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STATE BOARD OF ACCOUNTS
302 West Washington Street
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INDIANAPOLIS, INDIANA 46204-2769

AUDIT REPORT
OF

HARRISON COUNTY HOSPITAL
A COMPONENT UNIT OF
HARRISON COUNTY, INDIANA

January 1, 2010 to December 31, 2010

FILED
11/21/2011

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HOSPITAL OFFICIALS

Office	Official	Term
Chief Executive Officer	Steven L. Taylor	01-01-10 to 12-31-11
Chief Financial Officer	Jeffrey L. Davis	01-01-10 to 12-31-11
Chairman of the Hospital Board	Paul Martin	01-01-10 to 12-31-11
President of the Board of County Commissioners	James Goldman	01-01-10 to 12-31-11

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INDEPENDENT AUDITOR'S REPORT

TO: THE OFFICIALS OF THE HARRISON COUNTY HOSPITAL, HARRISON COUNTY, INDIANA

We have audited the accompanying basic financial statements of the business-type activities, of the Harrison County Hospital (Hospital) as of and for the year ended December 31, 2010, as listed in the table of contents. 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. We did not audit the financial statements of the Harrison MOB, LLC, which represents 100 percent, of the assets and revenues of the discretely presented component unit. Those financial statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Harrison MOB, LLC, is based on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over reporting. 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 and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Hospital and its discretely presented component unit as of December 31, 2010, and the respective changes in financial position and cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis, as listed in the Table of Contents, is not a required part of the basic financial statements but is supplementary information required by the accounting principles generally accepted in the United States of America. 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.

STATE BOARD OF ACCOUNTS

November 10, 2011

HARRISON COUNTY HOSPITAL

Management Discussion and Analysis (MD&A)

This section of Harrison County Hospital's (HCH) annual financial statements presents background information and management discussion and analysis of the HCH financial performance for the year ended December 31, 2010. HCH reports results on a fiscal year of January 1 to December 31, and any reference to a year in this MD&A indicates the HCH fiscal years. This MD&A does not include a discussion and analysis of the activities and results of the Harrison County Hospital Foundation or the Harrison MOB LLC.

This MD&A should be read together with the financial statements and accompanying Notes to the Financial Statements included in this report.

Financial Highlights

- HCH net assets increased by $4,464,739 in 2010, resulting from an operating loss of ($2,862,851), net non-operating items of ($672,410), and contributed capital of $8,000,000 from Harrison County.

- Total net patient revenue, net of provision for bad debt, decreased by 4.3%, while operating expenses decreased by 1.7%.

- Long term debt, including current maturities, is $28,155,000 at December 31, 2010. This amount represents revenue bonds payable for the new hospital construction. Payments related to the long term debt in 2010 consisted of principal of $675,000 and interest of $1,214,263. In December 2010 Harrison County pledged $8 million to HCH for the reduction of long term debt. HCH will use at least a matching amount of $8 million from cash reserves for debt reduction and restructuring that will take place in 2011. More information on the debt restructuring and long term debt is presented in the Notes to the Financial Statements.

- In 2006 HCH entered into an agreement with several physicians and healthcare providers to establish Harrison MOB, LLC. This entity was formed to invest in and operate a new medical office building to be located on the campus of the new HCH facility. HCH has invested $1,157,420 which includes ownership of approximately 58% of the shares of the LLC. Harrison MOB, LLC is a discrete component unit of HCH, and the financial statements of this unit are presented in a separate independent audit report.

- In 2008 the Harrison County Commissioners and the Board of Trustees formed an agreement to construct an ambulance station on the hospital campus, which replaces the ambulance station on the vacated hospital campus. The building is an asset of the hospital, and was substantially completed in July 2010. The total cost of the building was approximately $1.1 million, with Harrison County contributing capital equaling 68% of the cost and HCH contributing the balance.

- HCH continues to upgrade and expand hospital and physician practice information systems. Current projects in the planning and implementation stages include the enhancement and extension of electronic health records systems, which are intended to improve the portability of health information. This is a significant investment in technology which improves quality of information for clinical and financial management, which in turn will facilitate improved quality of care. The enhanced information systems will also allow for operational efficiencies as patient volumes increase, will be vital in conforming to regulatory requirements, and may allow HCH to qualify for government incentive payments in the future.

- Recruiting and retaining a core group of physicians has been part of the strategic plan of HCH for many years. In recent years HCH has entered into employment arrangements with a growing number of physicians, rather than the physicians maintaining independent practices. The strategy of hospitals employing physicians has become widespread due to changes in the industry which make the arrangement necessary and advantageous in many instances. The long term effect of physician employment will be that an adequate number of primary care and specialty providers will be retained in the community, which in turn will generate patients and revenue streams for HCH. In the short term, salary and benefits costs will increase in total and in relation to net revenue, as it normally will take the physician practices three to five years to build and mature.

The Financial Statements

The HCH financial statements consist of - a Statement of Net Assets, a Statement of Revenues, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These statements provide short-term and long-term financial information.

The Statement of Net Assets and Statement of Revenues, Expenses, and Changes in Net Assets provide information on the HCH resources and its activities. These two statements report the net assets of HCH and its changes. Increases or decreases of the HCH net assets are one indicator of whether its financial health is improving or eroding. However, other non-financial factors such as changes in economic conditions, population growth, patient demographic changes, and new or changed government legislation should also be considered.

The Statement of Net Assets includes all of the HCH assets and liabilities, and the net assets, which can be thought of as the net worth of HCH. All of the current year's revenue and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Assets. This statement measures the financial results of the HCH operations and presents revenue earned and expenses incurred. The other primary financial statement is the Statement of Cash Flows. This statement provides information about HCH sources and uses of cash during the year, and the cash flows from operating activities, capital and related financing activities, and investing activities.

A summary of the HCH Net Assets as of December 31, 2010 and 2009 is presented below, in 000's:

	2010	2009	$ Change	% Change
Assets:				
Cash and Investments	$17,375	$15,926	$1,449	9.1%
Capital Assets	42,795	46,770	(3,975)	-8.5%
Other Assets	11,372	10,179	1,193	11.7%
Restricted Assets - Cash	7,752	6,215	1,537	24.7%
Restricted Assets - Receivable	8,000	515	7,485	N/A
Total Assets	$87,294	$79,605	$7,689	9.7%
Liabilities:				
Long Term Debt Outstanding	$27,290	$28,155	($865)	-3.1%
Current and Other Liabilities	8,079	3,990	4,089	102.5%
Total Liabilities	35,369	32,145	3,224	10.0%
Net Assets:				
Invested in Capital Assets - Net of Related Debt	14,640	17,939	(3,299)	-18.4%
Unrestricted	29,122	28,792	330	1.1%
Restricted	8,163	729	7,434	1019.8%
Total Net Assets	51,925	47,460	4,465	9.4%
Total Liabilities and Net Assets	$87,294	$79,605	$7,689	9.7%

The 9.4% increase in total net assets in 2010 was primarily due to an $8 million pledge receivable recorded, which was received from Harrison County and designated for debt reduction. This was offset somewhat by a reduction in net capital assets, which is due to depreciation recognized on capital assets, which consists primarily of the new building and equipment acquired in 2008.

