

Paulding County Hospital

**Financial Report
with Additional Information
December 31, 2005**



**Auditor of State
Betty Montgomery**

Board of Directors
Paulding County Hospital
1035 West Wayne Street
Paulding, Ohio 45879

We have reviewed the *Independent Auditor's Report* of the Paulding County Hospital, prepared by Plante & Moran PLLC, for the audit period January 1, 2005 through December 31, 2005. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

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

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

BETTY MONTGOMERY
Auditor of State

April 19, 2006

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Paulding County Hospital

Contents

Report Letter	I
Management's Discussion and Analysis	2-9
Financial Statements	
Balance Sheet	10
Statement of Revenues, Expenses, and Changes in Net Assets	11
Statement of Cash Flows	12-13
Notes to Financial Statements	14-29
Additional Information	30
Report on Internal Control and Compliance	31-32

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Independent Auditor's Report

To the Board of Directors
Paulding County Hospital

We have audited the accompanying balance sheet of Paulding County Hospital (a component unit of Paulding County) as of December 31, 2005 and 2004 and the related statements of revenues, expenses, and 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Paulding County Hospital at December 31, 2005 and 2004 and the results of its operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis is not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 20, 2006 on our consideration of Paulding County Hospital's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide opinions on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Plante & Moran, PLLC

January 20, 2006

A member of



A worldwide association of independent accounting firms

Paulding County Hospital

Management's Discussion and Analysis

Management's Discussion and Analysis

The discussion and analysis of Paulding County Hospital's (the "Hospital") consolidated financial statements provide an overview of the Hospital's financial activities for the year ended December 31, 2005. Management is responsible for the completeness and fairness of the financial statements and the related footnote disclosures along with the discussion and analysis.

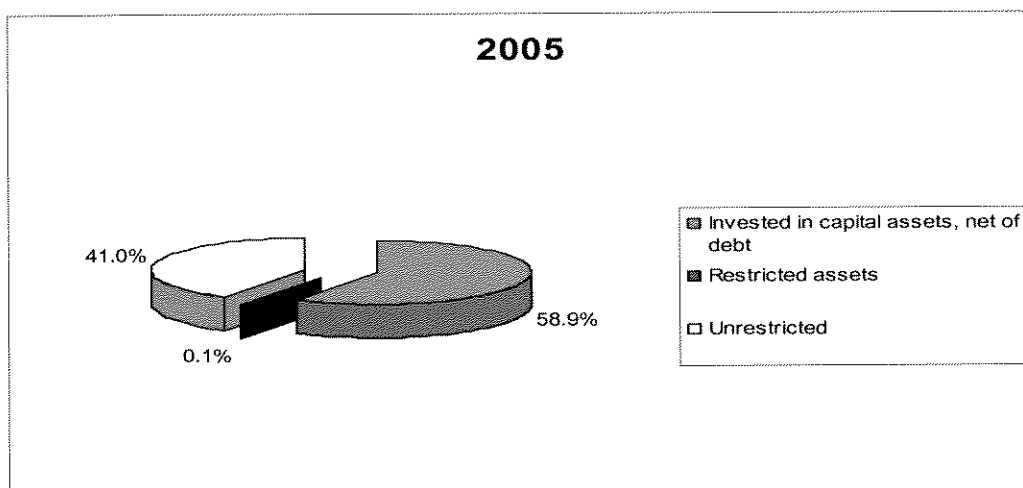
Using this Annual Report

The Hospital's financial statements consists of three statements - balance sheet, a statement of revenues, expenses, and changes in net assets, and a statement of cash flows. These financial statements and related notes provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purpose by contributors, grantors, or enabling legislation.

Financial Highlights

The Hospital's financial position improved during the year ended December 31, 2005. The current assets increased by \$112,414, or 3.1 percent from the prior year. In total, the Hospital's net assets increased \$400,654, or 3.2 percent from the previous year. The increase in net assets resulted from increases in patient revenue, driven largely by inpatient volumes.

The following chart provides a breakdown of net assets by category for the year ended December 31, 2005:



For the year ended December 31, 2005, the Hospital's revenues and other support exceeded expenses, creating an increase in net assets of \$400,654 (compared to a \$117,473 increase in the previous year).

Paulding County Hospital

Management's Discussion and Analysis (Continued)

The Balance Sheet and the Statement of Revenues, Expenses, and Changes in Net Assets

One of the most important questions asked about the Hospital's finances is, "Is Paulding County Hospital as a whole better off or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses, and changes in net assets report information on the Hospital as a whole and on its activities in a way that helps answer this question. When revenues and other support exceed expenses, the result is an increase in net assets. When the reverse occurs, the result is a decrease in net assets. The relationship between revenues and expenses may be thought of as Paulding County Hospital's operating results.

These two statements report the Hospital's net assets and changes in them. You can think of Paulding County Hospital's net assets - the difference between assets and liabilities - as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider many other nonfinancial factors, such as the trend in patient days, outpatient visits, conditions of the buildings, and strength of the medical staff, to assess the overall health of the Hospital.

