TIPTON COUNTY MEMORIAL HOSPITAL

COMBINED FINANCIAL STATEMENTS

AND

SUPPLEMENTARY INFORMATION

DECEMBER 31, 2008 AND 2007

CPAs / ADVISORS

blue

TIPTON COUNTY MEMORIAL HOSPITAL

TABLE OF CONTENTS
DECEMBER 31, 2008 AND 2007

CPAs / ADVISORS

blue

Blue & Co., LLC / One American Square, Suite 2200 / Box 82062 / Indianapolis, IN 46282
main 317.633.4705 fax 317.633.4889 email blue@blueandco.com

REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Tipton County Memorial Hospital
Tipton, Indiana

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

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

In our opinion, the combined financial statements referred to above, present fairly, in all material respects, the combined 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.

Management's discussion and analysis, on pages i through x, is not a required part of the basic combined financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of 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.

Blue & Co., LLC

April 30, 2009

REQUIRED SUPPLEMENTARY INFORMATION

TIPTON COUNTY MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2008 AND 2007

Tipton County Memorial Hospital's (the Hospital) annual combined financial statement presents background information and management's discussion and analysis of the Hospital's financial performance during the year ended December 31, 2008.

This section includes a discussion and analysis of activities as a result of the Hospital operations. Hospital facilities include Tipton County Memorial Hospital, a 25 bed (25 bed acute care, Medical/Surgical/ICU) unit and The Tipton County Memorial Hospital Foundation. All facilities are located in Tipton, Indiana and serve Tipton County and the surrounding counties in north central Indiana.

In 2008, the Hospital experienced 7,228 acute care patient days and 48,952 outpatient visits.

The Hospital bases its priorities and sets performance goals based on its Mission Statement, Core Strategies, and Key Financial Indicators.

MISSION STATEMENT

The Hospital is dedicated to being the community based center of high quality, compassionate health services and education to all citizens of Tipton County and neighboring areas, in a financially responsible manner.

CORE STRATEGIES

The Hospital has identified the following core strategies in a continued effort to fulfill our mission:

- Striving to become the regional benchmark for demonstrated outcomes,
- Service excellence,
- Cost effectiveness,
- Expanding and solidifying relationship with physicians,
- Working toward the goals of increasing primary care base/system entry points throughout the region and strengthening and differentiating select clinical services,
- To serve as the leader for a community-based approach to promote improved services health status while continuing a management agreement with Clarian Health Partners and applying best practices,

- The Hospital also strives to manage both human and material resources to assure sound economies of operations, optimum employment practices, and a reasonable return on investment.

The Hospital's goals are measured by set success indicators, which help assure accountability in providing the best practice and demonstrate quality outcomes for patients.

FINANCIAL INDICATORS - PERFORMANCE

The Hospital strives to offer quality, compassionate, and advanced medical care as indicated in the above performance measures, and works to balance those objectives with sound financial performance.

The accompanying hospital financial report consists of three statements – a Balance Sheet, Statement of Operations and Changes in Net Assets, and a Statement of Cash Flows. These reports should be reviewed in conjunction with the following discussion and analysis.

Selected Financial and Statistical Data, for the Year Ended December 31, 2008, is shown on the following page and the Management's Discussion and Analysis (MD & A) should be reviewed together with the financial statements included with this report.

FINANCIAL HIGHLIGHTS

During 2008, the Hospital made capital acquisitions and operational improvements as follows:

- January: Hospital appointed Anne Van Epern, Administrator of the Central Indiana Physicians Alliance (CIPA).
- February: Feb 8th, Hospital had an open house for the new Emergency Department, Radiology Department, Registration/Communication Department, as well a new Financial Counselor office, Lab blood draw area, and new classrooms.
- March: Hospital opened The Rehabilitative & Orthopedic Centers of Indiana office in Westfield, Indiana, with Dr Kevin Condict, MD on site to see patients.
- May: Hospital celebrates National Hospital week with 41 associates receiving service awards.
- May: Hospital announces the opening of a new Family Practice office in the Medical Arts Building with Dr Carl Pafford, MD as the new Family Practice physician.

- June: Tipton Hospital announces the opening of the Riley Safety Store at Tipton Hospital.
- June: Tipton Hospital dedicated the new Memorial Garden on June 14, 2008
- August: Tipton Hospital Board of Trustees along with County Leaders unanimously passed resolution to enter into a long term relationship with Clarian Health.
- August: Tipton Hospital Oncology department received the 3 year American College of Surgeons approval with commendations on July 10^{th}.
- August: Tipton Hospital announces Becky Bennet joins the Hospital team as manager of Health Information Services.
- September: Tipton Hospital announces Dr Destry Lambert, MD has joined employment of Tipton Hospital and CIPA.
- September: Tipton Hospital Foundation has a Barn Dance/Auction as a fundraiser at the Kelly's Round Barn
- October: Tipton Hospital announces the opening of a new Family Practice office in Cicero, Indiana with Dr. Richard Hayes, MD, being the Family Practice physicians. The new office is known as Clarian Health Cicero, and also includes orthopedics, cardiology, and pain medicine.
- October: The new cardiologist group, Health Partners of Indiana, LLC, from Clarian Health Partners began seeing cardiology patients at Tipton Hospital.
- November: Tipton Hospital and Tipton Hospital Foundation begin Caring Hearts Coat Drive to donate coats to needy individuals.
- November: Miller Health System moved the 50 LT Care beds from Autumnwood Extended Care to Miller's new facility as agreed with Tipton Hospital.
- December: Tipton Hospital announces that Clarian Bariatric will begin seeing patients at Clarian Health Cicero
- December: Tipton Hospital purchases the medical office owned by Dr. Mike Harper, MD.
- December: Tipton Hospital announces that Dr Mike Harper will be employed by CIPA, starting January 1, 2009, as well as Dr. Lori Wisely, MD, in the January – February time frame.
- December: Tipton County Memorial Hospital completed the legal documents to become Tipton Hospital, Inc (501(c) 3 Not for Profit) on January 1, 2009

USING THIS ANNUAL REPORT

The Hospital's annual combined financial reports consist of three statements – a Balance Sheet, a Statement of Operations and Changes in Net Assets, and a Statement of Cash Flows. These combined financial statements and related notes provide information regarding the Hospital activities, including resources that are restricted for specific purposes by contributors, grantors, and other third parties.

