

ADAMS COUNTY HOSPITAL

FINANCIAL STATEMENTS

DECEMBER 31, 2006 AND 2005



Mary Taylor, CPA
Auditor of State

Board of Governors
Adams County Hospital
210 North Wilson Drive
West Union, Ohio 45693

We have reviewed the *Report of Independent Auditors* of the Adams County Hospital, Adams County, prepared by Blue & Co., LLC, for the audit period January 1, 2006 through December 31, 2006. 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 Adams County Hospital is responsible for compliance with these laws and regulations.

Mary Taylor

Mary Taylor, CPA
Auditor of State

May 21, 2007

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ADAMS COUNTY HOSPITAL

TABLE OF CONTENTS DECEMBER 31, 2006 AND 2005

	Page
Report of Independent Auditors	1
Required Supplementary Information	
Management's Discussion and Analysis (unaudited).....	i-vi
Financial Statements	
Balance Sheets.....	3
Statements of Operations and Changes in Net Assets.....	5
Statements of Cash Flows.....	6
Notes to Financial Statements.....	7
Other Information	
Report on Internal Control Over Financial Reporting And on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards.....	20
Schedule of Findings and Responses.....	22



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REPORT OF INDEPENDENT AUDITORS

Board of Trustees
ADAMS COUNTY HOSPITAL
West Union, Ohio

We have audited the accompanying balance sheet of Adams County Hospital, a component unit of Adams County, Ohio, as of December 31, 2006, and the related statement of operations and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements as of December 31, 2005 were audited by other auditors whose report dated March 10, 2006, expressed an unqualified opinion.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 audit provides 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 Adams County Hospital as of December 31, 2006 and the results of its operations, changes in net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Board of Trustees
ADAMS COUNTY HOSPITAL

Management's Discussion and Analysis on pages I through vi is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the 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 our report dated March 30, 2007, on our consideration of Adams County 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 read in conjunction with this report when considering the results of our audit.

Blue & Co., LLC

March 30, 2007

Adams County Hospital

A Component Unit of Adams County Hospital, State of Ohio
Management's Discussion and Analysis

The discussion and analysis of Adams County Hospital (the Hospital) financial performance provides an overview of the Hospital's financial activities for the fiscal years ended December 31, 2006 and 2005. Please read it in conjunction with the Hospital's financial statements, which begin on page 3.

Financial Highlights

- The Hospital's net assets increased approximately \$343,000 and \$1,700,000 in 2006 and 2005, respectively.
- During the year, the Hospital's operating revenues increased 5% to approximately \$20,600,000 while expenses increased 12.1% to \$21,325,000. The result is a loss from operations of approximately \$719,000 compared to \$597,000 in operating income in 2005.
- Significant capital acquisitions included a new hospital facility (to be completed in 2007), MRI and computer network equipment. Funding for these projects included cash flow from operations and prior-year bond issue proceeds.

Using This Annual Report

The Hospital's financial statements consist of three statements—a Balance Sheet; a Statement of Operations and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Hospital.

The Balance Sheet and Statement of Operations and Changes in Net Assets

The 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 Assets report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net assets and related changes. You can think of the Hospital's net assets—the difference between assets and liabilities—as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether 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.

Adams County Hospital

A Component Unit of Adams County Hospital, State of Ohio
Management's Discussion and Analysis

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 capital and related 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?"

Net Assets

Net assets increased by \$343,000 in 2006, as you can see in Table 1.

Table 1: Assets, Liabilities, and Net Assets (in thousands)

	<u>2006</u>	<u>2005</u>	<u>\$ change</u>
Assets			
Cash and cash equivalents	\$ 20,420	\$ 31,070	\$ (10,650)
Capital assets	16,643	5,397	11,246
Patient accounts receivable, net	3,486	3,499	(13)
Other assets	767	263	504
Total assets	<u>\$ 41,317</u>	<u>\$ 40,229</u>	<u>\$ 1,088</u>
Liabilities			
Current liabilities	\$ 2,814	\$ 2,712	\$ 102
Long - term obligations	<u>28,129</u>	<u>27,485</u>	<u>644</u>
Total liabilities	30,942	30,197	745
Net assets	<u>10,375</u>	<u>10,032</u>	<u>343</u>
Total liabilities and net assets	<u>\$ 41,317</u>	<u>\$ 40,229</u>	<u>\$ 1,088</u>

As can be seen above, net assets increased to approximately \$10,375,000 in 2006, up from \$10,032,000 in 2005.