The financial statements include all assets and 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.

Condensed Financial Information

The following is a comparative analysis of the major components of the statement of net assets of the Hospital as of December 31, 2005 and 2004:

	<u>Year Ended December 31</u>		<u>Change</u>	
	<u>2005</u>	<u>2004</u>	<u>Amount</u>	<u>Percent</u>
Assets				
Current assets	\$ 3,741,709	\$ 3,629,295	\$ 112,414	3.1%
Noncurrent assets	3,610,964	3,796,850	(185,886)	-4.9%
Capital assets	<u>9,812,630</u>	<u>8,768,757</u>	<u>1,043,873</u>	11.9%
Total assets	17,165,303	16,194,902	970,401	6.0%
Liabilities				
Current liabilities	2,080,277	2,092,816	(12,539)	-0.6%
Long-term liabilities	1,852,274	1,320,200	532,074	40.3%
Other liabilities	<u>351,112</u>	<u>300,900</u>	<u>50,212</u>	16.7%
Total liabilities	<u>4,283,663</u>	<u>3,713,916</u>	<u>569,747</u>	15.3%

Paulding County Hospital

Management's Discussion and Analysis (Continued)

	<u>Year Ended December 31</u>		<u>Change</u>	
	<u>2005</u>	<u>2004</u>	<u>Amount</u>	<u>Percent</u>
Net Assets				
Invested in capital assets - Net of debt	\$ 7,583,504	\$ 7,069,157	\$ 514,347	7.3%
Restricted assets	13,782	13,768	14	0.1%
Unrestricted	<u>5,284,354</u>	<u>5,398,061</u>	<u>(113,707)</u>	-2.1%
Total net assets	<u>\$12,881,640</u>	<u>\$12,480,986</u>	<u>\$ 400,654</u>	3.2%

Capital assets increased from continued upgraded enhancements to our radiology department. In 2005, the Hospital upgraded to a 16-slice CT scanner and new x-ray rooms with fluoroscopy.

Long-term liabilities increased resulting from the financing on the \$1,037,706 for the CT scanner, IV, and infusion pumps.

Invested in capital assets, net of debt reflects an increased ability to purchases capital through operations rather than additional debt.

Operating Results for the Year

	<u>Year Ended December 31</u>		<u>Change</u>	
	<u>2005</u>	<u>2004</u>	<u>Amount</u>	<u>Percent</u>
Operating Revenue				
Net patient service revenue	\$16,239,557	\$14,677,596	\$1,561,961	10.6%
Other	<u>208,341</u>	<u>179,365</u>	<u>28,976</u>	16.2%
Total operating revenue	16,447,898	14,856,961	1,590,937	10.7%
Operating Expenses				
Salaries and wages	7,730,211	7,186,360	543,851	7.6%
Employee benefits and payroll taxes	2,264,271	2,021,653	242,618	12.0%
Medical supplies and drugs	3,029,832	2,721,400	308,432	11.3%
Professional services and consultant fees	382,780	377,846	4,934	1.3%
Purchased services	1,633,019	1,600,297	32,722	2.0%
Depreciation and amortization	<u>1,069,433</u>	<u>861,848</u>	<u>207,585</u>	24.1%
Total operating expenses	<u>16,109,546</u>	<u>14,769,404</u>	<u>1,340,142</u>	9.1%
Operating Income	338,352	87,557	250,795	286.4%

Paulding County Hospital

Management's Discussion and Analysis (Continued)

Operating Results for the Year (Continued)

	<u>Year Ended December 31</u>		<u>Change</u>	
	<u>2005</u>	<u>2004</u>	<u>Amount</u>	<u>Percent</u>
Other Income (Expense)				
Investment income	\$ 121,810	\$ 59,062	\$ 62,748	106.2%
Contributions	15,995	49,997	(34,002)	-68.0%
Interest earnings on restricted assets	14	14	-	0.0%
Interest expense	(76,426)	(29,990)	(46,436)	154.8%
Other income	<u>909</u>	<u>(49,167)</u>	<u>50,076</u>	<u>101.8%</u>
Total other income	<u>62,302</u>	<u>29,916</u>	<u>32,386</u>	108.3%
Increase in Net Assets	400,654	117,473	<u>\$ 283,181</u>	241.1%
Net Assets - Beginning of year	<u>12,480,986</u>	<u>12,363,513</u>		
Net Assets - End of year	<u>\$12,881,640</u>	<u>\$12,480,986</u>		

Operating Revenues

Operating revenues include all transactions that result in the sales and/or receipts from goods and services such as inpatient services, outpatient services, physician offices, and the cafeteria. In addition, certain federal, state, and private grants are considered operating if they are not for capital purposes and are considered a contract for services.

