



FINANCIAL STATEMENTS

DECEMBER 31, 2008 AND 2007

CPAs / ADVISORS



MARGARET MARY COMMUNITY HOSPITAL, INC.

TABLE OF CONTENTS DECEMBER 31, 2008 AND 2007

	Page
Report of Independent Auditors	1
Financial Statements	
Balance Sheets	2
Statements of Operations	3
Statements of Changes in Net Assets	4
Statements of Cash Flows	5
Notes to Financial Statements	6



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REPORT OF INDEPENDENT AUDITORS

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

We have audited the accompanying balance sheets of Margaret Mary Community Hospital, Inc. (Hospital) as of December 31, 2008 and 2007, and the related statements of operations, changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of December 31, 2008 and 2007, and the results of its operations, changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Blue & Co., LLC

March 6, 2009

MARGARET MARY COMMUNITY HOSPITAL, INC.

BALANCE SHEETS DECEMBER 31, 2008 AND 2007

ASSETS		
	2008	2007
Current assets		
Cash and cash equivalents	\$ 1,652,899	\$ 2,516,960
Investments	17,942	17,307
Patient accounts receivable, net of uncollectible allowance of \$2,865,348 in 2008 and \$1,892,759 in 2007	7,032,741	8,341,442
Other receivables	117,322	177,343
Inventories	702,666	718,460
Prepaid expenses	437,404	342,232
Current portion of assets whose use is limited	1,121,972	625,000
Total current assets	11,082,946	12,738,744
Assets whose use is limited		
Board designated for capital improvements	20,334,784	20,651,017
Board designated for retirement plan	544,601	484,831
Held by trustee for capital improvements	7,250,450	-0-
	28,129,835	21,135,848
Less current portion	1,121,972	625,000
Assets whose use is limited - noncurrent	27,007,863	20,510,848
Property and equipment, net	46,620,534	42,821,206
Bond issue costs, net	338,576	280,340
Total assets	\$ 85,049,919	\$ 76,351,138
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable	\$ 2,901,688	\$ 1,131,314
Accrued wages and related liabilities	2,616,445	2,410,323
Estimated third-party settlements	858,066	975,998
Current portion of long-term debt	838,759	625,000
Total current liabilities	7,214,958	5,142,635
Derivative liability	3,262,339	355,397
Long-term debt, less current portion	27,750,675	19,620,000
Total liabilities	38,227,972	25,118,032
Net assets		
Unrestricted	46,766,419	51,125,637
Temporarily restricted	55,528	107,469
Total net assets	46,821,947	51,233,106
Total liabilities and net assets	\$ 85,049,919	\$ 76,351,138

See accompanying notes to financial statements.

MARGARET MARY COMMUNITY HOSPITAL, INC.

STATEMENTS OF OPERATIONS YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
Unrestricted revenue, gains and other support		
Patient service revenue	\$ 54,772,770	\$ 54,178,172
Gains, primarily investment income	1,465,247	1,707,606
Other revenue	375,826	485,746
Net assets released from restrictions	115,376	61,762
Total revenue, gains and other support	56,729,219	56,433,286
Expenses		
Salaries and wages	20,039,015	18,379,352
Employee benefits	6,775,566	7,027,258
Physician fees	2,198,073	2,024,839
Medical and surgical supplies	6,120,811	6,196,666
Other supplies	373,944	382,993
Purchased services	4,177,515	3,945,297
Equipment rentals	81,549	85,620
Food	272,316	319,413
Utilities	1,095,709	1,028,116
Bad debts	4,275,020	3,875,764
Insurance	483,314	498,360
Depreciation and amortization	4,257,431	4,076,669
Interest	1,032,867	857,902
Other	991,161	961,033
Total expenses	52,174,291	49,659,282
Excess revenues over expenses from continuing operations	4,554,928	6,774,004
Other changes in unrestricted net assets		
Unrealized loss on investments	(6,007,204)	(1,034,552)
Unrealized loss on derivative	(2,906,942)	(562,945)
Total other changes in unrestricted net assets	(8,914,146)	(1,597,497)
Change in unrestricted net assets before discontinued operations	(4,359,218)	5,176,507
Loss from operations of discontinued component	-0-	801,309
Change in unrestricted net assets	\$ (4,359,218)	\$ 4,375,198

See accompanying notes to financial statements.