THE BALANCE SHEET AND THE STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

The analysis of Hospital finances begins herein. One of the most important questions asked about the Hospital's financial position is, "Is the Hospital better or worse off as a result of the year's activities?" The Balance Sheet and the Statement of Operations and Changes in Net Assets report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report changes in the Hospital's net assets. A net asset – the difference between assets and liabilities – is one measure of the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are an indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in the Hospital's patient volume and quality measures and other economic factors need to be considered when assessing the overall health of the Hospital.

THE STATEMENT OF CASH FLOWS

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

THE HOSPITAL'S NET ASSETS

The Hospital's net assets are the difference between its assets and liabilities reported on the Balance Sheet on page 3. The Hospital's net assets decreased over the past year by $2,050,306 or 8.2% in 2008. In 2007, net assets increased by $1,757,020 or 7.6%. The Hospitals net assets are detailed in the following table:

	2008	2007
ASSETS		
Current assets	$ 9,827,126	$ 10,736,084
Capital assets, net	38,357,294	27,143,893
Other noncurrent assets	8,854,959	18,547,506
Total assets	$ 57,039,379	$ 56,427,483
LIABILITIES		
Long-term debt outstanding	$ 25,978,761	$ 26,290,500
Other current and noncurrent liabilities	8,161,392	5,187,451
Total liabilities	$ 34,140,153	$ 31,477,951
NET ASSETS		
Invested in capital assets, net of related debt	$ 11,518,404	$ 8,642,286
Restricted		
Held by trustee	-0-	8,588,421
Unrestricted	11,380,822	7,718,825
Total net assets	$ 22,899,226	$ 24,949,532

Certain significant changes in the Hospital's assets included the increase in capital assets as a result of the construction in progress of $11,506,002 as part of the existing building program. The Hospital also saw a decrease in non-current assets of $9,692,547, which represents payments from the 2006 bond issue. The Hospital's liabilities increased $2,662,202 as a result of the increase in outstanding equipment purchases at year end (pending opening of new project in January 2009) and the increase in the Bond Swap (derivative liability).

OPERATING RESULTS AND CHANGES IN THE HOSPITAL'S NET ASSETS

In 2008, the Hospital's net assets decreased by $2,050,306 as shown in the next table. This decrease is made up of various different components, and will be further explained as operating results and changes in net assets are discussed.

Operating Income

The summary component of overall changes in the Hospital's net assets is its operating income – generally, the difference between net patient services revenue plus the other operating revenue minus the expenses incurred to perform those services. During 2008, the Hospital had an operating gain of $157,403 compared to $1,255,726 gain in 2007; (note 2007 has been reclassified to show a discontinued operation gain of $41,273 on a separate line below operating income from continuing operations. In 2008, the Hospital saw the operating revenue (net patient revenue plus other operating revenue) increase $4,408,826 or 12.9% over the 2007 level. The Hospital saw gross inpatient revenues (charges) increase $4,797,427 or 28.4% over 2007, as well as gross outpatient revenues (charges) increase by $7,913,051 or 19.0% in 2008, more than the 2007 year. Many departments saw increases in activity in 2008 and a few saw decreases in 2008. The Hospital had 715 or 11.0% more acute care patient days (Med/Surg, and ICU) in 2008 compared to 2007; or, 19.8 patients per day in 2008, compared to 17.8 patients per day in 2007. With the increase in total days (Acute Care) of 715, more supplies, food and drugs were used to care for these patients. On the outpatient side of the business, we saw increased charges in Operating Room/GI Lab, MRI, CT Scans, Nuclear Medicine, Ultrasound, Radiology, Lab, Emergency Department, Rehab Services, Oncology, and the (in house) Sleep Lab Program.

The contractual allowance increased by $6,309,542, which was 43.1% of gross revenue for 2008, compared to 41.6% in 2007. The contractual allowance is the difference between hospital charges, and what is paid by Medicare, Medicaid, and other third party payors (such as Blue Cross, Sagamore, Aetna, etc.). The Medicare and Medicaid programs set the rates for reimbursement to hospitals and other healthcare providers; in contrast the Hospital negotiates the various contracts with the other third parties – Managed Care Agreements. The Hospital had bad debts of $2,634,051 or 3.7% of gross revenue compared to $1,411,188 or 2.4% of gross revenue in 2007. The Hospital's charity care (for 2008 was $1,389,303) increased $510,527 or 58.1% over the 2007 level.

TIPTON COUNTY MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2008 AND 2007

	2008	2007
Operating revenues		
Net patient service revenue	$ 36,556,263	$ 31,888,717
Other operating revenue	2,046,251	2,304,971
Total operating revenue	38,602,514	34,193,688
Operating expenses		
Salaries and benefits	20,683,047	18,167,804
Medical supplies and drugs	5,680,612	4,326,750
Depreciation and amortization	2,320,358	1,725,792
Other operating expenses	9,761,094	8,717,616
Total operating expenses	38,445,111	32,937,962
Operating income from continuing operations	157,403	1,255,726
Nonoperating income (expenses)		
Investment income (loss)	(999,455)	952,927
Interest expense	(711,371)	(15,493)
Unrealized loss on interest rate swap	(590,995)	(279,010)
Payments related to the agency agreement	-0-	(198,403)
Total nonoperating income (expenses)	(2,301,821)	460,021
Change in net assets before discontinued operations	(2,144,418)	1,715,747
Income from operations of discontinued components	94,112	41,273
Changes in net assets	$ (2,050,306)	$ 1,757,020

The Hospital's mix of receivables is as follows:	2008	2007
Medicare	33%	36%
Medicaid	4%	4%
Blue Cross	21%	17%
Commercial	24%	25%
Self-pay	18%	18%
Total	100%	100%

The Hospital's net patient service revenue increased $4,667,546 or 14.6% in 2008, compared to 2007.

The Hospital's operating expenses increased by $5,507,149 or 16.7% over 2007.

The increase in inpatient days (715) and with an increase in outpatient visits (3,687), and increase in surgeries (96) over 2007, had large effect on orthopedic supplies and oncology drugs. The salaries and benefits increased $2,515,243 or 13.8% over 2007 levels; with approximately 3% to maintain competitive wage rates; the employment of physicians to cover the Emergency Department, OB/GYN office practice and Pediatric office practice and three Family Practice offices, and an Orthopedic office; the increase in health insurance cost for associates, as well as increase in employer incentive matching (limit 1%) of the 403B benefit. The Hospital also has seen an increase in provision for bad debts which has increased from 2.4% in 2007 to 3.7% of gross revenue.