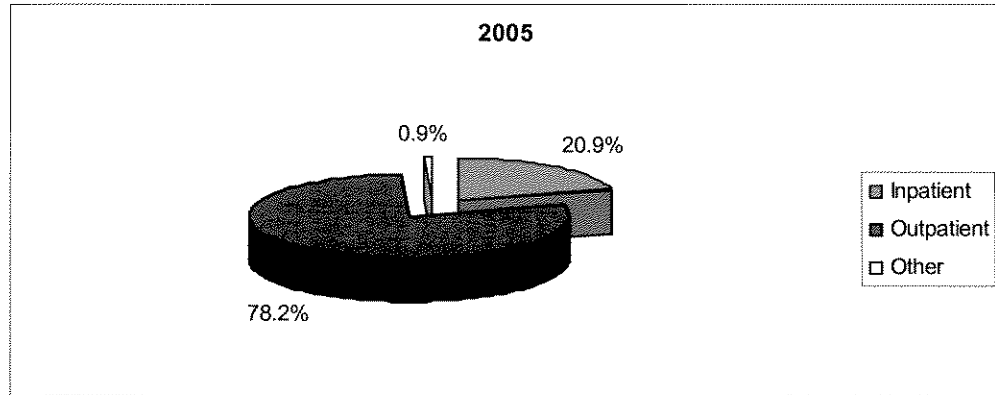
Operating revenue changes were a result of the following factors:

- Net patient service revenue increased 10.7 percent. This was attributable to a 7.3 percent increase in gross outpatient revenues and a 35.7 percent increase in gross inpatient revenues. Gross patient revenue is reduced by revenue deductions. These deductions are the amounts that are not paid to the Hospital under contractual arrangements primarily with Medicare, Medicaid, and Anthem. These revenue deductions increased from 28.2 percent to 27.2 percent as a percentage of gross revenue.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

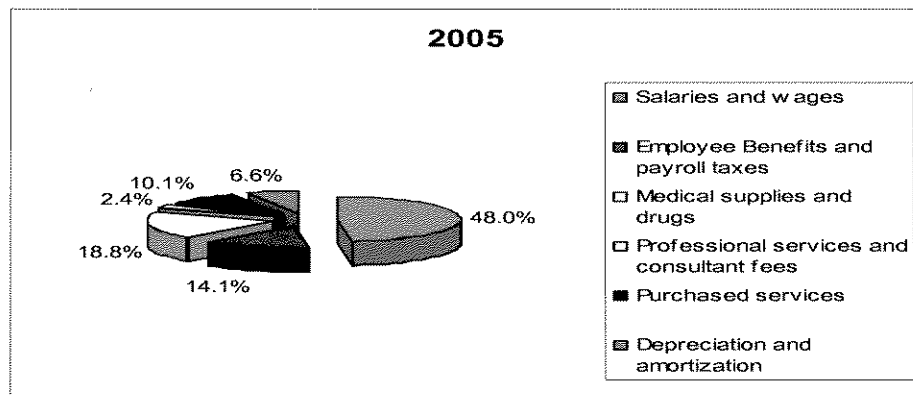
- The following is a graphic illustration of operating revenues by source:



Operating Expenses

Operating expenses are all the costs necessary to perform and conduct the services and primary purposes of the Hospital. The operating expense changes were the result of the following factors:

- Salary cost increased 7.6 percent as a result of an additional employed physician. Patient care salaries also increased as a result of higher inpatient and outpatient volumes.
- Employee benefits increased 12.0 percent, reflecting increased self-funded health insurance claims, and an increase in Bureau of Workers' Compensation premiums.
- Medical supply and drug expenses increased by 11.3 percent as a result of increased patient volumes.
- Depreciation expense increased 24.1 percent reflecting additions to property, plant, and equipment.
- The following is a graphic illustration of operating expenses by type:



Paulding County Hospital

Management's Discussion and Analysis (Continued)

Nonoperating Gains (Losses)

Nonoperating gains and losses are all sources and uses that are primarily nonexchange in nature. They would consist primarily of investment income (including realized and unrealized gains and losses), interest expense, grants, and contracts that do not require any services to be performed.

The category "other," within nonoperating gains (losses), consists of items that are typically nonrecurring or unusual to the Hospital. Examples would be capital grants, additions to permanent endowments, and transfers from related entities.