Adams County Hospital

A Component Unit of Adams County Hospital, State of Ohio
Management's Discussion and Analysis

A summary of the Hospital's changes in net assets for the years ended December 31, 2006 and 2005 is presented below (in thousands):

	2006	2005	\$ change	% change
Operating revenues				
Net patient service revenues	\$ 20,111	\$ 18,976	\$ 1,135	6.0%
Other	494	638	(144)	-22.6%
Total revenue	20,605	19,614	991	5.1%
Operating expenses				
Salaries and benefits	11,454	10,415	1,039	10.0%
Supplies	2,852	2,675	177	6.6%
Purchased services	2,602	2,145	457	21.3%
Other	4,417	3,782	635	16.8%
Total operating expenses	21,325	19,017	2,308	12.1%
Income (loss) from operations	(719)	597	(1,316)	
Non operating revenue	1,062	1,101	(39)	
Change in net assets	\$ 343	\$ 1,698	\$ (1,355)	

Sources of Revenue

During 2006 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.

Adams County Hospital

A Component Unit of Adams County Hospital, State of Ohio
Management's Discussion and Analysis

Payer Mix

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.

Operating Gains/Losses

Revenues

The Hospital generated significantly more gross revenues from patients in 2006. Net patient service revenues increased approximately \$1,135,000 in 2006 primarily due to volume increases and the operating of the Winchester Family Medicine practice.

Expenses

Total operating expenses increased approximately \$2,308,000 or 12.1% in 2006 which was attributable to an increase in personnel costs, costs from purchased and contracted services, costs for supplies and drugs and utilities and other expense.

Adams County Hospital

A Component Unit of Adams County Hospital, State of Ohio
Management's Discussion and Analysis

PROPERTY, PLANT AND EQUIPMENT

During 2006, the Hospital invested \$12.1 million in a broad range of property, plant and equipment which is included in the table below (in thousands):

	<u>2006</u>	<u>2005</u>
Land improvements	\$ 299	\$ 299
Buildings and fixed equipment	21,714	11,859
Major moveable and leased equipment	<u>7,616</u>	<u>5,336</u>
Total property, plant and equipment	29,629	17,494
Less accumulated depreciation	<u>12,986</u>	<u>12,097</u>
Capital assets, net	<u>\$ 16,643</u>	<u>\$ 5,397</u>

Property, plant, and equipment have increased because the Hospital has expanded its patient service capacity to meet the needs of the community. Also, there was a bond issuance in 2005 for \$27,480,000. The proceeds are being utilized for the building of a new hospital in Seaman, Ohio. Approximately \$10.3 million has been incurred relating to this new hospital. Additionally, the Hospital continues to replace equipment as it becomes obsolete as well as upgrading the capabilities of its information system.

Adams County Hospital

A Component Unit of Adams County Hospital, State of Ohio
Management's Discussion and Analysis

DEBT

At December 31, 2006, the Hospital had \$27,480,000 in outstanding Hospital Facility Improvement Bonds, the entire amount of which was issued in 2005. All but \$340,000 of this debt is long-term.

Other existing debt as of December 31, 2006 is approximately \$1,306,000, of which approximately \$391,000 is payable in 2007. This debt consists of capital lease obligations.

ECONOMIC FACTORS AND 2007 BUDGET

The Hospital's Board and management considered many factors when setting the 2007 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:

- The new Hospital facility in Seaman, Ohio and its impact on the Hospital's patient volume and demographics, as well as its results of operations.
- Debt management and covenants related to bonded debt
- Demographics and impact areas of population growth and the expanding need for services
- Continuously increasing expectations of quality improvements
- 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 Adams County, continuous quality improvement, cost control, capital requirements, and financing in support of net assets improvement.

