physician practices. The Hospital is deemed to have control over MEDF. The financial statements of MEDF have been consolidated with the Hospital's financial statements. All material intercompany balances and transactions have been eliminated in the consolidation.

Nature of Operations

The Hospital's operations consist almost exclusively of providing healthcare services to the residents of Mercer County, Ohio, and the surrounding area.

Basis of Accounting

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

Accounting Standards

Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that do not conflict with or contradict GASB pronouncements, including those issued after November 30, 1989.

Estimates

The process of preparing financial statements in conformity with U.S. generally accepted accounting principles requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues, and expenses. Certain estimates relate to unsettled transactions and events as of the date of the financial statements. Other estimates relate to assumptions about the ongoing operations and may impact future periods. Accordingly, upon settlement, actual results may differ from estimated amounts.

Cash and Cash Equivalents

Cash and cash equivalents are deposited in financial institutions as authorized and directed by State statutes. All deposits are collateralized by pledged securities of the financial institutions up to or exceeding the value of the deposits, as specified by State statutes.

For cash flow purposes, cash and cash equivalents are defined as those unrestricted and undesignated funds on deposit which have maturities of three months or less.

Cash and Cash Equivalents Whose Use is Limited

Cash and cash equivalents whose use is limited include assets set aside by the Board of Trustees for future capital improvements, over which the Board of Trustees retains control and may at its discretion subsequently use for other purposes.

NOTE 1 – ACCOUNTING POLICIES (Continued)

Inventories

Inventories consist primarily of supplies and drugs and are valued at the lower of cost under the first-in, first-out (FIFO) method, or market.

Property, Plant and Equipment

Property, plant and equipment is recorded at cost or at fair market value at the date received if acquired by gift. It is the Hospital's policy to capitalize acquired property, plant and equipment with a cost or fair market value of \$500 or greater. Expenditures for maintenance and repairs, which do not extend the life of the applicable assets, are charged to expense as incurred. Depreciation is computed using the straight line method over the estimated useful lives of the depreciable assets as follows:

Land Improvements	5 - 20 Years
Buildings and Fixed Equipment	5 - 40 Years
Major Movable Equipment	2 - 20 Years

Compensated Absences

Vacation and sick pay is expensed to operations when earned. Unused and earned benefits are recorded as a current liability in the financial statements.

Net Patient Service Revenues

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare. Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient non-acute services are paid at a prospectively determined rate per day based on clinical, diagnostic and other factors. Outpatient services are reimbursed on a prospective rate scale based on Ambulatory Patient Classifications. Home Health Services are reimbursed on a prospective basis for episodes of care spanning 60 days. There are exceptions which could adjust the 60-day payment period. The payment rates are based on a clinical assessment system called OASIS (the Outcome and Assessment Information Set). Final settlements are determined upon submission of the annual cost report by the Hospital and audits thereof by the Medicare Fiscal Intermediary.

Medicaid. Inpatient services rendered to Medicaid program beneficiaries are reimbursed on a rate per discharge basis. Outpatient services rendered to Medicaid program beneficiaries are reimbursed on a fee schedule basis. Inpatient capital costs are reimbursed at a tentative rate with a final settlement to be determined after submission of the annual cost report by the Hospital and audits thereof by the State Medicaid Agency.

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.

NOTE 1 – ACCOUNTING POLICIES (Continued)

Reclassifications

Certain amounts in the prior year financial statements have been reclassified for comparative purposes to conform with the presentation in the current year financial statements.

Charity Care

The Hospital provides care to patients who meet 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 determined to qualify as charity care, they are not reported as revenues.

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 illness; 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.

NOTE 2 – CASH AND CASH EQUIVALENTS

Legal Requirements

State statutes require the classification of monies held by the Hospital into three categories:

Category 1 consists of "active" monies, those monies required to be kept in a "cash" or "near-cash" status for current demands. Such monies must be maintained either as cash or in depository accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts.

Category 2 consists of "inactive" monies, those monies not required for use within the current two year period of designation of depositories. Inactive monies may be deposited or invested only as certificates of deposit maturing no later than the end of the current period of designation of depositories.