Statement of Cash Flows

Another way to assess the financial health of a hospital is to look at the statement of cash flows. Its primary purpose is to provide relevant information about the cash receipts and cash payments of an entity during a period. The statement of cash flows also helps assess:

- An entity's ability to generate future net cash flows
- Its ability to meet its obligations as they come due
- Its needs for external financing

	<u>2005</u>	<u>2004</u>	<u>Increase (Decrease)</u>
Net cash from:			
Operating and nonoperating activities	\$ 499,993	\$ 1,739,120	\$(1,239,127)
Investing activities	73,605	47,983	25,622
Noncapital and financing activities	15,995	49,997	(34,002)
Capital and related financing activities	<u>(1,660,332)</u>	<u>(1,171,013)</u>	<u>(489,319)</u>
Net Increase (Decrease) in Cash	(1,070,739)	666,087	(1,736,826)
Cash - Beginning of year	<u>5,024,166</u>	<u>4,358,079</u>	<u>666,087</u>
Cash - End of year	<u>\$ 3,953,427</u>	<u>\$ 5,024,166</u>	<u>\$(1,070,739)</u>

The following discussion amplifies the overview of cash flows presented above:

Cash provided by operating and nonoperating activities decreased \$1,239,127 from the prior year. This was primarily as a result of increasing of accounts receivable by 12 days. Capital and related financing activities decreased as a result of additional payments on notes payable reflecting increased debt.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

Capital Assets and Debt Administration

Capital Assets - At December 31, 2005, the Hospital had \$9.8 million invested in capital assets, net of accumulated depreciation of \$10.6 million. Depreciation and amortization totaled \$1,069,433 in the current year compared to \$861,848 last year. Details of these assets for the past two years are shown below.

	<u>2005</u>	<u>2004</u>	<u>Increase (Decrease)</u>
Land	\$ 30,609	\$ 30,609	\$ -
Land improvements	84,237	63,301	20,936
Buildings and improvements	6,926,799	5,119,501	1,807,298
Furniture, fixtures, and equipment	2,770,985	1,400,595	1,370,390
Construction in process	<u>-</u>	<u>2,154,751</u>	<u>(2,154,751)</u>
Total	<u>\$ 9,812,630</u>	<u>\$ 8,768,757</u>	<u>\$ 1,043,873</u>

Debt - At year end, the Hospital had \$2,733,798 in debt outstanding as compared to \$2,087,536 the previous year. The table below summarizes these amounts by type of debt instrument:

	<u>2005</u>	<u>2004</u>	<u>Increase (Decrease)</u>
Lease obligations	\$ 71,959	\$ 318,470	\$ (246,511)
Note payable	2,157,167	1,381,130	776,037
Compensated absences	<u>504,672</u>	<u>387,936</u>	<u>116,736</u>
Total long-term liabilities	<u>\$ 2,733,798</u>	<u>\$ 2,087,536</u>	<u>\$ 646,262</u>

In 2005, the Hospital has incurred debt of \$1,037,706 for the purchase of a new CT scanner, IV, and infusion pumps.

Economic Factors that Will Affect the Future

The economic position of Paulding County Hospital is closely tied to that of the local economy. Job market growth in the community is anticipated to increase with the relocation plans for U.S. Highway 24.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

The Supplemental Inpatient Upper Payment Limit and Healthcare Assurance programs have provided valuable relief toward Medicaid shortfalls. The Hospital has and will continue to monitor suggested changes to these programs in conjunction with the Ohio Hospital Association and Department of Job and Family Services.

In addition, the board of directors approved an average increase of 3.0 percent in the charge structure for the upcoming fiscal year.

Contacting the Hospital's Management

This financial report is intended to provide our county and bondholders with a general overview of the Hospital's finances, and to show the Hospital's accountability for the money it had received in the past. If you have questions about this report or need additional information, we welcome you to contact the chief financial officer.

Robert L. Goshia, II
Chief Financial Officer

Paulding County Hospital

Balance Sheet

	December 31, 2005	December 31, 2004
Assets		
Current Assets		
Cash and cash equivalents (Note 2)	\$ 389,500	\$ 1,259,117
Accounts receivable (Note 3)	2,436,327	1,646,325
Notes receivable	47,396	13,378
Third-party settlements (Note 8)	168,703	38,545
Prepaid expenses and other	204,678	237,314
Inventory	495,105	434,616
Total current assets	3,741,709	3,629,295
Assets Limited as to Use (Notes 2 and 4)	3,610,964	3,796,850
Capital Assets - Net (Note 5)	9,812,630	8,768,757
Total assets	\$ 17,165,303	\$ 16,194,902
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt (Note 6)	\$ 376,852	\$ 379,400
Accounts payable	540,945	633,798
Accrued liabilities and other (Note 7)	1,162,480	1,079,618
Total current liabilities	2,080,277	2,092,816
Long-term Debt (Note 6)	1,852,274	1,320,200
Other Liabilities (Note 6)	351,112	300,900
Total liabilities	4,283,663	3,713,916
Net Assets		
Invested in capital assets - Net of related debt	7,583,504	7,069,157
Restricted - Expendable for education and other purposes	13,782	13,768
Unrestricted	5,284,354	5,398,061
Total net assets	12,881,640	12,480,986
Total liabilities and net assets	\$ 17,165,303	\$ 16,194,902