Cash on hand increased almost $3 million in 2010 as a result of positive cash flow generated from operations. Current and other liabilities increased by $4 million at the end 2010 compared to 2009. The increase was due to the recognition in 2010 of a liability on a derivative instrument of $3 million, and estimated amounts payable to Medicare of $1 million for cost report settlements.

A summary of the HCH Statement of Revenues, Expenses and Changes in Net Assets as of December 31, 2010 and 2009 is presented below, in 000's:

	2010	**2009**	**$ Change**	**% Change**
Revenue:				
Net Patient Service Revenue, net of provision for Bad Debt: 2010 ($5,404); 2009($4,562)	$36,821	$38,461	($1,640)	-4.3%
Other	1,243	1,680	(437)	-26.0%
Total Operating Revenue	38,064	40,141	(2,077)	-5.2%
Expenses:				
Salaries and Benefits	22,716	22,594	122	0.5%
Medical Supplies and Drugs	3,688	3,689	(1)	0.0%
Depreciation and Amortization	5,093	5,061	32	0.6%
Other	9,430	10,276	(846)	-8.2%
Total Operating Expenses	40,927	41,620	(693)	-1.7%
Operating Income	(2,863)	(1,479)	(1,384)	93.6%
Non-Operating Revenue	678	713	(35)	-4.9%
Non-Operating Expense	(1,350)	(1,348)	(2)	0.1%
Excess of Revenue over Expenses	(3,535)	(2,114)	(1,421)	67.2%
Capital Grants and Contributions	8,000	750	7,250	966.7%
Total Net Assets - Beginning of Year	47,460	48,824	(1,364)	-2.8%
Total Net Assets - End of Year	$51,925	$47,460	$4,465	9.4%

Sources of Revenue

During 2010 and 2009 HCH derived substantially all of its revenue from patient service and other related programs. Revenue is received from Medicare and Medicaid programs, self pay patients, insurance carriers, preferred provider organizations, and managed care companies. Other revenue includes subsidies from Harrison County for the operation of the county ambulance service, totaling $1,274,505 in 2010 and $1,266,729 in 2009.

The following table presents the percentages of gross revenue for patient services, by payer, for the years ended December 31, 2010 and 2009, respectively.

Payer	2010	2009
Medicare	44.1%	43.8%
Medicaid	15.6%	14.0%
Anthem	14.0%	16.4%
Commercial Insurance	3.1%	3.4%
Managed Care	12.6%	12.0%
Self Pay	7.6%	7.2%
Other	3.0%	3.2%
Total	100.0%	100.0%

Operating and Financial Performance

Revenue

Net patient service revenue decreased 4.3% during 2010 due to several factors related to the local economy and continued shifts in payer mix. HCH experienced lower patient volumes, an increase in Medicaid utilization, and an increase in uninsured care.

- Inpatient days of service decreased by 2% in 2010, while total outpatient visits decreased by 3%.

- The portion of deductions from gross revenue recognized by HCH for uninsured care and charity care in 2010 was $8.3 million, or 8.7% of gross revenue, compared to $7.2 million, or 8.0% of gross revenue in 2009. Uninsured care is included in provision for bad debt expense and represents uncollected charges for services not covered by insurance, and for patients that do not have health insurance. Charity care is recognized as a deduction from gross revenue, and represents charges written off that were incurred in providing care to uninsured low income and indigent patients. HCH has a policy and a commitment to provide emergency care to all patients without regard for their ability to pay for services. Over the past ten years there has been a trend of increasing uninsured care.

- Settlements totaling $1,268,560 were received in 2010 under the Indiana Medicaid program, relating to the State of Indiana's fiscal year 2010. These payments were made as part of the Disproportionate Share Hospital program, and are recorded as offsets to revenue adjustments in the HCH accounting records. These payments were made from funds that are available to partially cover the hospital's cost of care to Medicaid and uninsured patients.

Expenses

Total operating expenses decreased by 1.7% in 2010. Factors that had an impact on expenses are discussed below.

- Salaries and benefits costs for 2010 increased slightly by 1%. Labor costs in many hospital departments were reduced in response to lower patient volumes and in an effort to improve productivity. The savings were partially offset by the employment of several physicians and office staff for new practices. Wage and salary rates were frozen for 2010 as lower payer reimbursements and patient volumes reduced margins.

- All operating expenses other than salaries and benefits decreased by 4.3%, or $815,000 from 2009. Professional services expense decreased by $684,000 with the conversion of contract anesthesia providers to an employed physician, and a reduction in the amount of physician guarantees that were forgiven during 2010. Other various expenses were reduced as a result of a number of cost reduction efforts.

Capital Contributions

A pledge for a capital contribution from Harrison County in the amount of $8,000,000 was recognized in 2010. This contribution was designated for the retirement of a portion of the long term debt outstanding.

Long Term Debt

At fiscal year end 2010, HCH had total notes payable of $27.3 million, which represents revenue bonds that HCH issued for the construction of the new hospital facility. Annual principal payments on these bonds began in October, 2008, with interest being paid monthly. HCH plans to reduce and restructure the long term debt in 2011. HCH plans to retire a large portion of the long term debt and refinance the remaining portion in 2011. More detailed information on HCH's long term debt is presented in the Notes to the Financial Statements.

Capital Assets

During 2010 HCH invested $1.02 million in various capital assets. A summary of the capital assets is presented below, in 000's:

	2010	2009	$ Change	% Change
Land and Land Improvements	$6,750	$6,737	$13	0.2%
Buildings and Fixed Equipment	36,931	35,821	1,110	3.1%
Equipment	19,453	19,109	344	1.8%
Total Capital Assets	63,134	61,667	1,467	2.4%
Less Accumulated Depreciation	(20,387)	(15,392)	(4,995)	32.5%
Construction in Progress	48	494	(446)	-90.3%
Capital Assets - Net	$42,795	$46,769	($3,974)	-8.5%

HCH continues to invest in capital equipment in order to meet the needs of the service area population. These capital improvements result in increased service capacity, greater efficiencies, and upgraded technology. With the addition of substantially all new facilities and equipment in 2008, major asset purchases will be minimal for several years, with the probable exception of information systems. Federal and industry requirements to expand electronic health records systems will necessitate the upgrade of hospital and physician information systems.

The table below shows HCH's 2011 capital budget with projected spending of $1.6 million for capital projects. Equipment to be placed in service in 2011 will be purchased from operating cash and cash reserves.