MARGARET MARY COMMUNITY HOSPITAL, INC.

STATEMENTS OF CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
Unrestricted net assets		
Change in unrestricted net assets	\$ (4,359,218)	\$ 4,375,198
Temporarily restricted net assets		
Contributions	63,435	49,380
Net assets released from restrictions	<u>(115,376)</u>	<u>(61,762)</u>
Change in temporarily restricted net assets	<u>(51,941)</u>	<u>(12,382)</u>
Change in net assets	(4,411,159)	4,362,816
Net assets		
Beginning of year	<u>51,233,106</u>	<u>46,870,290</u>
End of year	<u>\$ 46,821,947</u>	<u>\$ 51,233,106</u>

See accompanying notes to financial statements.

MARGARET MARY COMMUNITY HOSPITAL, INC.

STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
Operating activities		
Change in net assets	\$ (4,411,159)	\$ 4,362,816
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation and amortization	4,257,431	4,076,669
Depreciation included in discontinued operations	-0-	3,800
Bad debts	4,275,020	3,875,764
Realized and unrealized loss on investments	6,371,729	1,244,170
Unrealized loss on derivative	2,906,942	562,945
Loss on disposal of property and equipment	59,466	74,785
Change in operating assets and liabilities		
Patient accounts receivable	(2,966,319)	(4,499,330)
Other receivables	60,021	141,427
Inventories	15,794	(152,347)
Prepaid expenses	(95,172)	11,518
Accounts payable	648,570	(112,179)
Accrued wages and related liabilities	206,122	302,370
Estimated third-party settlements	(117,932)	370,800
Net cash flows from operating activities	11,210,513	10,263,208
Investing activities		
Proceeds from sale of investments	159,468	10,453,778
Purchases of investments	(13,525,184)	(16,257,281)
Proceeds from sale of property and equipment	3,400	2,052
Additions to property and equipment	(6,984,628)	(3,444,100)
Other changes in investing activities	(635)	(941)
Net cash flows from investing activities	(20,347,579)	(9,246,492)
Financing activities		
Payments for bond issuance costs	(71,429)	-0-
Proceeds from long-term debt	9,000,000	-0-
Principal payments on long-term debt	(655,566)	(605,000)
Net cash flows from financing activities	8,273,005	(605,000)
Net change in cash and cash equivalents	(864,061)	411,716
Cash and cash equivalents		
Beginning of year	2,516,960	2,105,244
End of year	\$ 1,652,899	\$ 2,516,960
Noncash investing, capital and related financing activities		
Property and equipment included in liabilities	\$ 1,121,804	\$ -0-
Supplemental disclosure of cash flows information		
Cash paid for interest net of amounts capitalized of \$74,022 in 2008 and \$-0- in 2007	\$ 1,032,867	\$ 857,902

See accompanying notes to financial statements.

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

1. SIGNIFICANT ACCOUNTING POLICIES

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

Organization

The Hospital, located in Batesville, Indiana, is a not-for-profit acute care hospital also providing home health services. The Hospital discontinued providing long-term care services in 2006. The Hospital provides inpatient, outpatient, and other ancillary services to the residents of Ripley and surrounding counties. Admitting physicians are primarily practitioners in the local area.

Use of Estimates

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

Charity Care

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

Patient Accounts Receivable and Revenues

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

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

The Hospital is a provider of services to patients entitled to coverage under Titles XVIII and XIX of the Health Insurance Act (Medicare and Medicaid). In 2006, the Hospital was granted Critical Access Status by Medicare and is paid for Medicare services based upon a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at an interim rate, with final settlement determined after submission of annual cost reports.

Differences between the total program billed charges and the payments received are reflected as deductions from revenue. At the Hospital's year-end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients.