Paulding County Hospital

Statement of Revenues, Expenses, and Changes in Net Assets

	Year Ended	
	December 31, 2005	December 31, 2004
Operating Revenues		
Net patient service revenue (Note 9)	\$ 16,239,557	\$ 14,677,596
Other	208,341	179,365
Total operating revenues	16,447,898	14,856,961
Operating Expenses		
Salaries and wages	7,730,211	7,186,360
Employee benefits and payroll taxes	2,264,271	2,021,653
Medical supplies and drugs	3,029,832	2,721,400
Professional services and consultant fees	382,780	377,846
Purchased services	1,633,019	1,600,297
Depreciation and amortization	1,069,433	861,848
Total operating expenses	16,109,546	14,769,404
Operating Income	338,352	87,557
Other Income (Expenses)		
Investment income	121,810	59,062
Contributions	15,995	49,997
Interest earnings on restricted assets	14	14
Interest expense	(76,426)	(29,990)
Other income (expense) (Note 14)	909	(49,167)
Total other income	62,302	29,916
Increase in Net Assets	400,654	117,473
Net Assets - Beginning of year	12,480,986	12,363,513
Net Assets - End of year	\$ 12,881,640	\$ 12,480,986

Paulding County Hospital

Statement of Cash Flows

	Year Ended	
	December 31, 2005	December 31, 2004
Cash Flows from Operating Activities		
Cash received from patients and third-party payors	\$ 15,319,397	\$ 15,356,666
Cash payments to suppliers for services and goods	(5,372,698)	(4,737,657)
Cash payments to employees for services	(9,753,006)	(9,072,526)
Other operating receipts	306,300	192,637
Net cash provided by operating activities	499,993	1,739,120
Cash Flows from Noncapital Financing Activities -		
Unrestricted contributions received	15,995	49,997
Cash Flows from Investing Activities		
Investment income	106,588	54,697
Recovery on uninsured investments	-	21,531
Advances to physicians - Net of forgiveness	(34,018)	1,782
Other	1,035	(30,027)
Net cash provided by investing activities	73,605	47,983
Cash Flows from Capital and Related Financing Activities		
Proceeds from issuance of debt	1,037,705	1,400,000
Principal payments on notes payable	(261,668)	(51,102)
Interest paid on long-term debt - Net of amount capitalized	(76,426)	(29,990)
Purchase of capital assets	(2,131,432)	(2,259,129)
Proceeds from sale of capital assets	18,000	19,976
Principal payments on capital leases	(246,511)	(250,768)
Net cash used in capital and related financing activities	(1,660,332)	(1,171,013)
Net (Decrease) Increase in Cash and Cash Equivalents	(1,070,739)	666,087
Cash and Cash Equivalents - Beginning of year	5,024,166	4,358,079
Cash and Cash Equivalents - End of year	\$ 3,953,427	\$ 5,024,166
Balance Sheet Classification of Cash		
Current assets	\$ 389,500	\$ 1,259,117
Restricted cash and cash equivalents	3,563,927	3,765,049
Total cash	\$ 3,953,427	\$ 5,024,166

Paulding County Hospital

Statement of Cash Flows (Continued)

	Year Ended	
	December 31, 2005	December 31, 2004
Reconciliation of Operating Income to Net Cash from Operating Activities		
Operating income	\$ 338,352	\$ 87,557
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation	1,069,433	861,848
Provision for bad debts	486,240	425,060
Changes in assets and liabilities:		
Increase in patient accounts receivable	(1,276,242)	(155,240)
Increase in inventories	(60,489)	(53,821)
(Increase) in prepaid expenses and other receivables	32,636	(7,258)
Decrease in accounts payable	(92,853)	(42,981)
Increase in other accrued expenses	133,074	214,705
Increase (decrease) in third-party settlement receivables	(130,158)	409,250
Net cash provided by operating activities	<u>\$ 499,993</u>	<u>\$ 1,739,120</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note I - Nature of Business and Significant Accounting Policies

Organization - Effective January 1, 2001, Paulding County Hospital (the "Hospital") became a 25-bed critical access hospital located in Paulding, Ohio. The Hospital operates under the authority of Section 339, Ohio Revised Code, to provide inpatient, outpatient, and emergency care services for the residents of Paulding County, Ohio. A board of directors appointed by the county commissioners, the probate judge, and the Judge of the Court of Common Pleas of Paulding County governs the Hospital. The Hospital is considered a component unit of Paulding County, Ohio (the "County"), and is included as a component unit in the general purpose financial statements of the County.

Basis of Presentation - The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, issued in June 1999. The Hospital follows the business-type activities reporting requirements of GASB Statement No. 34, which provides a comprehensive look at the Hospital's activities. No component units are required to be reported in the financial statements.

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 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 are defined as short-term highly liquid investments purchased with initial maturities of three months or less. Cash and cash equivalents included in assets limited as to use are considered cash and cash equivalents for the purpose of the statement of cash flows.

Accounts Receivable - Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges. An allowance for uncollectible accounts is established on an aggregate basis by using historical write-off rate factors applied to unpaid accounts based on aging. Loss rate factors are based on historical loss experience and adjusted for economic conditions and other trends affecting the Hospital's ability to collect outstanding amounts. Uncollectible amounts are written off against the allowance for doubtful accounts in the period they are determined to be uncollectible. An allowance for contractual adjustments and interim payment advances is based on expected payment rates from payors based on current reimbursement methodologies. This amount also includes amounts received as interim payments against unpaid claims by certain payors.