Capital Budget (in 000's)	**2011**
Equipment Replacement & Upgrades	$925
Information Systems	675
Total Capital Budget	$1,600

More information on HCH's capital assets is presented in the Notes to the Financial Statements.

Economic and Industry Factors for 2011 Budget

The HCH Board of Trustees and management considered many factors when setting the 2011 budget. Of primary importance in setting the budget was the status of the economy and industry trends, which takes into account market forces and regulatory factors such as the following items:

- Population growth, demographic shifts, and the expanding need for services
- Continuously increasing expectations for quality improvement
- Advances in medical equipment technology and the need to replace obsolete equipment
- Healthcare reform legislation and requirements to improve electronic medical records
- Privacy legislation – Health Insurance Portability and Accountability Act (HIPAA)
- Increasing emphasis on the integrity of public financial information
- Growing number of uninsured and underinsured patients
- Increasing costs of labor, medical supplies and drugs, and insurance
- Access to additional capital, and management of cash and debt levels
- Cash and resource requirements needed for the HCH strategic plan

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

Contacting HCH's Financial Manager

This report is designed to provide our citizens, customers, and creditors with a general overview of HCH's finances and to demonstrate accountability. If you have questions about this report or need additional information, contact the Chief Financial Officer, Jeffrey L. Davis at 812-738-4251.

HARRISON COUNTY HOSPITAL
A COMPONENT UNIT OF HARRISON COUNTY, STATE OF INDIANA
STATEMENT OF NET ASSETS
December 31, 2010

Assets	Primary Government
Current assets:	
Cash and cash equivalents	$ 17,375,117
Patient accounts receivable, net of estimated uncollectibles of $8,410,302	4,613,930
Other receivables-restricted	8,000,000
Supplies and other current assets	2,395,214
Noncurrent cash and investments:	
Internally designated	7,589,255
Held by trustee for debt service	162,891
Capital assets:	
Land and construction in progress	3,250,393
Depreciable capital assets, net of accumulated depreciation	39,545,010
Other assets:	
Investment in affiliated companies	1,034,072
Deferred outflow of Resources	2,921,376
Other	406,555
Total assets	$ 87,293,813

Liabilities and Net Assets	
Current liabilities:	
Current maturities of long-term debt	$ 865,000
Accounts payable and accrued expenses	2,299,734
Estimated third-party payor settlements	1,136,706
Other current liabilities	842,834
Long-term debt, net of current maturities	27,290,000
Other long-term liabilities	
Derivative Instrument - 2005 SWAP	2,921,376
Other	13,144
Total liabilities	35,368,794
Net assets:	
Invested in capital assets, net of related debt	14,640,403
Restricted:	
Expendable for debt service	8,162,892
Unrestricted	29,121,724
Total net assets	51,925,019
Total liabilities and net assets	$ 87,293,813

The accompanying notes are an integral part of the financial statements.

HARRISON COUNTY HOSPITAL
A COMPONENT UNIT OF HARRISON COUNTY, STATE OF INDIANA
BALANCE SHEET
December 31, 2010

Assets	Discrete Component Unit
Current assets:	
Cash	$ 127,397
Receivables:	
Tenants - rent	4,526
Tenants - suite improvements	3,969
Related party	13,144
Net receivables	21,639
Prepaid expenses	2,931
Total current assets	151,967
Other Asset	
Unamortized loan costs (net of amortization of $53,499)	108,149
Property	
Tenant improvements	2,474,919
Buildings	4,712,880
Total property	7,187,799
Less accumulated depreciation	493,511
Net property	6,694,288
Total assets	$ 6,954,404
Liabilities and Members' Equity	
Current Liabilities	
Current installments of long-term debt	$ 91,948
Accounts payable	23,361
Accounts payable - related party	78,278
Deferred revenue	1,105
Total current liabilities	194,692
Long-Term Liabilities	
Long-term debt, less current installments	5,441,518
Interest rate swap	1,108,502
Total long-term liabilities	6,550,020
Members' Equity:	
Contributed capital	1,493,515
Deficit	(207,319)
Accumulated other comprehensive loss	(1,076,504)
Total members' equity	209,692
Total liabilities and members' equity	$ 6,954,404

The accompanying notes are an integral part of the financial statements.

HARRISON COUNTY HOSPITAL
A COMPONENT UNIT OF HARRISON COUNTY, STATE OF INDIANA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
Year Ended December 31, 2010

	Primary Government
Operating revenues:	
Net patient service revenue (net of provision for bad debt)	$ 36,820,748
Other	1,243,641
Total operating revenues	38,064,389
Operating expenses:	
Salaries and benefits	22,715,840
Professional fees and purchased services	5,503,524
Medical supplies and drugs	3,688,152
Insurance	621,038
Other supplies	2,167,006
Depreciation and amortization	5,093,420
Other	1,138,260
Total operating expenses	40,927,240
Operating loss	(2,862,851)
Nonoperating revenues (expenses):	
Investment income	572,970
Interest expense	(1,214,263)
Noncapital grants and contributions	105,404
Loss on sale of equipment	(15,553)
Loss on investment in affiliated companies	(110,223)
Other	(10,745)
Total nonoperating expenses	(672,410)
Deficiency of revenues under expenses before capital grants and contributions	(3,535,261)
Capital grants and contributions	8,000,000
Increase in net assets	4,464,739
Net assets beginning of the year	47,460,280
Net assets end of the year	$ 51,925,019

The accompanying notes are an integral part of the financial statements.

HARRISON COUNTY HOSPITAL
A COMPONENT UNIT OF HARRISON COUNTY, STATE OF INDIANA
STATEMENT OF INCOME, EXPENSES, AND CHANGES IN MEMBERS' EQUITY
Year Ended December 31, 2010

	Discrete Component Unit
Rental Income	$ 829,157
Operating expenses:	
Utilities	94,063
Rent	59,361
Repairs and maintenance	22,577
Insurance	7,923
Depreciation	241,290
Amortization	16,165
Professional fees	22,064
Cleaning	15,451
Security	9,767
Miscellaneous	3,048
Total operating expenses	491,709
Operating income	337,448
Other income (expenses):	
Interest income	2,781
Interest expense	(417,113)
Loss on interest rate swap	(5,351)
Total other expenses	(419,683)
Deficiency of income under expenses before other comprehensive loss and return of capital distributions	(82,235)
Other comprehensive loss	(181,931)
Return of capital distributions	(84,000)
Members' equity beginning of the year	557,858
Members' equity end of the year	$ 209,692

The accompanying notes are an integral part of the financial statements.