In 2008, the Hospital is no different than other surrounding hospitals in that we are seeing more individuals with more self pay balances due to higher deductibles or little or no insurance coverage.

NON-OPERATING INCOME, CONTRIBUTION, AND ENDOWMENTS

Non-operating income consists of an investment loss of $999,455 and donations from the Tipton County Memorial Hospital Auxiliary of hours worked only; they saved their proceeds to donate the new Baby Grand player piano (December, 2007) in the South Lobby. The Hospital also receives a semiannual interest income distribution, which is included in the investment income from the Lebo Endowment (managed by the Tipton County Foundation). Also, starting in 2004, the interest expense is reported under Non-operating Income (expense) and was $(711,371) in 2008 compared to $(15,493) in 2007. See the Debt Section under this report for further discussion regarding interest expense.

THE HOSPITAL'S CASH FLOW

The Hospital's cash flow decreased throughout the 2008 period, as the Medicare per diem rate for the acute care side of the Hospital saw little change, even though the Hospital patient accounting staff continued to gain efficiency in the billing and collection process with the current computer system. The net change in cash was a decrease of $618,805 in 2008 compared with a decrease of $52,537 in 2007. The decrease in cash position is a result of the acquisition and construction of capital assets, purchase of physician practices and start up costs of Central Indiana Physician Alliance (CIPA), even though the Hospital's days of revenue in accounts receivable at 50 days, is well below the State average of around 55 - 60 days for a similar sized hospital.

CAPITAL ASSET AND DEBT ADMINISTRATION

At the end of 2008, the Hospital had $38,357,294 invested in capital assets, net of accumulated depreciation, as shown in a previous table and detailed in Note 9 to the financial statements, compared to $27,143,893 in 2007. In 2008, the Hospital purchased new equipment totaling $922,879 of which most was used to open the Westfield and Cicero medical practices. During 2008, the Hospital disposed of equipment of $751,268, which was fully depreciated. Those items disposed of were throughout the Hospital and had little net book value. The Hospital also increase building value with the addition of the storage building in Tipton, as well as spending $11,506,002 on construction in progress for the 2006 Expansion Project including (architect and construction costs) which started in the spring of 2006.

In the future the Hospital believes it is more economical in certain cases to lease certain high–cost clinical and diagnostic equipment than to purchase. Leasing spreads the cost over a 48 or 60 month time period, when many times the equipment may only have a four or five year expected life, due to advances in technology changes/enhancements, and allow the hospital to remain current with the changing technology.

DEBT

At year end, the Hospital had $26,838,890 in long term debt, consisting of 2006 Series A (Tax Free) Bonds of $24,200,000, 2006 Series B (Taxable) Bonds of $1,925,000, backed by a letter of credit from Fifth Third Bank (to provide credit enhancement and liquid support for both 2006 issues). The Hospital also has a capital lease (Trane Co. – Chiller Lease and Vitros (Lab) Lease with Leasing Associates of Barrington). The Hospital defeased the 1997 Series A and B Bonds and the 2002 Series Bonds, in June 2006.

In addition, the Hospital has a $750,000 line of credit thru Harris Bank, but this line of credit has never been drawn upon. Also, the Hospital had a $3,000,000 line of credit (bridge loan) with Harris Bank, to use to continue the construction of the 2nd and 3rd floor build out. At December 31, 2008, the hospital had an outstanding balance of \$1,038,505. See Note 12 Line of Credit (notes to the financial statements) for further information.

OTHER ECONOMIC FACTORS

The Hospital sees little changes in the primary service area (county population is expected to remain static over the next few years). However, the Hospital must continue to increase its market share in the Tipton service area, provide high quality care, in a sound fiscal manner to maintain positive financial results, by opening offices in Westfield and Cicero. Currently, the Hospital is the second largest employer in the county with 323 paid FTE's (full time equivalent) at year end.

CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional information, contact the Hospital's Financial Management, at Tipton County Memorial Hospital, 1000 S. Main St., Tipton, IN 46072, Michael Harlowe, President and CEO, Vernon Schmaltz, VP – Finance/CFO.

TIPTON COUNTY MEMORIAL HOSPITAL

COMBINED BALANCE SHEETS
DECEMBER 31, 2008 AND 2007

ASSETS

	2008	2007
Current assets		
Cash and cash equivalents	$ 2,258,044	$ 2,694,433
Certificates of deposit	99,516	282,939
Assets limited as to use	869,338	808,737
Patient accounts receivable, net of allowance for doubtful accounts of $1,146,542 and $780,468 for 2008 and 2007, respectively	5,003,015	4,701,155
Other receivables	6,520	241,300
Estimated third-party settlements	-0-	616,241
Supplies and other current assets	1,590,693	1,391,279
Total current assets	9,827,126	10,736,084
Assets limited as to use		
Board designated	9,205,168	10,151,186
Funds held by trustee	-0-	8,588,421
Total assets limited as to use	9,205,168	18,739,607
Assets limited as to use for current obligations	(869,338)	(808,737)
Noncurrent assets limited as to use	8,335,830	17,930,870
Capital assets, net	38,357,294	27,143,893
Other assets	519,129	616,636
Total assets	$ 57,039,379	$ 56,427,483

See accompanying notes to combined financial statements.

TIPTON COUNTY MEMORIAL HOSPITAL

COMBINED BALANCE SHEETS
DECEMBER 31, 2008 AND 2007

LIABILITIES AND NET ASSETS

	2008	2007
Current liabilities		
Line of credit	$ 1,038,505	$ -0-
Current portion of long-term debt	860,129	799,528
Accounts payable and accrued expenses	2,551,757	1,421,730
Accrued payroll and related liabilities	2,002,977	2,041,120
Estimated third-party settlements	254,818	-0-
Other current liabilities	148,157	150,619
Total current liabilities	6,856,343	4,412,997
Long-term liabilities		
Interest rate swap liability	1,234,582	643,587
Other long-term liabilities	70,467	130,867
Capital lease obligations	317,699	243,779
Revenue bonds payable	25,661,062	26,046,721
Total long-term liabilities	27,283,810	27,064,954
Total liabilities	34,140,153	31,477,951
Net assets		
Invested in capital assets net of related debt	11,518,404	8,642,286
Restricted		
Held by trustee	-0-	8,588,421
Unrestricted	11,380,822	7,718,825
Total net assets	22,899,226	24,949,532
Total liabilities and net assets	$ 57,039,379	$ 56,427,483

See accompanying notes to combined financial statements.