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Inventories - Inventories, consisting primarily of medical supplies, food, and drugs, are valued at the lower of cost or market determined on a first-in, first-out (FIFO) basis.

Assets Limited as to Use - Assets limited as to use include assets set aside by the Hospital board of directors for future capital improvements, over which the board retains control, and may, at its discretion, subsequently use for other purposes. Assets limited as to use also include assets restricted by contributors for education and other purposes of the home health department.

Capital Assets - Capital assets are recorded at cost, or if donated, at fair value at the date of receipt. Depreciation is provided over the estimated useful life and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the useful life of the equipment. Such amortization is included in depreciation and amortization in the financial statements. Interest costs incurred on borrowed funds during the period of construction of capital assets are capitalized as a component of the cost of acquiring those assets.

Notes Receivable - Notes receivable represent loans to physicians under various cash flow support and loan arrangements. These loans are to be repaid in varying monthly installments including varying interest rates, ranging from the minimum applicable federal rate to 8 percent, and are unsecured. A majority of the physician notes receivable are forgiven over time under the terms specified in the physician loan agreement.

Compensated Absences - Paid time off is charged to operations when earned. Unused and earned benefits are recorded as a current liability in the financial statements. Employees accumulate vacation days at varying rates depending on years of service. Employees are not paid for accumulated sick leave if they leave before retirement. However, employees who retire from the Hospital may convert accumulated sick leave to termination payments equal to one-half of the accumulated balance calculated at the employee's base pay rate as of the retirement date. Employees hired after June 8, 2001 are only eligible to receive termination payments on one-half of the accumulated sick leave balance up to a maximum of 240 hours.

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 unrestricted resources before restricted resources.

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Classification of Net Assets - Net assets of the Hospital are classified in four 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, or contributors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures. Restricted nonexpendable net assets equal the principal portion of permanent endowments. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

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. Retroactive adjustments to these estimated amounts are recorded in future periods as final settlements are determined.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Management believes that it is in compliance with all applicable laws and regulations. Final determination of compliance of such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusions from the Medicare and Medicaid programs.

Income from Operations - The Hospital's statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services. Nonexchange revenues, including taxes, 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.

Investment Income - Investment income on board-designated funds (funded depreciation) and general funds is recorded as nonoperating gains. Interest earnings on funds restricted by contributors are also recorded as nonoperating gains.

Charity Care - The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as net patient service revenue.

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

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 certain reported amounts and disclosures in the financial statements. Actual results could differ from those estimates.

Pension Plan - Substantially all of the Hospital's employees are eligible to participate in a defined benefit pension plan sponsored by the Ohio Public Employees' Retirement System (OPERS). The Hospital funds pension costs accrued based on contribution rates determined by OPERS.

Federal Income Tax - As a political subdivision, the Hospital is exempt from taxation under Section 501(c)(3) of the Internal Revenue Code.

Reclassification - Certain prior year amounts have been reclassified to conform to the current year presentation.

Note 2 - Deposits and Investments

Chapter 135 of the Ohio Uniform Depositor Act authorizes local and governmental units to make deposits in any national bank located in the state subject to inspection by the superintendent of financial institutions and is eligible to become a public depository. Section 135.14 of the Ohio Revised Code allows the local governmental to invest in United States treasury bills, notes, bonds, or any other obligation or security issued by the United States Treasury or any other obligation guaranteed as to principal and interest by the United States of America and bonds and other obligations of the State of Ohio. Investments in no-load money market mutual funds, repurchase agreements, commercial paper, and bankers' acceptances are permitted subject to certain limitations that include completion of additional training, approved by the auditor of state, by the treasurer or governing board investing in these instruments.

The Hospital has designated Antwerp Exchange Bank, Community First Bank, Farmers & Merchants State Bank, Fifth Third Bank, First Federal Savings & Loan, Sherwood State Bank, State Bank & Trust, and Sky Bank for the deposit of its funds. An investment policy has not been filed with the auditor of state on behalf of the Hospital. Investment of interim funds is limited to bonds, notes, debentures, or any other obligations or securities issued by any federal government agency or instrumentality, no-load money market mutual funds, and the Ohio subdivision's fund (STAR Ohio).

Note 2 - Deposits and Investments (Continued)

Statutes require the classification of funds held by the Hospital into three categories:

Active Funds - Those funds required to be kept in a "cash" or "near cash" status for immediate use by the Hospital. Such funds must be maintained either in depository accounts or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts.

Inactive Funds - Those funds not required for use within the current five-year period of designated depositories. Ohio law permits inactive monies to be deposited or invested as certificates of deposit, maturing no later than the end of the current period of designated depositories or as savings or deposit accounts, including, but not limited to passbook accounts.