HARRISON COUNTY HOSPITAL
A COMPONENT UNIT OF HARRISON COUNTY, STATE OF INDIANA
STATEMENT OF CASH FLOWS - RESTRICTED AND UNRESTRICTED FUNDS
Year Ended December 31, 2010

	Primary Government
Cash flows from operating activities:	
Receipts from and on behalf of patients	$ 37,181,147
Payments to suppliers and contractors	(11,526,929)
Payments to employees	(22,572,437)
Other receipts and payments, net	1,785,468
Net cash provided by operating activities	4,867,249
Cash flows from noncapital financing activities:	
Noncapital grants and contributions	105,404
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(561,278)
Principal paid on long-term debt	(675,000)
Interest paid on long-term debt	(1,214,263)
Proceeds from sale of assets	1,750
Net cash used by capital and related financing activities	(2,448,791)
Cash flows from investing activities:	
Interest and dividends on investments	622,792
Loan to affiliated company	(79,510)
Investment in affiliated company	(30,000)
Proceeds from sale of investments	10,596,495
Net cash provided by investing activities	11,109,777
Net increase in cash and cash equivalents	13,633,639
Cash and cash equivalents at beginning of year	11,330,733
Cash and cash equivalents at end of year	$ 24,964,372
Reconciliation of cash and cash equivalents to the Statement of Net Assets:	
Cash and cash equivalents in current assets	$ 17,375,117
Internally designated cash and cash equivalents	7,589,255
Total cash and cash equivalents	$ 24,964,372
Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	$ (2,862,851)
Adjustments to reconcile operating loss to net cash flows provided in operating activities:	
Depreciation and amortization	5,093,420
Provision for bad debts	5,403,512
(Increase) decrease in current assets:	
Other receivable-intercompany construction	2,485
Patient accounts receivable	(5,043,113)
Estimated third-party payor settlements	1,378,994
Supplies and other current assets	785,650
Increase (decrease) in current liabilities:	
Accounts payable and accrued expenses	(278,243)
Other current liabilities	145,861
Estimated third-party payor settlements	255,406
Other liabilities related to operating activities	(13,872)
Net cash provided in operating activities	$ 4,867,249

Noncash investing, capital, and financing activities:
The Hospital received a contribution of capital assets from Harrison County of $504,004 for the EMS building project.

The accompanying notes are an integral part of the financial statements.

I. Summary of Significant Accounting Policies

A. Reporting Entity

Harrison County Hospital (Hospital) is a county-owned facility and operates under the Indiana County Hospital Law, Indiana Code 16-22. The Hospital provides short-term inpatient and outpatient health care.

The Board of County Commissioners of Harrison County appoints the Governing Board of the Hospital and a financial benefit/burden relationship exists between the County and the Hospital. For these reasons, the Hospital is considered a component unit of Harrison County.

The accompanying financial statements present the activities of the Hospital (primary government) and its significant component unit. The component unit discussed below is included in the Hospital's reporting entity because of the significance of its operational or financial relationship with the Hospital. Blended component units, although legally separate entities are in substance part of the government's operations and exist solely to provide services for the government; data from these units is combined with data of the primary government. Discretely presented component units are involved in activities of an operational nature independent from the government; their transactions are reported on a separate page in the basic financial statements to emphasize that it is legally separate from the Hospital.

<u>Discretely Presented Component Unit</u>

The Harrison MOB, LLC, was organized in September 2006, and is a significant discretely presented component unit of the Hospital. The discrete component unit is fiscally dependent on the primary government. The discrete component unit is a partnership that reports its financial results according to Accounting Standards Codification 820 (formerly Statement of Financial Accounting Standards No. 157). No modifications have been made to the discrete component unit's financial information in the Hospital's financial reporting entity for these differences; however, significant note disclosures to the discrete component unit's financial statements have been incorporated into the Hospital's notes to the financial statements.

The financial statements of the discrete component unit may be obtained from its respective office as follows:

Harrison County Hospital
1141 Hospital Drive NW
Corydon, IN 47112

A separate audit report is prepared for the individual component unit.

B. Enterprise Fund Accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the enterprise fund statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their enterprise funds, subject to this same limitation. The Hospital has elected not to follow subsequent private-sector guidance.

During the year 2010, the Hospital adopted GASB Statement No. 53, *"Accounting and Financial Reporting for Derivative Instruments."*

C. Assets, Liabilities and Net Assets or Equity

1. Deposits and Investments

Cash and cash equivalents include demand deposits and investments in highly liquid debt instruments with an original maturity date of three months or less.

Short-term investments are investments with remaining maturities of up to ninety days.

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

Nonparticipating certificates of deposit, demand deposits, and similar nonparticipating negotiable instruments that are not reported as cash and cash equivalents are reported as investments at cost.

Debt securities are reported at fair value. Debt securities are defined as securities backed by the full faith and credit of the United States Treasury or fully insured or guaranteed by the United States or any United States government agency.

Open-end mutual funds are reported at fair value.

Money market investments that mature within one year or less at the date of their acquisition are reported at amortized cost. Other money market investments are reported at fair value.

Investments in affiliated companies are reported using the equity method of accounting, or at cost, as applicable.

Other investments are generally reported at fair value.

Investment income, including changes in the fair value of investments, is reported as nonoperating revenues in the Statement of Revenues, Expenses, and Changes in Net Assets.

2. 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 disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Capital Assets

Capital assets, which include land, land improvements, buildings and fixed equipment, and equipment, are reported at actual or estimated historical cost based on appraisals or deflated current replacement cost. Contributed or donated assets are reported at estimated fair value at the time received.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods and estimated useful lives of capital assets reported in the financial statements are as follows:

	Capitalization Threshold	Depreciation Method	Estimated Useful Life
Land	$ 5,000	Not Applicable	Not Applicable
Land improvements	5,000	Straight-line	AHA guide
Buildings and fixed equipment	5,000	Straight-line	AHA guide
Equipment	5,000	Straight-line	AHA guide

For depreciated assets, the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed. The total interest expense incurred by the Hospital during the current year was $1,214,263. Of the amount, $0 was included as part of the cost of capital assets under construction in connection with new medical facilities and various other renovation projects. The total interest expense incurred by the discrete component unit during the current year was $417,113. Of the amount, $0 was included as part of the cost of building and improvements.

4. Other Assets

Other Assets consist of a deferred outflow of resources from an interest rate swap, Investment in affiliated companies, and other.

5. Net Assets and Members' Equity

Net assets of the Hospital are classified in three components.

Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets.

Restricted expendable net assets are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, contributors, or enabling legislation external to the hospital, including amounts deposited with trustees as required by revenue bond indentures, discussed in Note II G.

Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

Members' equity of the discrete component unit is classified in three components.

Contributed capital consists of purchases of shares of units net of any return of capital distributions.

Deficit is the accumulated net income (loss).

Accumulated other comprehensive loss consists of the gain or loss on the effective portion of the change in the fair value of the derivative financial instrument.