ADAMS COUNTY HOSPITAL

BALANCE SHEETS DECEMBER 31, 2006 AND 2005

ASSETS

	<u>2006</u>	<u>2005</u>
Current assets		
Cash and cash equivalents	\$ 3,088,678	\$ 4,079,110
Patient accounts receivable, net of allowance for doubtful accounts of approximately \$766,322 and \$596,787 in 2006 and 2005, respectively	3,486,109	3,498,664
Inventories	225,830	233,088
Estimated third party settlements	236,237	-
Prepaid expenses and other current assets	55,254	30,992
Total current assets	<u>7,092,108</u>	<u>7,841,854</u>
Asset whose use is limited		
Board designated for future capital purposes	485,589	485,820
Capital assets, net	16,643,303	5,396,657
Note receivable	250,000	-
Restricted cash - bond issuance	<u>16,846,104</u>	<u>26,504,880</u>
Total assets	<u>\$ 41,317,104</u>	<u>\$ 40,229,211</u>

See accompanying notes to financial statements.

ADAMS COUNTY HOSPITAL

BALANCE SHEETS
DECEMBER 31, 2006 AND 2005

LIABILITIES AND NET ASSETS

	<u>2006</u>	<u>2005</u>
Current liabilities		
Accounts payable	\$ 410,260	\$ 481,285
Estimated third-party settlements	-	879,065
Accrued expenses	1,745,018	1,286,640
Current portion of bonds payable	340,000	-
Current portion of capital lease obligations	318,235	18,731
Current portion of notes payable	-	46,789
Total current liabilities	<u>2,813,513</u>	<u>2,712,510</u>
Long-term liabilities		
Bonds payable	27,140,000	27,480,000
Capital lease obligations	988,589	4,837
Total long-term liabilities	<u>28,128,589</u>	<u>27,484,837</u>
Total liabilities	30,942,102	30,197,347
Net assets		
Invested in capital assets, net of related debt	4,702,583	4,351,180
Unrestricted	5,544,478	5,524,946
Restricted by donors	<u>127,941</u>	<u>155,738</u>
Total net assets	<u>10,375,002</u>	<u>10,031,864</u>
Total liabilities and net assets	<u>\$ 41,317,104</u>	<u>\$ 40,229,211</u>

See accompanying notes to financial statements.

ADAMS COUNTY HOSPITAL

STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
Operating revenues		
Net patient service revenue	\$ 20,111,445	\$ 18,975,986
Operating grants and other revenues	493,885	638,210
Total operating revenues	20,605,330	19,614,196
Operating expenses		
Salaries and benefits	11,453,660	10,415,109
Medical professional fees	1,046,001	994,820
Supplies	2,851,739	2,674,698
Purchased services	2,602,169	2,144,524
Equipment rentals	172,228	276,678
Repairs and maintenance	553,354	402,223
Utilities	561,716	582,237
Depreciation	1,006,085	681,500
Other	1,077,083	845,141
Total operating expenses	21,324,035	19,016,930
Income (loss) from operations	(718,705)	597,266
Sales tax levy and other non-operating revenue	1,061,843	1,100,786
Change in net assets	343,138	1,698,052
Net assets beginning of year	10,031,864	8,333,812
Net assets, end of year	\$ 10,375,002	\$ 10,031,864

See accompanying notes to financial statements.