TIPTON COUNTY MEMORIAL HOSPITAL

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

	2008	2007
Operating revenue		
Net patient service revenue	$ 36,556,263	$ 31,888,717
Other	2,046,251	2,304,971
Total operating revenue	38,602,514	34,193,688
Operating expenses		
Salaries and benefits	20,683,047	18,167,804
Medical professional fees	624,996	285,075
Other professional fees	3,340,515	3,207,682
Medical supplies and drugs	5,680,612	4,326,750
Other supplies	1,029,966	1,032,766
Depreciation and amortization	2,320,358	1,725,792
Insurance	472,871	533,722
Other	4,292,746	3,658,371
Total operating expenses	38,445,111	32,937,962
Operating income from continuing operations	157,403	1,255,726
Nonoperating income (expense)		
Investment income (loss)	(999,455)	952,927
Interest expense	(711,371)	(15,493)
Unrealized loss on interest rate swap	(590,995)	(279,010)
Payment related to the agency agreement	-0-	(198,403)
Total nonoperating income	(2,301,821)	460,021
Change in net assets before discontinued operations	(2,144,418)	1,715,747
Income from operations of discontinued components	94,112	41,273
Change in net assets	(2,050,306)	1,757,020
Net assets, beginning of year	24,949,532	23,192,512
Net assets, end of year	$ 22,899,226	$ 24,949,532

See accompanying notes to combined financial statements.

TIPTON COUNTY MEMORIAL HOSPITAL

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

	2008	2007
Operating activities		
Cash received from patient services	$ 36,376,146	$ 31,934,511
Cash paid to employees	(20,721,094)	(18,164,576)
Cash paid to vendors and suppliers	(13,939,404)	(13,645,999)
Other receipts, net	2,035,396	2,516,046
Net cash flows from operating activities	3,751,044	2,639,982
Capital and related financing activities		
Acquisition and construction of capital assets	(12,807,933)	(11,679,385)
Proceeds from sale of capital assets	48,880	18,751
Proceeds from line of credit	1,038,505	-0-
Interest on long term debt	(711,371)	(15,493)
Proceeds from long term debt	341,000	-0-
Principal paid on long term debt	(814,921)	(124,707)
Payment related to the agency agreement	-0-	(198,403)
Net cash flows from capital and related financing activities	(12,905,840)	(11,999,237)
Investing activities		
Investment income	(999,455)	952,927
Net change from other investing activities	9,535,446	8,353,791
Net cash flows from investing activities	8,535,991	9,306,718
Net change in cash and cash equivalents	(618,805)	(52,537)
Cash and cash equivalents, beginning of year	3,242,167	3,294,704
Cash and cash equivalents, end of year	$ 2,623,362	$ 3,242,167
Reconciliation of cash and cash equivalents		
Cash and cash equivalents in current assets	$ 2,258,044	$ 2,694,433
Cash and cash equivalents in assets limited as to use		
Board designated	365,318	512,782
Held by Trustee	-0-	34,952
Total cash and cash equivalents	$ 2,623,362	$ 3,242,167

See accompanying notes to combined financial statements.

TIPTON COUNTY MEMORIAL HOSPITAL

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

	2008	2007
Reconciliation of operating income to cash flows from operating activities		
Operating income (loss)	$ 157,403	$ 1,255,726
Adjustments to reconcile operating income to net cash flows operating activities		
Depreciation and amortization	2,320,358	1,725,792
Provision for bad debts	2,634,051	1,411,188
Gain on disposal of property	(10,855)	(5,755)
Results from discontinued operations	94,112	41,273
Changes in operating assets and liabilities		
Patient accounts receivable	(2,935,911)	(1,923,999)
Other current assets	32,904	(178,752)
Estimated third-party settlements	871,059	(530,018)
Accounts payable and accrued expenses	626,066	508,426
Accrued payroll and related liabilities	(38,143)	336,101
Net cash from operating activities	$ 3,751,044	$ 2,639,982
Noncash investing, capital and related financing activities		
Capital lease obligation incurred for use of equipment	$ 213,574	$ 182,200
Property additions included in accounts payable	$ 503,961	$ -0-
Supplemental cash flows information		
Cash paid for interest net of amounts capitalized of $274,495 in 2008 and $1,211,216 in 2007	$ 711,371	$ 15,493

See accompanying notes to combined financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Tipton County Memorial Hospital (the 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 to Tipton County and other surrounding counties. The Board of County Commissioners of Tipton 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 Tipton County.

Accounting principles generally accepted in the United States of America require that these financial statements present 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.

Blended Component Units

The Tipton County Memorial Hospital Foundation (the Foundation) is a blended component unit of the Hospital. The primary government appoints a voting majority of the Foundation's board and a financial benefit/burden relationship exists between the Hospital and the Foundation. Although it is legally separate from the Hospital, the Foundation is reported as if it were a part of the Hospital because it provides services entirely or almost entirely to the Hospital. The Foundation is a 501(c)(3) not-for-profit organization. To obtain the separate financials of the Foundation, please contact the Hospital's Financial Management, at Tipton County Memorial Hospital, 1000 S. Main St., Tipton, IN 46072, Michael Harlowe, President and CEO, Vernon Schmaltz, VP – Finance/CFO.

The Foundation's total assets (cash and cash equivalents) as of December 31, 2008 and 2007 were $101,973 and $88,973, respectively. The Foundation's net assets as of December 31, 2008 and 2007 were $101,973 and $88,973, respectively. The Foundation's total program revenue for the years ended December 31, 2008 and 2007 was $53,814 and $55,666, respectively. The Foundation's total program expenses for the years ended December 31, 2008 and 2007 were $40,814 and $41,405, respectively.

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.

Principles of Combination

The accompanying combined financial statements include the accounts of Tipton County Memorial Hospital and its blended component unit, the Foundation. All material intercompany transactions have been eliminated. Because the Foundation's sole purpose is to support the activities of the Hospital, the results of these activities have been combined.

Enterprise Fund Accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

Cash and Cash Equivalents

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

Certificates of Deposit

The certificates of deposit have original maturities of greater than 90 days and are reported at fair value.

Assets Limited As To Use And Investments

Board Designated Funds: This fund includes investments set aside to fund its depreciation expense in order to meet capital equipment replacement needs. It also includes board designated funds set aside by the Hospital for other board directed purposes.