D. Grants and Contributions

From time to time, the Hospital receives grants from Harrison County and the State of Indiana as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

From time to time, the discrete component unit receives grants from Harrison County Hospital, individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as other income. Amounts restricted to capital acquisitions are reported after other income and expenses.

E. Restricted Resources

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

F. Operating Revenues and Expenses

The Hospital's Statement of Revenues, Expenses, and Changes in Net Assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Hospital's principal activity. Nonexchange revenues, including grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

G. Net Patient Service Revenue

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

H. Charity Care

The Hospital has a policy of providing charity care to patients who are unable to pay. Such patients are identified based on financial information obtained from the patient and subsequent analysis. Because the agency does not expect payment, estimated charges for charity are not included in revenue.

I. Supplies

Inventories of drugs and other supplies are stated at the lower of cost (first-in, first-first-out) or market.

J. Compensated Absences

The Hospital's policy on paid days off (which includes vacation, sick leave, personal leave, and holidays) allows full-time employees and regular part-time employees to accrue paid days off, to a maximum of 60 days.

Paid days off are accrued when incurred and reported as a liability.

K. Fair Value of Financial Instruments

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

Cash and Cash Equivalents

The carrying amount reported in the Statement of Net Assets for cash and cash equivalents approximates its fair value.

Short-Term Investments

The carrying amount reported in the Statement of Net Assets is the investment's fair value on the day it becomes a short-term investment.

Investments

Fair values, which are the amounts reported in the Statement of Net Assets, are based on quoted market prices, if available, or are estimated using quoted market prices for similar securities.

Other Assets

The carrying amount reported in the Statement of Net Assets for deferred outflow of resources from an interest rate swap are based on mathematical approximations of market values derived from proprietary models as of the close of business on December 31, 2010.

Accounts Payable and Accrued Expenses

The carrying amount reported in the Statement of Net Assets for accounts payable and accrued expenses approximates its fair value.

Estimated Third-Party Payor Settlements

The carrying amount reported in the Statement of Net Assets for estimated third-party payor settlements approximates its fair value.

Long Term Debt

Fair values of the Hospital's revenue notes are based on current traded value. The fair value of the Hospital's remaining long term debt is estimated using discounted cash flow analyses, based on the Hospital's current incremental borrowing rates for similar types of borrowing arrangements.

Effective January 1, 2009, the discrete component unit adopted the provisions of ASC 820, Fair Value Measurements, for financial assets and financial liabilities. The discrete component unit has no nonfinancial assets and nonfinancial liabilities determined at fair value.

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following three levels:

1. Inputs to the valuation methodology are quoted prices, unadjusted for identical assets or liabilities in active markets. A quoted market price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

2. Inputs to the valuation methodology include quoted market prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted market prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that are derived principally from or can be corroborated by observable market data by correlation or other means.

3. Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using discounted cash flow methodologies, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The discrete component unit's interest rate swap liability is measured on a recurring basis. As of December 31, 2010, the balance of the interest rate swap was a liability in the amount of $1,108,502, using level 2 above.

Interest Rate Swap. The interest rate swap is reported at fair value on a recurring basis using Level 2 inputs. The fair value is based on expected cash flows over the life of the contract. The expected cash flows are determined by evaluating transactions with a pricing model using a specific market environment. The value of the interest rate swap was estimated using the closing mid-market rate/price environment of December 31, 2010. While management believes the discrete component unit's valuation methodologies are appropriate and consistent, the use of different methodologies or assumptions to determine fair value could result in a different estimate of fair value at the reporting date.

Derivative Financial Instrument

The discrete component unit has designated a fixed rate interest rate swap as a cash flow hedge of the variability of cash flows to be paid on long-term debt. The gain or loss on the effective portion of the hedge (i.e., change in the fair value) is initially recorded as a component of other comprehensive income. The remaining gain or loss, if any, representing the ineffective portion is recognized currently in earnings. Amounts in accumulated other comprehensive income are reclassified into earnings in the same period in which the hedged forecasted transaction affects earnings (when interest expense is recognized in earnings).

The discrete component unit documents the relationship between its hedging instruments and hedged liabilities. This process includes linking all derivatives that are designated as cash flow hedges to specific forecasted interest payments for long-term debt.

The discrete component unit assesses both at the cash flow hedge's inception and on an ongoing basis, whether the derivative instruments that are used in hedging transactions have been highly effective in offsetting changes in cash flows and whether they are expected to continue to be highly effective in future periods. When it is determined that a derivative has ceased to be highly effective as a cash flow hedge, the discrete component unit discontinues hedge accounting prospectively.

The discrete component unit discontinues cash flow hedge accounting prospectively when (1) it is determined that the derivative is no longer effective in offsetting changes in the cash flows of the hedged item; (2) the derivative expires or is sold, terminated, or exercised; (3) the derivative is de-designated as a hedge instrument, because it is unlikely that the forecasted transaction (cash flows) will occur; or (4) management determines that designation of the derivative as a hedge instrument is no longer appropriate. When hedge accounting is discontinued because it is probable that a forecasted transaction will not occur, the net derivative gain or loss that was accumulated in other comprehensive income will be recognized immediately in earnings. In all other situations in which cash flow hedge accounting is discontinued, the net derivative gain or loss related to the discontinued cash flow hedge remains in accumulated other comprehensive income and is reclassified into earnings in the same period or periods during which the hedged forecasted transaction offsets earnings.

II. Detailed Notes

A. Deposits and Investments

1. Deposits

Custodial credit risk is the risk that, in the event of a bank failure, the government's deposits may not be returned to it. Indiana Code 16-22-3-16 allows a Hospital Governing Board to deposit public funds in a financial institution. The Hospital does not have a formal policy regarding custodial credit risk for deposits. At December 31, 2010, the Hospital had deposit balances in the amount of $25,483,767.

The bank balances were insured by the Federal Deposit Insurance Corporation or the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Harrison MOB, LLC, maintains its cash at financial institutions. At times, the balances may be in excess of federally insured limits.

2. Investments

Authorization for investment activity is stated in Indiana Code 16-22-3-20. As of December 31, 2010, the Hospital had the following investments:

Investment Type	Primary Government Market Value
U.S. treasuries and securities	$ 162,891

Statutory Authorization for Investments

Indiana Code 16-22-3-20 authorizes the Hospital to invest in:

Any interest bearing account that is authorized to be set up and offered by a financial institution or brokerage firm registered and authorized to do business in Indiana

Repurchase or resale agreements involving the purchase and guaranteed resale of any interest bearing obligations issued or fully insured or guaranteed by the United States or any United States government agency in which type of agreement the amount of money must be fully collateralized by interest bearing obligations as determined by the current market value computed on the day the agreement is effective

Mutual funds offered by a financial institution or brokerage firm registered and authorized to do business in Indiana

Securities backed by the full faith and credit of the United States Treasury or fully insured or guaranteed by the United States or any United States government agency

Pooled fund investments for participating hospitals offered, managed, and administered by a financial institution or brokerage firm registered or authorized to do business in Indiana.