The difference between computed reimbursement and interim reimbursement is reflected as a receivable from or payable to the third-party program. The year end cost reports filed with the Medicare and Medicaid programs through December 31, 2006 have been audited by these programs and any resulting differences are reflected in the financial statements. During 2008 and 2007, the Hospital recognized decrease in net assets of approximately \$400,000 and \$-0-, respectively, due to the differences between original estimates and subsequent revisions for the final settlement of cost reports.

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

A summary of patient service revenue for 2008 and 2007 follows:

	<u>2008</u>	<u>2007</u>
Inpatient routine	\$ 6,095,602	\$ 5,686,495
Inpatient ancillary	14,770,521	13,462,241
Outpatient services	<u>70,311,544</u>	<u>68,523,939</u>
	91,177,667	87,672,675
Less provisions for		
Contractual adjustments under third-party reimbursement programs	35,529,665	32,594,943
Charity care	<u>875,232</u>	<u>899,560</u>
Total provisions	<u>36,404,897</u>	<u>33,494,503</u>
Patient service revenue	<u>\$ 54,772,770</u>	<u>\$ 54,178,172</u>

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Investments

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

Inventories

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

Property and Equipment and Provision for Depreciation

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

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

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

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

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor restrictions about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service. During 2008 and 2007, there were no gifts of long-lived assets with restrictions.

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Assets Whose Use is Limited

Assets whose use is limited by internal board designation includes cash and cash equivalents, accrued interest receivable, and marketable securities. Marketable securities include investments in fixed income mutual funds, equity mutual funds and common stock. Such securities are stated at fair market value. Donated securities are recorded at fair market value at the date of the donation.

Assets held by trustee include cash, certificates of deposit and investments for debt service payments and/or capital improvements in compliance with the Indiana Health Facility Financing Authority bond issues described in the long-term debt note.

The Hospital holds Level 1 investments, in which fair market values are readily determinable using quoted prices in active markets for identical assets as determined by FAS 157: *Fair Value Measurements*. Level 2 investments fair market values are determined by significant other observable inputs.

Bond Issue Costs

Unamortized bond issue costs as of December 31, 2008 and 2007 were \$338,576 and \$280,340. Bond issue costs are amortized over the life of the bonds. Accumulated amortization as of December 31, 2008 and 2007 was \$52,770 and \$39,577, respectively. Amortization expense for the years ending December 31, 2009 through 2015 is approximately \$27,000 per year.

Temporarily Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital has been limited by external sources for a specific time period or purpose. When a restriction expires, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statements of operations and changes in net assets as net assets released from restrictions. Restrictions that are met within the year of receipt are reflected with unrestricted net assets. As of December 31, 2008 and 2007, temporarily restricted net assets were \$55,528 and \$107,469, respectively. These assets are restricted for scholarships and other Hospital programs.

Excess Revenues Over Expenses

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

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Federal and State Income Taxes

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

Accounting for Uncertainty in Income Taxes

The Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), which clarifies generally acceptable accounting principles for recognition, measurement, presentation and disclosure relating to uncertain tax positions. FIN 48 applies to business enterprises, not-for-profit entities, and pass-through entities, such as S corporations and limited liability companies. As permitted by FIN 48 (as amended), the Hospital elected to defer the application of FIN 48 until issuance of its December 31, 2009 financial statements. For financial statements covering periods prior to calendar 2009, the Hospital evaluates uncertain tax positions in accordance with existing generally accepted accounting principles and makes such accruals and disclosures as might be required thereunder.

Costs of Borrowing

Except for capital assets acquired through gifts, contributions or capital grants, interest cost on borrowed funds, as well as interest earned on those funds, during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Capitalized interest cost was \$74,022 and \$-0- in 2008 and 2007, respectively, and capitalized interest income was \$33,663 and \$-0- in 2008 and 2007, respectively.

Advertising Costs

The Hospital's policy is to expense advertising costs when the advertising first takes place. Advertising expenses were \$156,585 and \$177,574 in 2008 and 2007, respectively.