ADAMS COUNTY HOSPITAL
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
Operating activities		
Cash received from customers	\$ 19,008,698	\$ 19,974,098
Cash paid to vendors for goods and services	(8,448,728)	(8,701,523)
Cash paid to employees for wages and benefits	(11,488,625)	(10,354,508)
Other operating activities	493,885	676,710
Net cash from operating activities	<u>(434,770)</u>	<u>1,594,777</u>
Cash flow from non-capital financing activities		
Non-operating revenues	811,843	1,100,786
Cash flow from capital and related financing activities		
Acquisition of property and equipment	(10,740,728)	(3,718,293)
Proceeds from long-term debt	-	27,480,000
Principal paid on long-term debt	(285,784)	(237,749)
Net cash from capital and related financing activities	<u>(11,026,512)</u>	<u>23,523,958</u>
Net change in cash and cash equivalents	(10,649,439)	26,219,521
Cash and cash equivalents		
Beginning of year	31,069,810	4,850,289
End of year	<u>\$ 20,420,371</u>	<u>\$ 31,069,810</u>
Recap of cash and cash equivalents		
Undesignated Cash	\$ 2,959,737	\$ 3,923,372
Designated Cash	485,589	485,820
Restricted cash - bond issuance	16,846,104	26,504,880
Other restricted cash	128,941	155,738
Total cash and cash equivalents	<u>\$ 20,420,371</u>	<u>\$ 31,069,810</u>
Reconciliation of operating income to net cash from operating activities		
Operating income (loss)	\$ (718,705)	\$ 597,266
Adjustment to reconcile operating income (loss) to net cash from operating activities		
Depreciation	1,006,085	681,500
Bad debts	2,436,929	1,969,285
Loss on disposal of capital assets	10,248	-
Changes in assets and liabilities		
Patient accounts receivable	(2,424,374)	(2,696,702)
Rural Health Collaborative Grant Receivable	-	38,500
Inventories	7,258	(41,974)
Prepaid expenses and other current assets	(24,262)	5,978
Accounts payable	(71,025)	85,596
Accrued expenses	458,378	283,051
Estimated third-party settlements	(1,115,302)	672,277
Net cash from operating activities	<u>\$ (434,770)</u>	<u>\$ 1,594,777</u>

Supplemental disclosure of non-cash capital and related financing activity:

The Hospital entered into capital leases totaling \$1,522,251 in 2006.

The Hospital exchanged certain assets for a note receivable of \$250,000 in 2006.

See accompanying notes to financial statements.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

1. NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Organization and Reporting Entity

Adams County Hospital (the Hospital) is a 25-bed facility, located in Adams County, Ohio and operated by a Board of Trustees as provided for under Ohio Revised Code Section 339. The board of trustees, appointed by Adams County judges and commissioners, is charged with the management and operation of the Hospital, its finances and staff. The Hospital is considered a component unit of Adams County, Ohio, and is included as a component unit in the general-purpose financial statements of Adams County.

The Hospital's operations consist of providing healthcare services to the residents of Adams 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 revenue and expenses are subject to accrual. 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 issues after November 30, 1989.

Other activities that result in gains or losses unrelated to the Hospital's primary mission are considered to be non-operating. Non-operating gains and losses include proceeds from the sales tax levy, unrestricted contributions, interest earnings on investments and gains and losses from sale of assets.

Use of Estimates

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

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

Cash and Cash Equivalents

The Hospital considers cash and cash equivalents as those funds on deposit which mature in three months or less.

Inventories

Inventories are valued at the lower of cost or market as determined by the first-in, first-out (FIFO) method.

Assets Whose Use is Limited

Assets whose use is limited represent cash and cash equivalents 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.

Property, Plant and Equipment

Property, plant and equipment are reported on the basis of 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 \$5,000. Expenditures for maintenance and repairs, which do not extend the useful lives of the applicable assets, are charged to expenses as incurred. Depreciation is computed using the straight-line method over the expected useful lives of depreciable assets. Equipment under capital leases are amortized using the straight-line method over the lessor of the lease term or the estimated useful life of the equipment. The estimated useful lives are as follows:

Land improvements	5 - 20 years
Building and fixed equipment	5 - 40 years
Major movable equipment	2 - 20 years
Leased equipment	3- 15 years

Restricted Cash – Bond Issuance

Restricted cash-bond issuance includes assets in separate cash accounts restricted for payments related to the new Adams County Hospital facility in Seaman, Ohio.

Reclassifications

Certain 2005 accounts have been reclassified to conform to the 2006 presentation.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

Lease agreements

The liability for lease obligations which are in substance installment purchases have been recorded in the financial statements and the leased equipment capitalized as capital assets. The assets and liabilities under capital lease obligations are recorded at the lower of the present value of the minimum lease payments or the fair value of the assets. Depreciation of capital leases is included in depreciation expense on the statements of operations and changes in net assets. Annual rentals pertaining to leases which convey merely the right to use property are charged to current operations.