Investment Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Hospital does not have a formal investment policy for custodial credit risk for investments. The Hospital's investments did not have custodial credit risk.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Hospital does not have a formal investment policy for interest rate risk for investments. The Hospital's investments did not have interest rate risk.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Hospital does not have a formal investment policy for credit risk for investments. The Hospital's investments did not have credit risk.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The Hospital does not have a policy in regards to concentration of credit risk. United States of America government and United States of America governmental agency securities are exempt from this policy requirement. The Hospital's investments did not have concentration of credit risk.

Foreign Currency Risk

The Hospital does not have a formal policy in regards to foreign currency risk. The Hospital's investments did not have foreign currency risk.

B. Accounts Receivable and Payable

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the Hospital at year end consisted of these amounts:

Patient Accounts Receivable	
Receivable from patients and their insurance carriers	$ 8,913,241
Receivable from Medicare	3,612,756
Receivable from Medicaid	498,235
Total patient accounts receivable	13,024,232
Less allowance for uncollectible amounts	8,410,302
Patient accounts receivable, net	$ 4,613,930

Accounts Payable and Accrued Expenses	
Payable to employees	$ 794,687
Payable to suppliers	1,505,047
Total accounts payable and accrued expenses	$ 2,299,734

C. Capital Assets

Capital asset activity for the year ended December 31, 2010, was as follows:

Primary Government	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	$ 3,202,421	$ -	$ -	$ 3,202,421
Construction in progress	494,317	999,961	1,446,306	47,972
Total capital assets, not being depreciated	3,696,738	999,961	1,446,306	3,250,393
Capital assets, being depreciated:				
Land improvements	3,534,345	13,394	-	3,547,739
Buildings and fixed equipment	35,821,185	1,433,621	323,994	36,930,812
Equipment	19,109,485	427,515	83,632	19,453,368
Totals	58,465,015	1,874,530	407,626	59,931,919
Less accumulated depreciation for:				
Land improvements	717,103	259,701	-	976,804
Buildings and fixed equipment	4,317,908	2,047,511	-	6,365,419
Equipment	10,357,442	2,767,587	80,343	13,044,686
Totals	15,392,453	5,074,799	80,343	20,386,909
Total capital assets, being depreciated, net	43,072,562	(3,200,269)	327,283	39,545,010
Total primary government capital assets, net	$ 46,769,300	$ (2,200,308)	$ 1,773,589	$ 42,795,403
Discretely Presented Component Unit				
Capital assets, being depreciated:				
Tenant improvements	$ 2,474,919	$ -	$ -	$ 2,474,919
Buildings	4,712,880	-	-	4,712,880
Totals	7,187,799	-	-	7,187,799
Less accumulated depreciation	252,221	241,290	-	493,511
Total discretely presented component unit capital assets, net	$ 6,935,578	$ (241,290)	$ -	$ 6,694,288

D. Construction Commitments

Construction work in progress is composed of the following:

Project	Total Project Authorized	Expended to December 31, 2010	Committed
Information Systems	$ 44,950	$ 37,596	$ 7,354
EMS Phone System	10,400	10,376	23
Totals	$ 55,350	$ 47,972	$ 7,377

E. Leases

Operating Leases

The Hospital has entered into various operating leases having initial or remaining noncancelable terms exceeding one year for office space. Rental expenditures for these leases were $663,932. The following is a schedule by years of future minimum rental payments as of year end:

2011	$ 718,469
2012	672,695
2013	672,695
2014	672,695
2015	672,695
2016-2018	2,036,402
Total	$ 5,445,651

F. Long-Term Liabilities

1. Revenue Bonds

The Hospital issues bonds to be paid by income derived from the acquired or constructed assets. Revenue bonds outstanding at year end are as follows:

Purpose	Interest Rates	Balance at December 31
2005 Hospital construction revenue bonds	variable	$ 28,155,000

Disclosure information for the 2005 Revenue Bond Issue which includes interest rate swap agreements follows:

As a means to lower its borrowing costs, when compared against fixed-rate bonds at the time of issuance in November 2005, the Hospital entered into an interest rate swap in connection with its $30,000,000 Series 2005 auction rate bond. The intention of the swap was to effectively change the Hospital's variable interest rate on the bond to a synthetic fixed rate of 3.55 percent.

Under the swap agreement, the Hospital pays the counterparty, U.S. Bancorp Piper Jaffray Financial Products Inc., a fixed payment of 3.81 percent and receives a variable payment computed as 70 percent of the London Interbank Offered Rate (LIBOR). The swap has equal notional amount totaling $25,000,000 and the associated auction rate bonds have a $25,000,000 principal amount. The swap was entered into at the same time the bonds were issued in November 2005. The notional value of the swap declined by $675,000 in 2010 and in increasing amounts in future years as the principal amount of the associated debt declines. The auction rate on the bonds closely approximates the Bond Market Association Municipal Swap Index (BMA). The bonds and related swap agreement matures on October 1, 2032. As of December 31, 2010, rates were as follows:

	Terms	Rates (%)
Interest rate swap:		
Fixed payment to counterparty	Fixed	3.81%
Variable payment from counterparty	70% of LIBOR	0.19%
Net interest rate swap payments		3.62%
Variable auction-rate bond payments		-0.51%
Synthetic interest rate of bonds		3.11%

As of December 31, 2010, the swap had a negative fair value of $2,921,376. The negative fair value of the swap may be countered by reductions in total interest payments required by the auction rate bond, creating lower synthetic rates. Because the auction rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value increase.

As of December 31, 2010, the Hospital was not exposed to credit risk in the amount of the derivative's fair value, because the swap had a negative fair value. However, should interest rates change and the fair value of the swap become positive, the Hospital would be exposed to credit risk in the amount of the derivative's fair value. The swap counterparty is currently rated A by Standard & Poor's, A2 by Moody's Investors Service and A by Fitch Ratings. The swap agreement does not contain collateral provisions for either party.

The swap exposes the Hospital to basis risk should the relationship between LIBOR and auction rates converge, changing the synthetic rate on the bonds. If a change occurs that results in the rates' moving to convergence, the expected cost savings may not be realized.

The derivative contracts use the International Swaps and Derivatives Association Master Agreement, which include standard termination events, such as failure to pay and bankruptcy. The Schedules to the Master Agreements include additional termination events. The swap may be terminated by the Hospital if the counterparty's credit rating falls below BBB- by Standard & Poor's, Aa3 by Moody's Investors Service or if either rating is withdrawn or suspended. The counterparty may terminate the swap agreement if the Hospital's rating by Standard & Poor's falls below BBB- or the rating is withdrawn or suspended. Either party may terminate the swap if the other fails to perform under the terms of the contract. If the swap is terminated, the auction rate bonds would no longer carry a synthetic interest rate. Also, if at the time of termination the swap has a negative fair value, the Hospital would be liable to the counterparty for a payment equal to the swap's fair value.