Trustee Held Assets: The Hospital funds certain debt requirements which are held by the trustee in accordance with the trust indenture.

Assets limited as to use that are required for obligations classified as current liabilities are reported in current assets

Patient Accounts Receivable and 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. 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.

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

Federal and State Income Taxes

The Hospital is a governmental instrumentality organized under Title 16, Article 12, of the Indiana statutes. The Hospital is exempt from federal income tax as a unit of local government.

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.

Advertising

The Hospital expenses advertising costs as they are incurred. Advertising expenses for the years ended December 31, 2008 and 2007 were $332,331 and $280,358, respectively.

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 determined to qualify as charity care, they are not reported as net patient revenue.

Capital Assets

Depreciable capital assets are depreciated on a straight-line basis over their estimated useful life. Estimated useful lives range from 3 to 40 years. The Hospital capitalizes property and equipment in excess of $5,000 which have a useful life of at least two years. Capital lease assets are amortized over their estimated useful lives and are included in depreciation expense.

Grants and Contributions

From time to time, the Hospital receives grants as well as contributions from individuals and 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 income. Amounts restricted to capital acquisitions are reported after nonoperating income and expenses.

Restricted Resources.

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

Net Assets

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, and contributors external to the Hospital. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

Operating Revenues And Expenses

The Hospital's combined statements of operations and changes in net assets distinguish 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 investment income, 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.

Compensated Absences

The Hospital maintains a Paid Time Off (PTO) policy. PTO accrual rates are determined based on the number of years of service. PTO accruals have maximums based on years of service and there is a 'cash-out' option in June and November of each year. Accrued PTO is paid to employees upon termination of employment if the employee has completed his or her 90 day probationary period. PTO is accrued when earned and reported as a liability.

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. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

Investments

Investments are reported at fair value, as determined by quoted market prices. Interest, dividends, and gains and losses, both realized and unrealized, on investments are included in nonoperating revenue when earned.

Bond Issue Costs

The Hospital provides for the amortization of costs incurred for the issuance of bonds over the life of the debt. Bond issue costs were approximately $510,000. Issue costs are amortized utilizing the straight-line method. Accumulated amortization as of December 31, 2008 and 2007 is $60,721 and $40,480, respectively. Amortization expense for the years ending December 31, 2009 through 2013 is approximately $20,000 per year.

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 $274,495 and $1,211,216 in 2008 and 2007, respectively, and capitalized interest income was $385,299 and $799,204 in 2008 and 2007, respectively.

Minimum Revenue Guarantees

Under FASB Staff Position No. 45-3, “Application of FASB Interpretation No. 45 to Minimum Revenue Guarantees Granted to a Business or Its Owners” (“FIN 45-3”), a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. One example cited in FIN 45-3 involves a guarantee provided by a healthcare entity to a non-employed physician in order to recruit such physician to move to the entity’s geographical area and establish a private practice, which is the approach the Hospital uses in recruiting physicians to the community. FIN 45 is effective for new minimum revenue guarantees issued or modified on or after January 1, 2006.

The Hospital adopted this amendment to FIN 45 effective January 1, 2006. For periods ending before January 1, 2006, the Hospital did not report the fair value of its obligations under physician revenue guarantee agreements. However, under FIN 45 as amended, the Hospital is required to report the liability for these physician revenue guarantees on its balance sheets at fair value and amortize the related prepaid physician recruitment expense over the period of the physician's contractual commitment to practice in the local community, which is typically three years. As of December 31, 2008 and 2007, the Hospital had entered and modified physician revenue guarantee agreements, the effects of which are disclosed.

Reclassifications

Certain amounts from 2007 have been reclassified in order to conform to the current year presentation.

2. AGENCY RELATIONSHIP

The Hospital entered into an agency relationship agreement with Clarian Health Partners during 1998. Clarian acting as the agent of the Hospital provides certain key personnel, administrative and clinical assistance including participation in a managed care plan and a clinical affiliation agreement and other specified assistance for which Clarian receives a management fee. Through the agency relationship Clarian had a funding obligation of $1,000,000 that was paid in four installments of $250,000 each ending in 2001. The funding obligation is for specific purposes including implementing a management plan, enhancing the Hospital's operations and systems, supporting the integration between the Hospital and Clarian and exploring innovative approaches to rural health care. The agreement required these payments be deposited into a restricted fund where the Board of Trustees of the Hospital and Clarian approved all withdrawals in advance. The restricted funds have been expended as of December 31, 2002. The Hospital is required to repay Clarian for the funding obligation annually with 20% of the operating income which excludes certain revenue from an agreement between the Hospital and Tipton County and the Hospital's investment and endowment income. Accordingly, the Hospital has accrued $0 and $198,403 as of December 31, 2008 and 2007, respectively. The minimum repayment of $500,000 and the maximum of $1,500,000 shall be repaid by the Hospital over the 10 year term of the agreement ending in 2008. The cumulative amount paid to Clarian Health Partners as of December 31, 2008 is approximately $704,000. As of January 1, 2009, the Hospital was purchased by Clarian and this agreement was terminated. The remaining balance of the original $1,000,000 was forgiven. See note 20 for details of the new affiliation agreement.

3. CHARITABLE ASSETS' HELD BY OTHERS

The Hospital is named as the beneficiary of certain assets held by an independent organization. The assets fair value as of December 31, 2008 and 2007, is approximately $8,243,000 and $7,356,000, respectively. The assets are maintained by a trustee and are invested in stocks, bonds and cash. The corpus of the assets is to be held in perpetuity with the Hospital receiving the income generated.

4. CHARITY CARE

Charges excluded from net patient service revenue under the Hospital's charity care policy were $1,389,303 and $878,776 for 2008 and 2007, respectively.

5. 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 other 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 entities 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 activities, changes in net assets and financial position. Using the provisions within SFAS No. 157, 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 financial position 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. Investments include mutual funds.

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 government obligations and corporate bonds that trade infrequently and 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.