Compensated absences

The Hospital's employees earn vacation days at varying rates depending on years of service. Employees also earn sick leave benefits based on varying rates depending on years of service.

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.

Net Patient Service Revenue

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 payment 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.

Operating Revenues

For purposes of these financial statements, operating revenues are those revenues generated by the Hospital for healthcare services rendered, grants received, or any other activity related to the Hospital's primary purpose as previously noted in Note 1.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

Third-Party Payors

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 and Medicaid

The Hospital is a provider of services under the Medicare and Medicaid programs. The Hospital is designated as a critical access facility by the Medicare program. As a result, Medicare inpatient and outpatient services are reimbursed at 101% of the cost of providing those services. Payment for a majority of Medicaid inpatient and outpatient services is based on a prospectively determined amount.

Other Payors

The Hospital has entered into agreements with certain commercial carriers. Reimbursement for services under these agreements includes discounts from established charges and other payment methodologies.

Gross patient service revenue and the allowances to reconcile to net patient service revenue for the years ended December 31, 2006 and 2005, are as follows:

	<u>2006</u>	<u>2005</u>
Gross patient service revenue	\$ 39,900,387	\$ 36,226,601
less:		
Third party allowances	17,174,838	15,137,003
Charity care	177,175	144,327
Bad debts	2,436,929	1,969,285
Net patient service revenue	<u>\$ 20,111,445</u>	<u>\$ 18,975,986</u>

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. Charges excluded from revenue under the Hospital's charity care policy for patients unable to pay were \$177,175 and \$144,327 for 2006 and 2005, respectively.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

Restricted Resources

It is the Hospital's policy to first apply unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available. Restricted resources are used only after unrestricted resources have been depleted.

2. DEPOSITS

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).

At year end, the carrying amount of the Hospital's deposits was \$20,420,371 and the bank balance was \$20,743,523. Of the bank balance \$300,000 was covered by federal depository insurance and would belong in the risk category "insured or collateralized"; and \$20,443,523 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".

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 – The Hospital may invest in United States obligations or any other obligation guaranteed by the United States; bonds, notes or any other obligations or securities issued by any federal government or instrumentality; time certificate of deposit or savings or deposit accounts, including passbook accounts, in any eligible institution mentioned in Section 135.32; bonds and other obligations of the State of Ohio or the political subdivisions of the state provided that such political subdivisions are located wholly or partly within the same county; and certain no load money market mutual funds; certain commercial paper; and certain repurchase agreements.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

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.

3. THIRD-PARTY SETTLEMENTS AND COMPONENTS OF PATIENT ACCOUNTS RECEIVABLE

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 each year. Such third-party settlements reflect differences owed to or by the Hospital. The years 2003 and thereafter remain unsettled at December 31, 2006 for Medicaid. The years 2005 and 2006 remain unsettled at December 31, 2006 for Medicare.

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

	December 31	
	2006	2005
Medicare	34%	41%
Medicaid	16%	15%
Commercial and other	20%	19%
Self-pay	30%	25%
	<u>100%</u>	<u>100%</u>

4. CAPITALIZED INTEREST

The hospital follows the policy of capitalizing interest as a component of the cost of capital assets constructed for its own use. In 2006, total interest incurred was \$1,241,278, of which \$85,904 was charged to non-operating activities. In accordance with Financial Accounting Standards Board (FASB) guidelines, interest income earned by the Hospital related to this was netted with the interest expense capitalized.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

5. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2006:

	12/31/05	Additions	Transfers/ Disposals	12/31/06
Property, plant and equipment				
Construction in progress	\$ 3,107,911	\$ 10,362,202	\$ 614,948	\$ 12,855,165
Depreciation property, plant and equipment				
Land improvements	\$ 298,786	\$ -	\$ -	\$ 298,786
Buildings	3,818,532	-	-	3,818,532
Fixed equipment	4,932,856	107,309	-	5,040,165
Major moveable equipment	3,910,634	271,217	(487,317)	4,669,168
Leased equipment	1,425,681	1,522,251	-	2,947,932
Total capital assets	<u>14,386,489</u>	<u>1,900,777</u>	<u>(487,317)</u>	<u>\$ 16,774,583</u>
Less accumulated depreciation				
Land improvements	279,174	12,825	-	291,999
Buildings	3,332,944	65,236	-	3,398,180
Fixed equipment	3,680,343	472,284	-	4,152,627
Major moveable equipment	3,523,334	212,490	(117,383)	3,618,441
Leased equipment	1,281,948	243,250	-	1,525,198
Total accumulated depreciation	<u>12,097,743</u>	<u>1,006,085</u>	<u>(117,383)</u>	<u>12,986,445</u>
Capital assets, net	<u>\$ 5,396,657</u>	<u>\$ 11,256,894</u>	<u>\$ 10,248</u>	<u>\$ 16,643,303</u>

Capital asset activity for the year ended December 31, 2005:

	12/31/04	Additions	Transfers/ Disposals	12/31/05
Property, plant and equipment				
Construction in progress	\$ 52,152	\$ 3,055,759	\$ -	\$ 3,107,911
Depreciation property, plant and equipment				
Land improvements	\$ 298,786	\$ -	\$ -	298,786
Buildings	3,668,656	149,876	-	3,818,532
Fixed equipment	4,770,061	163,102	307	4,932,856
Major moveable equipment	3,695,187	349,556	134,109	3,910,634
Leased equipment	1,425,681	-	-	1,425,681
Total capital assets	<u>\$ 13,858,371</u>	<u>\$ 662,534</u>	<u>\$ 134,416</u>	<u>\$ 14,386,489</u>
Less accumulated depreciation				
Land improvements	266,348	12,826	-	279,174
Buildings	3,263,472	69,472	-	3,332,944
Fixed equipment	3,217,159	463,491	307	3,680,343
Major moveable equipment	3,521,732	135,711	134,109	3,523,334
Leased equipment	1,281,948	-	-	1,281,948
Total accumulated depreciation	<u>11,550,659</u>	<u>681,500</u>	<u>134,416</u>	<u>12,097,743</u>
Capital assets, net	<u>\$ 2,359,864</u>	<u>\$ 3,036,793</u>	<u>\$ -</u>	<u>\$ 5,396,657</u>

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

6. LONG-TERM DEBT

The following is a summary of the Hospital's long-term debt:

	December 31, 2006		
	Bond payable	Note payable	Capital lease
Debt outstanding December 31, 2005	\$ 27,480,000	\$ 46,789	\$ 23,568
Additions of new debt	-	-	1,522,251
Repayments	-	46,789	238,995
Debt outstanding December 31, 2006	\$ 27,480,000	\$ -	\$ 1,306,824
Expected to be paid within one year	\$ 340,000	\$ -	\$ 318,235
	December 31, 2005		
	Bond payable	Note payable	Capital lease
Debt outstanding January 1, 2004	\$ -	\$ 95,742	\$ 212,364
Additions of new debt	27,480,000	-	-
Repayments	-	48,953	188,796
Debt outstanding December 31, 2005	\$ 27,480,000	\$ 46,789	\$ 23,568
Expected to be paid within one year	\$ -	\$ 46,789	\$ 18,731

Bonds payable

The Hospital is obligated to make payments in amounts sufficient to satisfy debt service requirements on bonds issued in 2005 to construct a new facility in Seaman, Ohio. The bonds are dated July 28, 2005 with an original issue of \$27,480,000. Interest rates range from 5.00% to 6.25%. No principal payments were required in 2006, thus the outstanding balance at December 31, 2006 was \$27,480,000. There are certain covenants associated with this bond payable, all of which were met for the year ended December 31, 2006. Future minimum principal and interest payments follow:

	Principal	Interest	Total
2007	\$ 340,000	\$ 1,755,000	\$ 2,095,000
2008	355,000	1,738,000	2,093,000
2009	375,000	1,818,363	2,193,363
2010	395,000	1,698,738	2,093,738
2011	420,000	1,676,025	2,096,025
2012-2016	2,510,000	7,959,125	10,469,125
2017-2021	3,395,000	7,071,313	10,466,313
2022-2026	4,635,000	5,834,400	10,469,400
2027-2031	6,350,000	4,119,050	10,469,050
2032-2036	8,705,000	1,768,000	10,473,000
Total	\$ 27,480,000	\$ 35,438,014	\$ 62,918,014

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

Capital lease obligations

The Hospital leases certain equipment under capital lease obligations. The following are the net minimum future lease payments under these leases:

	2007	\$ 400,362
	2008	395,472
	2009	321,161
	2010	306,300
	2011	<u>76,488</u>
Total net future minimum lease payments		1,499,783
Less: amount representing interest		<u>192,959</u>
Total capital lease obligations		1,306,824
Less: current portion		<u>318,235</u>
Long-term capital lease obligations		<u><u>\$ 988,589</u></u>

Net book value of lease equipment included within capital assets follows:

	2006	2005
Cost	\$ 2,947,932	\$ 1,425,681
Accumulated depreciation	1,525,198	1,281,748
Net book value	<u><u>\$ 1,422,734</u></u>	<u><u>\$ 143,933</u></u>

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:

	2007	\$ 98,695
	2008	24,203
	2009	20,168
	2010	13,394
	2011	<u>4,203</u>
Total		<u><u>\$ 160,663</u></u>

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

Total rental expense for operating leases, including those with terms of one month or less, for the years ended December 31, 2006 and 2005 was \$141,564 and \$515,234, respectively, and is included within other expenses on the statements of operations and changes in net assets.

8. PENSION PLAN

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

OPERS administers three separate pension plans; The Traditional Pension Plan (TP)- a cost-sharing multiple-employer defined benefit pension plan; the Member-Directed Plan (MD)- a defined contribution plan; and the Combined Plan (CO)- a cost-sharing multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan. OPERS provides retirement, disability, survivor and death benefits, annual cost of living adjustments, and post-retirement healthcare benefits to qualifying members of both the Traditional and Combined Plan; however healthcare benefits are not statutorily guaranteed.

Members of the Member-Directed Plan do not qualify for ancillary benefits, including post-employment health care coverage. Chapter 145 of the Ohio Revised Code assigns authority to establish and amend benefit provisions to the OPERS Board of Trustees.

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 43215, 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 13.70% and 9% respectively. The Hospital's contributions, representing 100% employer contributions, for the last three years are as follows:

Year	Contribution
2006	\$ 1,251,934
2005	1,120,884
2004	1,020,590

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

9. POSTEMPLOYMENT HEALTHCARE BENEFITS

In additions to the pension benefits described in Section 8 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 retirants 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 2006 employer rate for employees' coverage by OPERS was 13.70%, of which 4.5% was used to fund health care. The total Hospital contribution used to fund health care was approximately \$411,000 and \$331,000 for the years ended December 31, 2006 and 2005, 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, 2006 was 369,204. The actuarial value of the net assets available for OPEB at the most recent actuarial review performed December 31, 2005 was approximately \$11.1 billion. The actuarially accrued liability and the unfunded actuarially accrued liability, based on the actuarial cost method used, were approximately \$31.3 billion and \$20.2 billion, respectively, as of December 31, 2005.

The actuarial assumptions used to calculate these amounts are as follows:

- **Funding Method-** An entry age normal actuarial cost method of valuations 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 Valuations Method-** All investments are carried at market value. For actuarial valuations 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.
- **Investment Return-** The investment assumption rate for 2005 was 6.5%.

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

- **Active Employee Total Payroll-** An annual increase of 4.0% 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 .5% to 6.3%.
- **Health Care-** Health care costs were assumed to increase at the projected wage inflation rate plus an additional factor ranging from 0.5% to 6% for the next 9 years. In subsequent years, (10 and beyond) health care costs were assumed to increase at 4.0% (the projected wage inflation rate).