Interim Funds - Those funds which are not needed for immediate use but will be needed before the end of the current period of designation of deposit. Ohio law permits interim funds to be invested or deposited in the following securities:

1. Bonds, notes, or other obligations that are guaranteed by the United States, or those for which the faith of the United States is pledged for the payment of principal and interest
2. Bonds, notes debentures, or other obligations or securities issued by any federal governmental agency
3. No-load money market mutual funds consisting exclusively of obligations described in (1) or (2) above and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions
4. Interim deposits in the eligible institutions applying for interim funds to be evidenced by time certificates of deposit maturing not more than one year for date of deposit, or by savings or deposit accounts, including but not limited to, passbook accounts
5. Bonds and other obligations of the State of Ohio
6. The Ohio state treasurer's investment pool (STAR Ohio)
7. Commercial paper and bankers' acceptances which meet the requirements established by Ohio Revised Code, SEC 135.142
8. Under limited circumstances, corporate debt interest in either of the two highest rating classifications by at least two nationally recognized rating agencies

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 2 - Deposits and Investments (Continued)

Protection of the Hospital's deposits is provided by the Federal Deposit Insurance Corporation, by eligible securities pledged by the financial institution as security for repayment, by surety company bonds deposited with the treasurer by the financial institution, or by single collateral pool established by the financial institution to secure the repayment of all public funds deposited with the institution.

Investments in stripped principal or interest obligations, reverse repurchase agreements, and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, or the use of leverage and short selling are also prohibited. An investment must mature within five years from the date of purchase unless matched to a specific obligation or debt of the district, and must be purchased with the expectation that it will be held to maturity.

Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the treasurer or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian.

The Hospital's cash and investments are subject to the custodial credit risk, as examined in more detail below:

Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The government does not have a specific deposit policy for custodial credit risk. At year end, the Hospital had no bank deposits (certificates of deposit, checking, and savings accounts) that were uninsured and uncollateralized. The Hospital believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Hospital evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

The Hospital's deposits and investments are comprised of the following:

	2005	2004
Deposits	\$ 389,500	\$ 1,259,117
Certificates of deposit	3,563,927	3,765,049
Total	<u>\$ 3,953,427</u>	<u>\$ 5,024,166</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 2 - Deposits and Investments (Continued)

	2005	2004
Deposits:		
Amount of deposits reflected on the accounts of the bank (without recognition of checks written but not yet cleared or of deposits in transit)	\$ 3,500,026	\$ 5,264,280
Amount of deposits covered by federal depository insurance	(713,782)	(713,768)
Amount of deposits collateralized	<u>\$ 2,786,244</u>	<u>\$ 4,550,512</u>

Amounts of deposits not insured by federal depository insurance are collateralized by itemized securities pledged by the depository bank and held in the name of the Hospital and respective bank.

Note 3 - Patient Accounts Receivable

The details of patient accounts receivable are set forth below:

	2005	2004
Gross patient accounts receivable	\$ 4,053,512	\$ 2,886,450
Less:		
Uncollectible accounts	(647,424)	(647,117)
Contractual adjustments	(969,761)	(593,008)
Net patient accounts receivable	<u>\$ 2,436,327</u>	<u>\$ 1,646,325</u>

The Hospital provides services without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors was as follows:

	Percent	
	2005	2004
Medicare	40	34
Medical Mutual of Ohio	12	11
Medicaid	5	9
Other third-party payors	28	26
Patient pay	15	20
Total	<u>100</u>	<u>100</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 4 - Assets Limited as to Use

The composition of these assets is described in Note 2. The classification and limited uses of these assets are described below:

	2005	2004
Restricted by contributors for construction, education, and other purposes - Deposits in financial institutions	\$ 13,782	\$ 13,768
Designated by the board for capital improvements:		
Deposits in financial institutions	3,550,145	3,751,281
Accrued interest receivable	47,037	31,801
Total assets limited as to use	<u>\$ 3,610,964</u>	<u>\$ 3,796,850</u>

Note 5 - Capital Assets

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

	2004	Additions	Transfers	Retirements	2005
Land	\$ 30,609	\$ -	\$ -	\$ -	\$ 30,609
Land improvements	163,553	15,251	17,408	-	196,212
Building and improvements	9,664,279	323,696	2,000,734	-	11,988,709
Fixed equipment	1,378,938	-	-	(736)	1,378,202
Moveable equipment	3,931,988	1,792,485	136,609	(1,005,450)	4,855,632
Moveable equipment - Capital leases	1,976,948	-	-	-	1,976,948
Construction in progress	2,154,751	-	(2,154,751)	-	-
Total	19,301,066	2,131,432	-	(1,006,186)	20,426,312
Capital assets being depreciated:					
Land improvements	100,252	11,723	-	-	111,975
Building and improvements	4,544,778	517,132	-	-	5,061,910
Fixed equipment	1,375,672	1,218	-	(736)	1,376,154
Moveable equipment	3,413,886	539,360	-	(987,324)	2,965,922
Moveable equipment - Capital leases	1,097,721	-	-	-	1,097,721
Total	10,532,309	1,069,433	-	(988,060)	10,613,682
Net carrying amount	<u>\$ 8,768,757</u>	<u>\$ 1,061,999</u>	<u>\$ -</u>	<u>\$ (18,126)</u>	<u>\$ 9,812,630</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 5 - Capital Assets (Continued)