Based upon the levels as defined above the Hospital's investments as of December 31, 2008 are classified as follows:

	Total	Quoted market prices for identical assets Level 1	Significant other observable inputs Level 2	Significant unobservable inputs Level 3
Certificates of deposit	$ 99,516	$ -0-	$ 99,516	$ -0-
Assets whose use is limited				
Government obligations	$ 3,941,642	$ -0-	$ 3,941,642	$ -0-
Mutual funds	2,856,447	2,856,447	-0-	-0-
Certificates of deposit	65,000	-0-	65,000	-0-
Corporate bonds	1,976,761	-0-	1,976,761	-0-
	$ 8,839,850	$ 2,856,447	$ 5,983,403	$ -0-

6. ASSETS LIMITED AS TO USE

The composition of assets limited as to use includes the following as of December 31:

	2008	2007
Board designated		
Board designated		
Cash and cash equivalents	$ 365,318	$ 512,782
Investments	8,839,850	9,562,014
Accrued interest receivable	-0-	76,390
	9,205,168	10,151,186
Funds held by trustee		
Cash and cash equivalents	-0-	34,952
Investments	-0-	8,553,469
	-0-	8,588,421
Total assets limited as to use	$ 9,205,168	$ 18,739,607

7. DEPOSITS AND INVESTMENTS

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

Investments are carried at fair market value as determined by quoted market prices or significant other observable inputs. Net realized gains and losses on security transactions are determined on the specific identification cost basis. Funded depreciation investments consist of cash equivalents and U.S. Government securities.

The Hospital's investments generally are reported at fair value, as discussed in Note 1. As of December 31, 2008 and 2007, the Hospital had the following investments and maturities, all of which were held in the Hospital's name by custodial banks that are agents of the Hospital.

December 31, 2008

		Investment Maturities (in years)			
	Carrying Amount	Less than 1	1-5	6-10	More than 10
Corporate bonds	$ 1,976,761	$ 577,638	$ 1,399,123	$ -0-	$ -0-
U.S. government securities	3,941,642	1,192,410	2,348,902	263,169	137,161
Certificates of deposit	65,000	65,000	-0-	-0-	-0-
Mutual funds	2,856,447	2,856,447	-0-	-0-	-0-
	$ 8,839,850	$ 4,691,495	$3,748,025	$ 263,169	$ 137,161

December 31, 2007

		Investment Maturities (in years)			
	Carrying Amount	Less than 1	1-5	6-10	More than 10
Corporate bonds	$ 860,589	$ 298,957	$ 561,632	$ -0-	$ -0-
U.S. government securities	13,875,855	10,746,714	2,702,884	-0-	426,257
Certificates of deposit	319,967	254,967	65,000	-0-	-0-
Mutual funds	3,059,072	3,059,072	-0-	-0-	-0-
	$18,115,483	$14,359,710	$3,329,516	$ -0-	$ 426,257

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

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

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

Deposits and investments consist of the following as of December 31, 2008 and 2007:

	2008	2007
Carrying amount		
Deposits	$ 2,258,044	$ 2,694,433
Investments	9,304,684	19,022,546
	$ 11,562,728	$ 21,716,979
Included in the balance sheet captions		
Cash and cash equivalents	$ 2,258,044	$ 2,694,433
Certificates of deposit	99,516	282,939
Assets limited as to use	9,205,168	18,739,607
	$ 11,562,728	$ 21,716,979

8. ACCOUNTS RECEIVABLE AND PAYABLE

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the Hospital at December 31, 2008 and 2007 consisted of the following amounts:

	2008	2007
Patient accounts receivable		
Receivable from patients and their insurance carriers	$ 6,305,823	$ 5,185,664
Receivable from Medicare	3,301,319	3,099,730
Receivable from Medicaid	410,302	342,137
Total patient accounts receivable	10,017,444	8,627,531
Less contractual allowances	3,867,887	3,145,908
Less allowance for uncollectible amounts	1,146,542	780,468
Patient accounts receivable, net	$ 5,003,015	$ 4,701,155
Accounts payable and accrued expenses		
Accrued payroll and payroll taxes	$ 937,181	$ 920,551
Payable to suppliers	2,551,757	1,421,730
Accrued compensated absences	864,924	787,903
Accrued employee health benefit claims	200,872	332,666
Total accounts payable and accrued expenses	$ 4,554,734	$ 3,462,850

9. CAPITAL ASSETS

A summary of capital assets at December 31, 2008 and 2007, follows:

	Balance December 31, 2007	Additions	Retirements	Transfers	Balance December 31, 2008
Land	$ 125,482	$ -0-	$ -0-	$ -0-	$ 125,482
Land improvements	1,316,771	91,580	-0-	-0-	1,408,351
Buildings	17,265,295	1,005,007	-0-	16,083,301	34,353,603
Equipment	20,280,125	922,879	(751,268)	706,366	21,158,102
Construction in progress	12,409,224	11,506,002	-0-	(16,789,667)	7,125,559
Total capital assets	51,396,897	13,525,468	(751,268)	-0-	64,171,097
Less accumulated depreciation					
Land improvements	664,261	97,546	-0-	-0-	761,807
Buildings	17,279,069	1,374,580	-0-	-0-	18,653,649
Equipment	6,309,674	801,916	(713,243)	-0-	6,398,347
Total accumulated depreciation	24,253,004	2,274,042	(713,243)	-0-	25,813,803
Capital assets, net	$ 27,143,893	$ 11,251,426	$ (38,025)	$ -0-	$ 38,357,294

	Balance December 31, 2006	Additions	Retirements	Transfers	Balance December 31, 2007
Land	$ 125,482	$ -0-	$ -0-	$ -0-	$ 125,482
Land improvements	616,387	-0-	-0-	700,384	1,316,771
Buildings	17,057,444	207,851	-0-	-0-	17,265,295
Equipment	19,794,173	1,394,821	(908,869)	-0-	20,280,125
Construction in progress	2,850,695	10,258,913	-0-	(700,384)	12,409,224
Total capital assets	40,444,181	11,861,585	(908,869)	-0-	51,396,897
Less accumulated depreciation					
Land improvements	616,161	48,100	-0-	-0-	664,261
Buildings	16,325,457	953,612	-0-	-0-	17,279,069
Equipment	6,510,916	694,631	(895,873)	-0-	6,309,674
Total accumulated depreciation	23,452,534	1,696,343	(895,873)	-0-	24,253,004
Capital assets, net	$ 16,991,647	$ 10,165,242	$ (12,996)	$ -0-	$ 27,143,893

10. INTEREST RATE SWAP LIABILITY

The Hospital entered into a “cash flow hedge interest rate swap” agreement with an investment company. The Hospital pays a fixed interest rate and the financial institution pays a variable interest rate (2.00% and 3.74% at 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 investment company 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 greater than the financial institution’s present value of estimated projected cash flows.