10. MALPRACTICE INSURANCE

As of December 31, 2006, the Hospital carried occurrence basis malpractice insurance coverage of \$1,000,000 per claim and \$3,000,000 aggregate, plus excess liability coverage of \$5,000,000.

11. CONCENTRATIONS

Medicare and Medicaid accounted for approximately 60% and 59% of the Hospital's net patient service revenues during 2006 and 2005, respectively.

12. RESTRICTED FUND BALANCES

Temporarily restricted fund balances are available for the issuance of scholarships, purchase of gifts and for the purchase of medical equipment to be used to treat those with tobacco-related illnesses.

13. COMMITMENTS AND CONTINGENCIES

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

ADAMS COUNTY HOSPITAL

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006 AND 2005

14. FOUNDATION AND CONTRIBUTED LAND

The land on which the new Hospital facility is being constructed is being leased by its current owners to the Adams County Medical Foundation, Inc (the "Foundation"). The Foundation is allowing the Hospital to construct its new facility on the land. The Foundation's lease of the land is for \$1 for the term of the lease. The lease term is indefinite allowing the Foundation time to apply for nonprofit status under Sections 501 (c)(3) under the Internal Revenue Code. Upon approval of nonprofit status the land will be contributed to the Foundation.

The Foundation was formed exclusively for nonprofit charitable, scientific, or educational purposes and was established to provide services exclusively for the benefit of Adams County Hospital and to further the Hospital's goals and services relating to the general health and well-being of the citizens of Adams County, Ohio and surrounding areas.

The Foundation had financial activity of approximately \$5,000 in 2006.

It is anticipated that the Hospital and the Foundation will report under combined financial statements beginning in 2007 when the Foundation has greater financial activity.



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

To the Board of Trustees
 Adams County Hospital
 West Union, Ohio

We have audited the financial statements of Adams County Hospital, as of and for the year ended December 31, 2006, and have issued our report thereon dated March 30, 2007. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Adams County Hospital's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Adams County Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Adams County Hospital's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

We consider the deficiencies described in the accompanying schedule of findings and responses to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 2006-2 and 2006-3 to be material weaknesses.

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

Compliance and Other Matters

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

We noted certain matters that we reported to management of Adams County Hospital in a separate letter dated March 30, 2007.

Adams County Hospital's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit Adams County Hospital's responses and, accordingly, we express no opinion on it.

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 an should not be used by anyone other than those specified parties.

Blue & Co., LLC

March 30, 2007

**Adams County Hospital
Schedule of Findings and Responses
Year Ended December 31, 2006**

2006 – 1: Payroll Approval

During testing of the payroll cycle it was noted that the payroll department does not always receive timecards indicating management review and approval for certain groups of employees. Management asserts that there have been no concerns historically with the completeness and accuracy of submitted timecards; however, the missing approval does not document management's monitoring control activities. We recommend that department managers review and sign off on all submitted timesheets.

Management's Response:

This was addressed with the managers in a recent Department Manager's meeting. Payroll will not be processed without departmental manager's review and signature.

2006 – 2: Controls over non-routine and nonsystematic transactions

Adjustments were necessary to record capital leases and a note receivable which represent non-routine transactions for the Hospital. We recommend that the Hospital implement policies to ensure unusual and non-routine transactions are accounted for in accordance with prescribed accounting principles at the time they occur. If the Hospital has questions concerning these types of transactions during the year we welcome the opportunity to discuss these matters and to assist in addressing them.

Management's Response:

We will consult with the auditors to address non-routine and nonsystematic transactions to ensure that these transactions are addressed during the year and that they are accounted for in accordance with prescribed accounting principles.

2006 – 3: Contractual Allowances – Commercial Payors

The Hospital does not apply an allowance to commercial patient accounts receivable. An audit entry was proposed to allow for commercial accounts. We recommend that the client revise its contractual allowance model to consider commercial accounts in the analysis. This will help ensure that interim reporting is complete and accurate.

Management's Response:

The contractual model will be revised to include commercial accounts as a part of the contractual allowance monitoring.



Mary Taylor, CPA
Auditor of State

ADAMS COUNTY HOSPITAL

ADAMS 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
MAY 31, 2007**