Category 3 consists of "interim" monies; those monies which are not needed for immediate use, but will be needed before the end of the current period. Interim monies may be invested or deposited in the following securities:

Bonds, notes, or other obligations of or guaranteed by the United States, or those for which the full faith and credit of the United States is pledged for the payment of principal and interest;

Bonds, notes, debentures, or other obligations or securities issued by a federal government agency or instrumentality. The securities fall into three categories: obligations of the federal government, federal agencies, and federal instruments;

Time certificates of deposit or savings or deposit accounts, including, but not limited to passbook accounts in any eligible institution mentioned in Section 135.32 of the Ohio Revised Code having an office located within the territorial limits of the county;

Bonds or other obligations of the State of Ohio, its political subdivisions, or other units or agencies of this state or its political subdivisions;

NOTE 2 – CASH AND CASH EQUIVALENTS (Continued)

Effective October 7, 1993, no load money market funds consisting exclusively of obligations described as "active" and "inactive" monies above, and repurchase agreements secured by such obligations so long as they are made through eligible institutions mentioned in Section 135.32 of the Ohio Revised Code;

The State Treasurer's investment pool.

The investing authority may also enter into a written repurchase agreement under the terms of which agreement the investing authority purchases and the seller agrees unconditionally to repurchase any of the securities listed in categories 1 and 2 above. He also may sell any of such securities owned by the county under the same terms and conditions for repurchase.

The Governmental Accounting Standards Board has established risk categories for deposits as follows:

Insured or collateralized with securities held by the entity or by its agent in the entity's name;

Collateralized with securities held by the pledging financial institution's trust department or agent in the entity's name;

Uncollateralized. (This includes any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the entity's name).

As of March 31, 2005 and 2004, the carrying amount of the Hospital's deposits was \$5,121,289 and \$4,818,029, respectively, and the bank balance was \$5,106,837 and \$5,121,802, respectively. Of the bank balance:

At March 31, 2005 and 2004, \$199,047 and \$200,000, respectively, was covered by federal depository insurance and would belong in the risk category "insured or collateralized"; and

At March 31, 2005 and 2004, \$4,907,790 and \$4,921,802, respectively, was covered by collateral held by third-party trustees pursuant to Section 135.181 of the Ohio Revised Code, in collateral pools securing all public funds on deposit with specific depository institutions, and belongs in the risk category "uncollateralized".

NOTE 3 – THIRD-PARTY SETTLEMENTS AND COMPONENTS OF PATIENT ACCOUNTS RECEIVABLE

In addition to those patients unable to pay, there are patients receiving services who will not pay. The Hospital has established credit and collection policies to hold this cost to a minimum. Provisions for bad debts are recorded as operating expenses on the financial statements.

Estimated third-party settlements for the Medicare and Medicaid programs reflect differences between interim reimbursement and reimbursement as determined by cost reports filed after the end of the year. Such third-party settlements may reflect differences owed to or by the Hospital.

The Hospital's net patient accounts receivable (unsecured) were concentrated in the following major payor classes:

	2005	2004
Federal Government: Medicare	\$ 2,582,074	\$ 1,584,494
State of Ohio:		
Medicaid, Workers Compensation	565,893	313,283
Commercial Insurance, Self-Pay and Other	3,490,525	3,654,370
Total	\$ 6,638,492	\$ 5,552,147

MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL

NOTE 4 – PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment transactions for the year ended March 31, 2005 were as follows:

<u>Business-Type Activities</u>	<u>Balance April 1, 2004</u>	<u>Additions</u>	<u>Transfers/ Disposals</u>	<u>Balance March 31, 2005</u>
Property, Plant and Equipment Not Being Depreciated				
Construction in Progress	\$ 836,400	\$ 410,078	\$ -	\$ 1,246,478
Land	<u>44,300</u>	<u>-</u>	<u>-</u>	<u>44,300</u>
	880,700	410,078	-	1,290,778
Depreciable Property, Plant and Equipment				
Buildings and Improvements	19,829,246	183,171	(263,387)	19,749,030
Major Movable and Leased Equipment	<u>10,481,473</u>	<u>1,628,943</u>	<u>(685,878)</u>	<u>11,424,538</u>
	30,310,719	1,812,114	(949,265)	31,173,568
Total Property, Plant and Equipment at Historical Cost	<u>31,191,419</u>	<u>2,222,192</u>	<u>(949,265)</u>	<u>32,464,346</u>
Less Accumulated Depreciation				
Buildings and Improvements	12,250,266	566,343	(146,259)	12,670,350
Major Movable and Leased Equipment	<u>7,195,823</u>	<u>792,010</u>	<u>(698,988)</u>	<u>7,288,845</u>
Total Accumulated Depreciation	<u>19,446,089</u>	<u>1,358,353</u>	<u>(845,247)</u>	<u>19,959,195</u>
Property, Plant and Equipment – Net	<u>\$ 11,745,330</u>	<u>\$ 863,839</u>	<u>\$ (104,018)</u>	<u>\$ 12,505,151</u>

NOTE 5 – OTHER ASSETS

The Hospital is a member of the West Central Ohio Regional Healthcare Alliance, Ltd. (WCORHA) along with four other area hospitals. Each hospital loaned \$200,000 to WCORHA. The current project of the WCORHA is the operation of a cancer center.

NOTE 6 – LONG-TERM LIABILITIES

The following is a summary of the Hospital's long-term liabilities for the year ended March 31, 2005:

	<u>Notes Payable</u>	<u>Capital Lease Obligation</u>
Outstanding April 1, 2004	\$ -	\$ 194,587
Additions of New Debt	782,160	-
Repayments	<u>(145,254)</u>	<u>(40,808)</u>
Outstanding March 31, 2005	<u>\$ 636,906</u>	<u>\$ 153,779</u>
Amount Expected to be Paid Within One Year	<u>\$ 150,941</u>	<u>\$ 44,052</u>

NOTE 6 – LONG-TERM LIABILITIES (Continued)

Note Payable

	March 31,	
	2005	2004
<p>The Hospital has a note payable to a bank that funded the purchase of an X-Ray CT Scanner. The note charges interest at 4%. Monthly principal and interest payments are \$14,242 and the final payment is due in April 2009. The note is collateralized by the equipment purchased with the note proceeds.</p>	\$ <u>636,906</u>	\$ <u>-</u>

Capital Lease Obligation

The Hospital leases certain equipment under non-cancelable capital lease obligations. The following are the net minimum future lease payments for the lease:

	March 31,	
	2005	2004
2006	\$ 44,052	
2007	44,052	
2008	44,052	
2009	21,623	
Total Net Future Minimum Lease Payments	\$ 153,779	\$ 194,587
Less: Amount Representing Interest	-	-
Total Capital Lease Obligations	153,779	194,587
Less: Current Portion	44,052	44,052
Long-Term Capital Lease Obligations	\$ <u>109,727</u>	\$ <u>150,535</u>

Net book value of leased equipment included within Property, Plant and Equipment, was as follows:

Cost	\$ 220,284	\$ 220,284
Accumulated Depreciation	66,085	22,028
Net Book Value	\$ <u>154,199</u>	\$ <u>198,256</u>

NOTE 7 – OPERATING LEASES

The Hospital has entered into lease agreements for certain buildings and office equipment under operating lease terms. The following are the net future minimum lease payments for these leases:

2006	\$ 70,370
2007	65,930
2008	62,380
2009	10,095
Total	\$ <u>208,775</u>

Total rental expense for operating leases, including those with terms of one month or less, for the years ended March 31, 2005 and 2004 was \$136,526 and \$143,596, respectively, and were included within Other Expenses on the Statements of Operations.

NOTE 8 – PENSION PLAN

The Hospital participates in a state pension plan, the Ohio Public Employees Retirement System (OPERS), which covers substantially all employees.

The OPERS plan is a cost sharing, multiple employer, defined benefit, public employee retirement plan. It provides retirement, disability benefits, annual cost of living adjustments, healthcare benefits and death benefits to plan members and beneficiaries. Benefits provided under the plan are established by State Statute.

The plan issues a separate, publicly available financial report that includes a balance sheet and required supplementary information. This report may be obtained by contacting: Ohio Public Employees Retirement System, 277 East Town Street, Columbus, Ohio 42315, Telephone 1-800-222-7377.