As of December 31, 2010, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their terms, were as follows:

Year Ending	Variable-Rate Bonds		Interest Rate	Total
December 31	Principal	Interest	Swap, Net	Debt Service
2011	$ 865,000	$ 1,039,749	$ 987,898	$ 2,892,647
2012	895,000	1,005,650	955,499	2,856,149
2013	930,000	970,217	921,833	2,822,050
2014	960,000	933,641	887,081	2,780,722
2015	995,000	895,731	851,062	2,741,793
2016-2020	5,535,000	3,860,674	3,668,146	13,063,820
2021-2025	6,590,000	2,688,338	2,554,272	11,832,610
2026-2030	7,845,000	1,293,115	1,228,628	10,366,743
2031-2032	3,540,000	68,580	65,160	3,673,740
Totals	$ 28,155,000	$ 12,755,695	$ 12,119,579	$ 53,030,274

As rates vary, variable-rate bond interest payments and net swap payments will vary.

2. Harrison MOB, LLC, Note Payable

Long-term debt at December 31, 2010, was as follows:

Purpose	Interest Rates	Amount
Note payable to Harrison County Hospital in monthly installments of interest only, principal due April 2012	7.50%	$ 250,000
Note payable in monthly installments of principal and interest at one month LIBOR plus 1.25% maturing July 2017	Variable	5,283,466
Total		$ 5,533,466

Harrison MOB, LLC, (LLC) entered into a credit agreement in July 2007 to finance the construction of a medical office building. During construction, the agreement required payments of interest only on the outstanding balance. Upon substantial completion of the building, the agreement requires the commencement of principal payments to repay the obligation over 25 years. In February 2009, the building was deemed substantially complete and the LLC began making principal payments to amortize the balance of the loan of $5,440,000 over 25 years. Upon the commencement of principal payments, the interest rate on the loan decreased from LIBOR plus 1.35 percent to LIBOR plus 1.25 percent.

Following is a schedule by years of maturity requirements on long-term debt as of December 31, 2010:

Year Ending December 31	
2011	$ 91,948
2012	348,810
2013	106,185
2014	114,111
2015	122,628
Later years	4,749,784
Total	$ 5,533,466

The note payable is secured by all the LLC's assets and assignments of rents. The note payable was guaranteed by the Harrison County Hospital until the commencement of the payment of principal in February 2009.

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, the LLC entered into an interest rate swap agreement to hedge the variability in the forecasted interest payments for the variable rate term note described above. The agreement provides for the LLC to receive interest from the counterparty at one month LIBOR and to pay interest to the counterparty at a fixed rate of 5.97 percent on the outstanding notional amount which amortizes based on the expected amortization of the variable rate term note. At December 31, 2010, the fair value of the interest rate swap agreement was a liability in the amount of $1,108,502. This agreement was effective February 15, 2009 with the commencement of principal payments on the variable rate term note.

Summary information with respect to the interest rate swap agreement at December 31, 2010 was as follows:

	Fair Value	Notional Amount
Portion designated as a hedge	$ 1,076,830	$ 5,283,466
Portion not designated as a hedge	31,672	160,008
Total interest rate swap	$ 1,108,502	$ 5,443,474

3. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2010, was as follows:

Primary Government	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable:					
Revenue:					
Indiana Health and Educational Facility Financing Authority	$ 28,830,000	$ -	$ 675,000	$ 28,155,000	$ 865,000
Discretely Presented Component Unit					
General long-term debt	$ 5,621,398	$ -	$ 87,932	$ 5,533,466	$ 91,948

4. Net Revenue Available for Debt Service

The following disclosures concerning net revenue available for debt service applicable to the years ended December 31, 2010, are required by terms of the financing agreement between the Hospital and IHFFA:

Revenue from operations	$ 38,064,389
Investment income	572,970
Less:	
Net loss on disposal of assets	15,553
Expenses (excluding depreciation, amortization and interest on funded debt)	35,833,820
Total net revenue available for debt service	$ 2,787,986
Funded debt service for year	$ 1,889,263
Historical debt service coverage ratio	1:48

G. Restricted Net Assets

Hospital restricted, expendable net assets are available for the following purposes:

	2010
Expendable for debt service:	
General	$ 8,162,892

H. Net Patient Service Revenue

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:

1. Medicare

Inpatient acute care services and most outpatient services rendered to Medicare program beneficiaries are paid at 101 percent of allowable costs as reported on an annual Medicare Cost Report. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary.

2. Medicaid

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under bundled payments and fee for service payments, at amounts determined by the state. The Hospital is reimbursed at a these rates on an interim basis, with subsequent lump sum payments made that are based on formulas which factor in the amount and types of services to uninsured and Medicaid patients.

Revenue from the Medicare and Medicaid programs accounted for approximately 38.26 percent and 9.04 percent, respectively, of the Hospital's net patient revenue, net of bad debt expense, for the year ended 2010. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The 2010 net patient service revenue decreased approximately $518,182 due to prior year final settlement that is no longer subject to audits, reviews, and investigations.

The Hospital also has entered into payment agreements with certain commercial insurance carriers, HMO's, 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.

I. Charity Care

Charges excluded from revenue under the Hospital's charity care policy were $2,868,625 (7.79%) for 2010.

J. Internally Designated Assets

Non-current cash and investments internally designated include the following:

Funded Depreciation – Amounts transferred from the Operating Fund by the Hospital Board of Trustees through funding depreciation expense. Such amounts are to be used for equipment and building, remodeling, repairing, replacing or making additions to the Hospital buildings as authorized by Indiana Code 16-22-3-13.

Internally designated:	
Funded depreciation:	
Cash and cash equivalents	$ 7,589,255

III. Other Information

A. Risk Management

The Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; medical benefits to employees, retirees, and dependents (excluding postemployment benefits); and natural disasters.

The risks of torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; and natural disasters are covered by commercial insurance from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. There were no significant reductions in insurance by major category of risk.

Medical Benefits to Employees and Dependents

The Hospital has chosen to establish a risk financing fund for risks associated with medical benefits to employees and dependents. The risk financing fund is accounted for in the Operating Fund, where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of $100,000 per year for one claimant due to unusual medical circumstances and $45,000 per year for all others. Settled claims resulting from this risk did not exceed commercial insurance coverage in the past three years. Amounts are paid into the fund by all departments and are available to pay claims, claim reserves, and administrative costs of the program. Provisions are also made for unexpected and unusual claims.

Claim expenditures and liabilities of the fund are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported (IBNRs). Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amounts of payouts and other economic and social factors.