The swap was effective on June 29, 2006 and matures on June 1, 2016. It contains an outstanding notional amount of $18,400,000 with a 3.875% fixed rate of interest and is a derivative liability for the Hospital with a fair value as of December 31, 2008 and 2007 of $1,234,582 and $643,587, respectively. The interest rate swap liability is payable should the Hospital terminate the agreement.

The total interest rate swap unrealized loss recognized on the financial statements was $590,995 and $279,010 for the years ended 2008 and 2007, respectively.

11. PHYSICIAN RELOCATION AGREEMENTS AND OTHER MINIMUM REVENUE GUARANTEES

Consistent with the Hospital’s policy on physician relocation and recruitment, the Hospital provides income guarantee agreements to certain physicians who agree to relocate to the community to fill a need in the Hospital’s service area and commit to remain in practice there. Under such agreements, the Hospital is required to make payments to the physicians in excess of the amounts they earn in their practice up to the amount of the income guarantee. The income guarantee periods are typically two years. Such payments are recoverable from the physicians if they do not fulfill their commitment period to the community, which is typically three years. The Hospital also provides minimum revenue collection guarantees to Hospital-based physician groups providing certain services at our Hospital with terms ranging from one to three years. At December 31, 2008, the maximum potential amount of future payments under these guarantees was approximately $131,000.

In accordance with FASB Staff Position FIN 45-3, "Application of FASB Interpretation No. 45 to Minimum Revenue Guarantees Granted to a Business or Its Owners," during the year ended December 31, 2006, the Hospital recorded a liability of approximately $572,000 for the fair value of new or modified guarantees entered into during this period with an offsetting asset recorded in other assets on the accompanying balance sheet, which will be amortized over the commitment period. Approximately $72,000 and $195,000 was amortized during 2008 and 2007.

12. LINE OF CREDIT

The Hospital obtained a $750,000 line of credit during 2007. The line of credit is secured by all personal property of the Hospital. It expired September 24, 2008 and beared interest at the prime rate charged by the financial institution. There were no borrowings on the line of credit during 2008 or 2007.

The Hospital obtained a $3,000,000 revolving line of credit during 2008. The line of credit is secured by all personal property of the Hospital. It expires April 1, 2009 and bears interest at the prime rate charged by the financial institution less .25%. The following is a summary of the lines of credit activity for the years ended December 31, 2008 and 2007:

	Balance December 31, 2007	Additional borrowings	Payments	Balance December 31, 2008
Line of Credit	$ -0-	$ 1,038,505	$ -0-	$ 1,038,505

	Balance December 31, 2006	Additional borrowings	Payments	Balance December 31, 2007
Line of Credit	$ -0-	$ -0-	$ -0-	$ -0-

13. LONG-TERM DEBT

The Hospital's 1997 and 2002 bonds were retired during 2006. The defeasance of the 1997 and 2002 bonds resulted in a loss of approximately $101,000 which is amortized through 2017 as a component of interest expense.

The Hospital's $24,200,000, 2006 Series A Revenue Bonds are due in varying installments of $315,000 to $1,660,000 plus variable interest (2.00% at December 31, 2008) through June 1, 2031. The $2,590,000, 2006 Series B Revenue Bonds are due in varying installments of $470,000 to $745,000 plus variable interest (3.19% at December 31, 2008) through June 1, 2011. During 2006, the Hospital entered into an interest rate swap agreement (see footnote 10).

The Hospital has available letters of credit for $24,498,347 and $2,628,318 with a bank for the Series 2006 A and B revenue bonds, respectively. The letters of credit are intended to provide credit enhancement and liquidity support for the Hospital's Series 2006 A and B revenue bonds. Advances bear interest at a maximum interest rate of 10% and 12% per year for the Series 2006 A and B revenue bonds, respectively. The letters of credit both expire December 31, 2009 and may be extended in the bank's sole and absolute discretion upon written request of the Hospital to the bank, which request shall be given 120 days prior to December 31, 2009. There were no balances outstanding as of December 31, 2008 and 2007.

The Hospital has a note payable for $341,000 to a bank secured by a mortgage and assignment of all rents on the property. Payments are due monthly in installments of $3,802 including interest at 6.00%, balloon payment of $263,327 due January 1, 2012.

The Hospital has several capital lease obligations with imputed interest rates of 3% to 7.5%, collateralized by the leased equipment with a cost of $992,817 and $779,243 as of December 31, 2008 and 2007, respectively. Accumulated depreciation on capitalized assets totaled $543,111 and $383,548 as of December 31, 2008 and 2007, respectively.

A summary of long-term debt at December 31, 2008 and 2007 follows:

	Balance December 31, 2007	Additional borrowings	Payments	Balance December 31, 2008	Amounts due within one year
Revenue bonds					
Hospital Association					
$24,200,000 2006 Series A	$ 24,200,000	$ -0-	$ -0-	$ 24,200,000	$ -0-
$2,590,000 2006 Series B	2,590,000	-0-	665,000	1,925,000	710,000
Unamortized bond defeasance loss	(87,488)	-0-	(9,209)	(78,279)	(9,209)
Long-term debt					
Note Payable	-0-	341,000	-0-	341,000	25,868
Capital Leases					
Capital Leases	387,516	213,574	149,921	451,169	133,470
	$ 27,090,028	$ 554,574	$ 805,712	$ 26,838,890	$ 860,129

	Balance December 31, 2006	Additional borrowings	Payments	Balance December 31, 2007	Amounts due within one year
Revenue bonds					
Hospital Association					
$24,200,000 2006 Series A	$ 24,200,000	$ -	$ -	$ 24,200,000	$ -
$2,590,000 2006 Series B	2,590,000	-0-	-0-	2,590,000	665,000
Unamortized bond defeasance loss	(96,697)	-0-	(9,209)	(87,488)	(9,209)
Capital Leases					
Capital Leases	330,023	182,200	124,707	387,516	143,737
	$ 27,023,326	$ 182,200	$ 115,498	$ 27,090,028	$ 799,528

Scheduled principal payments of long-term debt at December 31, 2008 are as follows:

Year ending	Long-term debt		Capital lease obligations	
December 31,	Principal	Interest	Principal	Total
2009	$ 735,868	$ 527,055	$ 133,470	$ 51,614
2010	772,463	993,530	83,991	15,205
2011	1,072,669	950,673	69,322	11,467
2012	820,000	896,416	73,126	7,663
2013	855,000	865,641	69,522	3,629
2014-2018	4,765,000	3,823,421	21,738	615
2019-2023	5,740,000	2,858,699	-0-	-0-
2024-2028	6,905,000	1,697,317	-0-	-0-
2029-2032	4,800,000	364,797	-0-	-0-
	$ 26,466,000	$ 12,977,549	$ 451,169	$ 90,193

Long-term debt is secured by Hospital property and plant. The bonds and the related agreements contain restrictive covenants. Management believes the Hospital either complies with the covenants as of December 31, 2008 and 2007, or in instances of noncompliance has received a limited waiver from the requirements along with certain amendatory provisions effective as of December 31, 2008. Under the limited waiver and amendatory provisions the Hospital is subject to revised covenants and other terms and conditions for which management intends to maintain compliance thereto.