The Ohio Revised Code provides OPERS statutory authority for employer and employee contributions. The required, actuarially-determined contribution rates for the Hospital and for the employee are 13.55% and 8.5%, respectively. The Hospital's contributions, representing 100% of employer contributions, for the last three years were as follows:

<u>Year</u>	<u>Contribution</u>
2005	\$1,627,497
2004	1,519,960
2003	1,567,940

NOTE 9 – POSTEMPLOYMENT HEALTHCARE BENEFITS

In addition to the pension benefits described above, OPERS also provides post-retirement health care coverage, commonly referred to as OPEB (Other Post-Employment Benefits). The Ohio Revised Code provides the authority for public employers to fund post-retirement health care through their contributions.

OPERS provides post-retirement health care coverage to age and service retirees and dependents with 10 or more years of qualifying Ohio service credit. Health care coverage for disability recipients and primary survivor recipients is available. The 2004 employer rate for employees' coverage by OPERS was 13.55%, of which 4.0% was used to fund health care. The total Hospital contribution used to fund health care was \$500,768 and \$448,697 for the years ended March 31, 2005 and 2004, respectively.

OPEB are financed through employer contributions and investment earnings thereon. The contributions allocated to retiree health care, along with investment income on allocated assets and periodic adjustments in health care provisions, are expected to be sufficient to sustain the program indefinitely.

OPEB are advanced-funded on an actuarially-determined basis. The number of active contributing participants at December 31, 2004 was 369,885. The actuarial value of the net assets available for OPEB at the most recent actuarial review performed December 31, 2003 was \$10,500,000,000. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$26,900,000,000 and \$16,400,000,000 respectively, as of December 31, 2003. The actuarial assumptions used to calculate these amounts are as follows:

- Funding Method – An entry age normal actuarial cost method of valuation is used in determining the present value of OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of unfunded actuarial accrued liability.
- Assets Valuation Method – All investments are carried at market value. For actuarial valuation purposes, a smoothed market approach is used. Under this approach assets are adjusted annually to reflect 25% of unrealized market appreciation or depreciation on

investment assets.

NOTE 9 – POSTEMPLOYMENT HEALTHCARE BENEFITS (Continued)

- Investment Return – The investment assumption rate for 2003 was 8.00%.
- Active Employee Total Payroll – An annual increase of 4.00% compounded annually is the base portion of the individual pay increase assumption. This assumes no change in the number of active employees. Additionally, annual pay increases, over and above the 4.0% base increase, were assumed to range from 0.50% to 6.30%.
- Health Care – Health care costs were assumed to increase 4.0% annually.

NOTE 10 – MALPRACTICE INSURANCE

As of March 31, 2005, the Hospital carried occurrence basis malpractice insurance coverage of \$1,000,000 per claim and \$3,000,000 aggregate, plus excess liability coverage of \$3,000,000.

NOTE 11 – CONCENTRATIONS

Medicare and Medicaid accounted for approximately 38% and 37% of the Hospital's net patient service revenue during the years ended March 31, 2005 and 2004, respectively.

OTHER INFORMATION



**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED
ON AN AUDIT PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Trustees
Mercer County Joint Township Community Hospital

We have audited the basic financial statements of Mercer County Joint Township Community Hospital as of and for the year ended March 31, 2005, and have issued our report thereon dated July 22, 2005. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered Mercer County Joint Township Community Hospital's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance

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

This report is intended solely for the information and use of the board of trustees, management, and the Auditor of the State of Ohio and is not intended to be and should not be used by anyone other than these specified parties.

VonLehman and Company Inc.

Fort Mitchell, Kentucky
July 22, 2005

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
NONCOMPLIANCE CITATIONS - OHIO REVISED CODE
YEAR ENDED MARCH 31, 2005**

NONE

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
STATUS OF PRIOR AUDIT CITATIONS AND RECOMMENDATIONS**

NONE



**Auditor of State
Betty Montgomery**

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800-282-0370
Facsimile 614-466-4490

**MERCER COUNTY JOINT TOWNSHIP COMMUNITY HOSPITAL
MERCER COUNTY**

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
DECEMBER 30, 2005**