Statements of Cash Flows

For the purposes of reporting cash flows, cash and cash equivalents include all cash held in checking and money market accounts available for operating purposes with original maturities of 90 days or less. Cash paid for interest for 2008 and 2007 was \$1,032,867 and \$857,902, respectively.

Reclassification

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

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

2. CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy based on established rates. Charity care charges foregone during 2008 and 2007 were \$875,232 and \$899,560, respectively.

3. FAIR VALUE OF FINANCIAL INSTRUMENTS

Statement on Financial Accounting Standards No. 157, Fair Value Measurements (as amended), requires certain disclosures regarding the fair value of financial instruments. Financial instruments held by the Hospital impacted by this pronouncement include the Hospital's investments and assets whose use is limited which are measured using quoted prices in active markets and significant other observable inputs.

The Hospital partially adopted the provisions of FAS 157 for fiscal year 2008, but will delay adoption of non-financial assets and non-financial liabilities covered by FASB Staff Position No. FAS 157-2. This Staff Position permits companies to partially defer the effective date of FAS 157 for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis, until fiscal year 2009.

When fully adopted, the Hospital will apply the provisions of FAS 157-2 to certain non-financial assets and liabilities and is currently evaluating the impact of the full adoption of this statement on the changes in net assets and financial position.

Fair values of financial instruments as of December 31, 2008 are as follows:

	Total	Quoted market prices for identical assets Level 1	Significant other observable inputs Level 2	Significant unobservable inputs Level 3
Investments				
Mutual funds - fixed income	\$ 17,942	\$ 17,942	\$ -0-	\$ -0-
Assets whose use is limited				
Mutual funds - fixed income	\$ 9,159,979	\$ 9,159,979	\$ -0-	\$ -0-
Mutual funds - equities	\$ 9,722,644	\$ 9,722,644	\$ -0-	\$ -0-
Common stock	\$ 232,547	\$ 232,547	\$ -0-	\$ -0-
Certificates of deposit	\$ 7,250,450	\$ -0-	\$ 7,250,450	\$ -0-

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

In addition to quoted market prices in active markets, valuation techniques included:

- Level 2-estimates on similar investments
- Level 3-management's estimate of the present value of future cash flows arising from the arrangement

4. INVESTMENTS

Investments are recorded at fair market value and consist of the following as of December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Mutual funds - fixed income	<u>\$ 17,942</u>	<u>\$ 17,307</u>

5. PROPERTY AND EQUIPMENT

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

	<u>2008</u>	<u>2007</u>
Land	\$ 2,371,158	\$ 2,371,158
Land improvements	372,269	375,610
Buildings and improvements	47,932,112	47,611,294
Fixed equipment	5,734,199	5,691,265
Movable and minor equipment	<u>24,750,660</u>	<u>22,414,684</u>
	81,160,398	78,464,011
Less accumulated depreciation	<u>40,826,730</u>	<u>36,734,052</u>
	40,333,668	41,729,959
Construction in progress	<u>6,286,866</u>	<u>1,091,247</u>
	<u>\$ 46,620,534</u>	<u>\$ 42,821,206</u>

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

6. ASSETS WHOSE USE IS LIMITED

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

	2008	2007
Cash and cash equivalents	\$ 1,715,446	\$ 1,384,104
Accrued interest receivable	48,769	49,073
Marketable securities	19,115,170	19,702,671
Certificates of deposit	7,250,450	-0-
	\$ 28,129,835	\$ 21,135,848

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

	2008		2007	
	Market Value	Cost	Market Value	Cost
Mutual funds - fixed income	\$ 9,159,979	\$ 9,150,619	\$ 9,283,460	\$ 9,115,097
Mutual funds - equities	9,722,644	16,307,969	9,631,858	10,924,497
Common stock	232,547	396,069	787,353	396,069
	\$ 19,115,170	\$ 25,854,657	\$ 19,702,671	\$ 20,435,663

The following is a reconciliation of gains and losses and investment income for 2008 and 2007:

	2008	2007
Interest and dividends	\$ 1,829,772	1,917,224
Realized loss on investments	(364,525)	(209,618)
	\$ 1,465,247	\$ 1,707,606
Unrealized gain (loss) on investments	\$ (6,007,204)	\$ (1,034,552)

The following schedules summarize the fair value of securities included in assets whose use is limited that have gross unrealized losses (the amount by which historical cost exceeds the fair value) as of December 31, 2008 and 2007. The schedules further segregate the securities that have been in a gross unrealized position as of December 31, 2008 and 2007, for less than twelve months and those for twelve months or more. The gross unrealized losses of less than twelve months are a reflection of the normal fluctuations of the market and are therefore considered temporary. The gross unrealized losses of twelve months or longer are reflective of

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

current market fluctuations. The majority of the decline is attributable to securities which industry experts expect recovery in the short-term future.

The decline in value is determined by management to be temporary, and unrealized losses have not been reclassified to realized losses as of December 31, 2008 and 2007:

Description of securities	December 31, 2008					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Common Stocks	\$ -0-	\$ -0-	232,547	163,522	\$ 232,547	\$ 163,522
Mutual funds	-0-	-0-	9,722,645	6,585,323	9,722,645	6,585,323
Total	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ 9,955,192</u>	<u>\$ 6,748,845</u>	<u>\$ 9,955,192</u>	<u>\$ 6,748,845</u>

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

7. DERIVATIVE AGREEMENT

In 2004, the Hospital entered into a “cash flow hedge interest rate swap” agreement with a financial institution. The Hospital pays a fixed interest rate (3.48% at December 31, 2008 and 2007) and the financial institution pays a variable interest rate (.79% and 3.51% as of December 31, 2008 and 2007, respectively) over the term of the agreement.

The Hospital’s objective is to provide protection against market driven increases in variable interest rates. The fair value of the agreement was determined by the financial institution using the present value of the estimated projected cash flows. The Hospital is in a liability position as of December 31, 2008 due to the present value of its estimated projected cash flows being more than the financial institution’s present value of estimated projected cash flows.

The swap agreement matures on December 1, 2029, and contains an outstanding notional amount of \$20,000,000 with a 3.48% fixed rate of interest. The Hospital recorded a derivative liability of \$3,262,339 and \$355,397 as of December 31, 2008 and 2007, respectively. The total derivative loss recognized on the financial statements as other changes in unrestricted net assets was \$2,906,942 and \$562,945 for 2008 and 2007, respectively.

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

8. LONG-TERM DEBT

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

	<u>2008</u>	<u>2007</u>
Indiana Health Facility Financing Authority; dated March 1, 2004, due 2029; Variable Rate Demand Revenue Bonds; Series 2004A-1	\$ 19,620,000	\$ 20,245,000
Indiana Financing Authority Hospital Revenue Bonds Series 2008A; dated October 1, 2008, due 2038	8,969,434 <u>\$ 28,589,434</u>	-0- <u>\$ 20,245,000</u>
Less current portion	<u>838,759</u> <u>\$ 27,750,675</u>	<u>625,000</u> <u>\$ 19,620,000</u>

Annual maturities of long-term debt for the years succeeding December 31, 2008 are as follows:

<u>December 31,</u>	
2009	\$ 838,759
2010	868,296
2011	903,315
2012	933,840
2013	8,900,224
Thereafter	<u>16,145,000</u> <u>\$ 28,589,434</u>

In 2004, the Hospital borrowed from the Indiana Health Facility Financing Authority (the Authority) \$22,000,000 for the construction of an addition to the Hospital facilities. The Authority, created under Indiana Code 5-1-16, provides funds to eligible health facilities for financing capital expenditures. Interest expense is determined monthly based on the actual rate of interest paid by the Authority to its bondholders. The Authority's rate of interest is determined by the Remarketing Agent with due regard to prevailing financial market conditions. The variable rate on the Series 2004 bonds was .79% and 3.51% as of December 31, 2008 and 2007, respectively. The Series 2004 bonds are secured by a letter of credit in the amount of \$19,820,178 as of December 31, 2008 that expires March 15, 2012. The letter of credit is secured by the assignment of the Authority note, which is secured by a

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

pledge of gross revenues. The loan agreement and letter of credit require the Hospital to comply with certain restrictive covenants. Management believes the Hospital is in compliance with the covenants as of December 31, 2008.