However, claim liabilities cannot be reasonably estimated.

B. Subsequent Events

During 2011, the Hospital restructured its long term debt in order to lower ongoing interest costs and improve access to credit in the future. The outstanding 2005 Revenue Bonds in the amount of $28,155,000 were retired by the Hospital, with $8,000,000 being paid off in February 2011 and the balance of $20,155,000 retired in August 2011. The sources of funds to retire the debt consisted of an $8,000,000 contribution from Harrison County, $10,155,000 of hospital cash reserves, and a new loan of $10,000,000 from a consortium of four local and regional financial institutions.

The new loan of $10,000,000 is in the form of economic development bonds issued through Harrison County. The loan has a twenty year term, with a variable interest rate which is fixed at 3.55 percent through an interest rate swap that was in place with the 2005 revenue bonds. The loan requires fixed monthly payments with total annual payments of $701,734. Interest costs for this loan will be $171,166 in 2011 and $348,634 in 2012. The total annual interest cost for the Hospital as a result of the restructuring will not be reduced significantly for 2011 due to continuing swap payments. The hospital plans to lower the notional amount of the original interest rate swap to the amount of the new loan by the end of 2012.

C. Contingent Liabilities

Litigation

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

D. Fair Value Measurements

The Hospital has characterized its investments in securities, based on the priority of the inputs used to value the investments, into a three level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1), and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the investments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the investment.

Investments recorded in the Statement of Net Assets are categorized based on the inputs to valuation techniques as follows:

Level 1 – These are investments where values are based on unadjusted quoted prices for identical assets in an active market the Hospital has the ability to access.

Level 2 – These are investments where values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the investments. These investments are comprised of certificates of deposit.

Level 3 – These are investments where values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect assumptions of management about assumptions market participants would use in pricing the investments. These investments could be certain private equity investments.

Based upon the levels as defined the investments as of December 31, 2010, are classified as follows:

		Fair Value Measurements at Reporting Date Using:		
Hospital Investment Type	December 31, 2010	Quoted Prices in Active Markets For Identical (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. government securities	$ 162,891	$ -	$ 162,891	$ -

E. Investment in Affiliated Companies

Harrison-Floyd Health Services, LLC

In 2004, the Hospital entered into an agreement with Floyd Memorial Hospital and Health Services to establish and operate a limited liability company, Harrison-Floyd Health Services, LLC. In accordance with this agreement, each hospital invested $150,000 for 50 percent equity interest in the LLC. The investment was made in the fiscal years 2004 and 2005. The LLC began operation in 2004. The investment is recorded on the equity method. The Hospital's investment in affiliated company is included in the Other assets category of the Statement of Net Assets.

Summarized financial information as of December 31, 2010, and for the year then ended from the unaudited financial statements of the affiliated company follows:

Current assets	$ 43,016
Noncurrent assets	49,618
Current liabilities	14,583
Net assets	78,051
Revenues	90,125
Expenses	119,561
Net loss	(29,436)

Harrison MOB, LLC

On July 26, 2006, the Hospital entered into an agreement with several physicians and physician groups to establish and operate a medical office building to be located on the Hospital's campus in Corydon, Indiana, known as Harrison MOB, LLC (LLC). In accordance with this agreement, 68 Class A units and 37 Class B units were sold for $10,000 each, for an aggregate proceeds of $1,050,000. Each unit represents an equity interest of approximately .952 percent in the company. The Hospital purchased 64 units for an investment of $640,000 representing approximately 61.0 percent equity interest in the company. The medical office building was operational as of February 2009. The Hospital committed to lease available finished square footage in the building up to a 90 percent occupancy level for the first five years and up to 85 percent occupancy level for the next five years. The investment is recorded on the equity method. The Hospital's investment in affiliated company is included in the Other assets category of the Statement of Net Assets.

In July 2007, the LLC entered into a credit agreement in the principal amount of $5,440,000 to finance the construction of a medical office building on the campus of Harrison County Hospital. In February 2009, the building was deemed substantially complete and the LLC began making principal payments to amortize the balance of the loan of $5,440,000 over 25 years. The note payable is secured by all the LLC's assets, assignments of rents and a guarantee by Harrison County Hospital.

Summarized financial information as of December 31, 2010, and for the year then ended from the audited financial statements of the affiliated company follows:

Current assets	$ 151,967
Other assets	108,149
Capital assets, net	6,694,288
Current liabilities	194,692
Noncurrent liabilities	6,550,020
Members' equity	209,692
Revenues	831,938
Expenses	914,173
Net loss	(82,235)

Equity distributions were received by Harrison County Hospital from the LLC in 2010 in the amount of $49,850.

F. Revenues Pledged

Revenues Pledged in Connection with Component Unit Debt

The Hospital has entered into a 10 year master lease agreement with Harrison MOB, LLC, which requires the Hospital to rent enough space to maintain a 90 percent occupancy level during the first five years starting February 2009. During the remaining five years of the agreement the requirement drops to 85 percent. For the year ended December 31, 2010, the Hospital's leases totaled $601,863.

G. Pension Plan

Plan Description

The Hospital has a defined contribution pension plan administered by MetLife as authorized by IC 16-22-3-11. The plan provides retirement, disability, and death benefits to plan members and beneficiaries. The plan was established by written agreement between the Hospital Board of Trustees and the Plan Administrator. The Plan Administrator issues a publicly available financial report that includes financial statements and required supplementary information of the plan. That report may be obtained by contacting:

MetLife
c/o FasCare LLC
P.O. Box 173768
Denver, Colorado 80217-3768
Ph. (800) 543-2520

Funding Policy and Annual Pension Cost

The contribution requirements of plan members are established by the written agreement between the Hospital Board of Trustees and the Plan Administrator. Plan members are voluntary and are established by written authorization for payroll deduction into an annuity savings account. The Hospital is required to contribute at an actuarially determined rate. The current rate is 5 percent of annual covered payroll. Employer and employee contributions to the plan were $657,765 and $705,393, respectively.

H. Ambulance Service Subsidy

The Hospital provides ambulance service for Harrison County residents, through an agreement dated December 19, 1977. The agreement provides that Harrison County is to reimburse the Hospital, on a monthly basis, for the amount that expenses exceed revenues for the period. During the year 2010, Harrison County reimbursed the Hospital $1,274,505 for ambulance services. At December 31, 2010, Harrison County owed the Hospital an additional $271,352.

HARRISON COUNTY HOSPITAL
EXIT CONFERENCE

The contents of this report were discussed on November 10, 2011, with Steven L. Taylor, Chief Executive Officer; Jeffrey L. Davis, Chief Financial Officer; Paul Martin, Chairman of the Hospital Board; and Keith Lieber, Controller. Our audit disclosed no material items that warrant comment at this time.