14. 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.

Medicare - The Hospital has been granted Critical Access Status under which the Hospital is paid based upon a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate, with final settlement determined after submission of annual cost reports. Final determination of amounts earned is subject to review by the fiscal intermediary. Medicare reports have been settled through 2006. Management believes adequate provision has been made in the financial statements for any adjustments.

Medicaid - Inpatient and outpatient services rendered to the Medicaid program are paid based upon on a prospectively determined rates.

Revenue from the Medicare program accounted for approximately 49 and 50 percent, respectively of the Hospital's gross patient revenue for the years ended 2008 and 2007. Revenue from the Medicaid program accounted for approximately 5 and 4 percent, respectively of the Hospital's gross patient revenue for the years ended 2008 and 2007. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

The Hospital participates in the Disproportionate Share Hospital program. Subject to certain qualification criteria, the Hospital is entitled to participate in the program annually. This program is a Federal program administered by the state. Amounts received for DSH, net of intergovernmental transfers, approximated $1,395,000 and $581,000 for 2008 and 2007, respectively.

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

Patient service revenue for 2008 and 2007 consists of the following:

	2008	2007
Inpatient revenue	$ 21,689,044	$ 16,891,617
Outpatient revenue	49,593,845	41,680,794
Gross patient service revenue	71,282,889	58,572,411
Contractual allowances	30,703,272	24,393,730
Bad debt expense	2,634,051	1,411,188
Charity care	1,389,303	878,776
Deductions from revenue	34,726,626	26,683,694
Net patient service revenue	$ 36,556,263	$ 31,888,717

15. EMPLOYEE HEALTH PLAN

The Hospital participates in a self-funded health plan covering substantially all employees. Covered services include medical benefits. The plan has annual reinsurance coverage for individual claims in excess of $60,000 per year with an aggregate maximum of approximately $2,498,000. Employee health plan expense was $2,202,759 and $2,176,835 for 2008 and 2007, respectively.

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.

Changes in the balance of claim liabilities during the past two years are as follows:

	2008	2007
Unpaid claims, beginning of year	$ 332,666	$ 186,035
Incurred claims and changes in estimates	2,202,759	2,176,835
Claim payments	(2,334,553)	(2,030,204)
Unpaid claims, end of year	$ 200,872	$ 332,666

16. PENSION PLAN

The Hospital has a defined contribution pension plan that covers all employees who meet eligibility requirements as to age and length of service. 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 Hospital contributes 6% of annual covered payroll. Employer contributions to the plan were $665,056 and $525,573 for 2008 and 2007, respectively. The Plan was terminated effective as of December 31, 2008 and the funds were rolled into a new plan.

17. CONCENTRATIONS OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third party payors at December 31, 2008 and 2007 was as follows:

	2008	2007
Medicare	33%	36%
Medicaid	4%	4%
Blue Cross	21%	17%
Other third party payors	24%	25%
Self-pay	18%	18%
	100%	100%

18. DISCONTINUED OPERATIONS

During 2007, the Hospital discontinued certain lines of business including Delivery/Maternity, an Extended Care Unit, Homecare services and certain Behavioral Health services. During 2008, the Hospital discontinued its Assisted Living services. Operating results are included in the income from operations of the discontinued components in the statement of operations of $94,112 and $41,273 for 2008 and 2007, respectively. Net patient service revenues for the discontinued components were $121,743 and $775,435 for 2008 and 2007, respectively.

19. COMMITMENTS AND CONTINGENCIES

Litigation

The Hospital is involved in litigation and regulatory investigations arising in the normal 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.

Operating Leases

The Hospital leases various equipment and facilities under operating leases expiring at various dates through March 2013. Total rental expense in 2008 and 2007 for was $1,580,669 and $1,221,348 respectively.

The following is a schedule by year of future minimum lease payments under operating leases as of December 31, 2008, that have initial or remaining lease terms in excess of one year.

Year Ending December 31,	Amount
2009	$ 712,044
2010	634,836
2011	156,108
2012	37,068
2013	6,178

Malpractice Insurance

The Indiana Medical Malpractice Act, IC 27-12 (the Act), provides a recovery for an occurrence of malpractice and for any injury or death of a patient due to an act of malpractice in excess of certain thresholds. The Act requires the Hospital to maintain medical malpractice liability insurance on a per occurrence basis and in the annual aggregate for amounts below the thresholds of the Act.

Construction Commitments

The Hospital has committed to construction projects for a remaining estimated amount of approximately $1.9 million. The project is to complete the second and third floor build outs of the facility.

20. SUBSEQUENT EVENT

On October 31, 2008, Clarian Health entered into an Affiliation and Asset Purchase Agreement (Tipton Agreement) with Tipton County Hospital, a county hospital located in Tipton, Indiana and Tipton County, whereby effective January 1, 2009, Tipton County Hospital ceased to exist and sold its assets and liabilities (excluding Tipton Hospital Foundation) to Tipton Hospital, Inc. (Tipton), a newly created non-profit organization which has received tax exempt status from the IRS. Concurrent with the aforementioned transaction, Clarian Health became the sole corporate member of Tipton Hospital, Inc. The Tipton Agreement was designed to enable both organizations to better position themselves to serve patients and to provide Tipton with system support. In connection with the transaction, Clarian Health committed to loaning Tipton $7,500,000 to fund the remainder of certain capital projects. The loan is structured as a variable rate line of credit maturing in December 2009. At which time, the obligation will be refinanced to a term loan with principal to be repaid over a period of 20 years at an interest rate yet to be negotiated.

The structure of the integration is not yet finalized. Clarian Health expects operations to be partially integrated during 2009.