If the bonds cannot be remarketed, a liquidity drawing is made under the letter of credit bearing interest at the prime rate plus 2%. Liquidity drawings are due in monthly installments beginning 60 days after the initial draw through the later date of the stated expiration date of the letter of credit or date that would be the due date of the tenth monthly principal payment following the date of the original liquidity draw. For reimbursement drawings other than liquidity drawings, amounts are due on demand.

In 2008, the Hospital borrowed \$9,000,000 under the Indiana Financing Authority Hospital Revenue Bonds, Series 2008A to renovate the emergency services and radiology departments. The Series 2008A bonds can bear interest at fixed rates as determined by daily, weekly, flexible or long modes. The Series 2008A bonds are secured by an interest in the gross revenues of the Hospital.

On October 30, 2008, the Hospital, the Authority and Key Government Finance, Inc. (Key) entered into a Bond Purchase Agreement (Agreement) whereby Key purchased from the Authority all of the Series 2008A Bonds in a private placement. The Agreement provides that Key will hold the Series 2008A Bonds during the Initial Long Mode Period which runs through November 2013. During this Initial Long Mode Period, the Series 2008A Bonds bear interest at the fixed rate long mode (4.93%) for 60 months with principal and interest payments determined using a 25 year amortization schedule. At the end of the Initial Long Mode Period, the Series 2008A Bonds may be converted to another interest rate mode and remarketed to another bondholder or holders or renewed for another Long Mode Period with Key. The Series 2008A Bonds could be converted to another interest rate mode to accommodate market conditions at that time. If the Series 2008A Bonds cannot be remarketed at the end of the Initial Long Mode Period, the Hospital would be subject to payment of the remaining principal of approximately \$7,984,000 at the end of the Initial Long Mode Period.

9. RETIREMENT PLANS

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

In 2003, the Hospital adopted a 457(b) deferred compensation plan that provides for non-elective employer deferrals covering a select group of management or highly compensated individuals. Pension expense was \$567,756 and \$497,091 for 2008 and 2007, respectively.

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

10. CONCENTRATIONS OF CREDIT RISK

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

	<u>2008</u>	<u>2007</u>
Medicare	28%	24%
Medicaid	6%	7%
Blue Cross	16%	16%
Other third-party payors	17%	22%
Self pay	33%	31%
	<u>100%</u>	<u>100%</u>

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

11. COMMITMENTS AND CONTINGENCIES

Self-Funded Health Plan

The Hospital is committed to pay for employees' health care costs. A third-party administrator has been retained to process and present all benefit claims to the Hospital for payment. Under a stop loss agreement, the Hospital is responsible for the funding of all claims and related administrative costs up to \$150,000 per individual per policy year. There is no aggregate limit for the Plan under the stop loss agreement. Group health insurance expense for the years ended December 31, 2008 and 2007 totaled \$4,265,135 and \$4,755,561, respectively.

Estimated Malpractice Costs

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

MARGARET MARY COMMUNITY HOSPITAL, INC.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

Litigation

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

Construction Commitments

The Hospital has committed to construction projects to renovate the Emergency Services and Radiology departments. The estimated amount to complete the projects is approximately \$6,530,000.

Other

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

12. FUNCTIONAL EXPENSES

The Hospital is an acute care hospital also providing long-term care and home health services. The Hospital has provided inpatient, outpatient and other ancillary services to the residents within its geographical region. Expenses related to providing these services for 2008 and 2007 approximate the following:

	<u>2008</u>	<u>2007</u>
Health care services	\$ 45,717,423	\$ 43,513,661
General and administrative	6,456,868	6,145,621
	<u>\$ 52,174,291</u>	<u>\$ 49,659,282</u>

13. DISCONTINUED OPERATIONS

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