Capital asset activity for the year ended December 31, 2004 was as follows:

	2003	Additions	Transfers	Retirements	2004	Depreciable Life - Years
Land	\$ 30,609	\$ -	\$ -	\$ -	\$ 30,609	
Land improvements	163,553	-	-	-	163,553	5-25
Building and improvements	9,655,763	9,166	-	(650)	9,664,279	5-50
Fixed equipment	1,455,292	-	-	(76,354)	1,378,938	5-20
Moveable equipment	4,812,667	189,799	-	(1,070,478)	3,931,988	5-20
Moveable equipment - Capital leases	1,976,948	-	-	-	1,976,948	5
Construction in progress	94,587	2,060,164	-	-	2,154,751	
Total	18,189,419	2,259,129	-	(1,147,482)	19,301,066	
Less accumulated depreciation:						
Land improvements	91,878	8,374	-	-	100,252	
Building and improvements	4,117,028	428,400	-	(650)	4,544,778	
Fixed equipment	1,450,858	1,168	-	(76,354)	1,375,672	
Moveable equipment	4,163,710	260,007	-	(1,009,831)	3,413,886	
Moveable equipment - Capital leases	933,822	163,899	-	-	1,097,721	
Total	10,757,296	861,848	-	(1,086,835)	10,532,309	
Net carrying amount	\$ 7,432,123	\$ 1,397,281	\$ -	\$ (60,647)	\$ 8,768,757	

Note 6 - Long-term Debt

The lease obligations consist of three amounts summarized as follows:

- Capital lease payable over 60 months, with monthly payments of \$4,324, including interest at 5.75 percent, collateralized by equipment
- Capital lease payable over 120 months, with monthly payments of \$18,385, including interest at 5.52 percent, collateralized by HVAC system, paid in full in 2005
- Capital lease payable over 60 months, with monthly payments of \$262, at 0 percent interest, collateralized by automobile

The notes payable are summarized below:

- Note payable over 60 months, with monthly payments of \$1,881, including interest at 5.94 percent, collateralized by roof, paid in full in 2005
- Notes payable over 120 months, with monthly payments of \$13,631, including interest at 3.13 percent, collateralized by future revenues of the Hospital
- Notes payable over 60 months, with monthly payments of \$18,763, including interest at 3.25 percent, collateralized by CT Scanner

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 6 - Long-term Debt (Continued)

Long-term debt activity for the year ended December 31, 2005 was as follows:

	2004	Additions	Deductions	2005	Current Portion
Leases, bonds, and loans payable:					
Leases payable	\$ 318,470	\$ -	\$ (246,511)	\$ 71,959	\$ 66,442
Notes payable	1,381,130	1,037,705	(261,668)	2,157,167	310,410
Compensated absences	387,936	515,811	(399,075)	504,672	153,560
Total long-term liabilities	<u>\$ 2,087,536</u>	<u>\$ 1,553,516</u>	<u>\$ (907,254)</u>	<u>\$ 2,733,798</u>	<u>\$ 530,412</u>

Long-term debt activity for the year ended December 31, 2004 was as follows:

	2003	Additions	Deductions	2004	Current Portion
Leases, bonds, and loans payable:					
Lease payable	\$ 569,238	\$ -	\$ (250,768)	\$ 318,470	\$ 246,512
Notes payable	32,232	1,400,000	(51,102)	1,381,130	132,888
Compensated absences	320,648	477,208	(409,920)	387,936	87,036
Total long-term liabilities	<u>\$ 922,118</u>	<u>\$ 1,877,208</u>	<u>\$ (711,790)</u>	<u>\$ 2,087,536</u>	<u>\$ 466,436</u>

The following is a schedule by years of note principal and interest and future minimum lease payments as of December 31, 2005:

	Note Payable	Note Interest	Leases Payable
2006	\$ 324,348	\$ 64,386	\$ 55,037
2007	334,949	53,785	19,659
2008	345,767	42,968	-
2009	357,197	31,538	-
2010	217,331	21,298	-
2011-2015	<u>577,575</u>	<u>35,834</u>	<u>-</u>
Total payments	<u>\$ 2,157,167</u>	<u>\$ 249,809</u>	74,696
Less amount representing interest			<u>(2,737)</u>
Net present value			<u>\$ 71,959</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 6 - Long-term Debt (Continued)

The carrying value of equipment under capital lease obligations is as follows:

	2005	2004
Cost of equipment under capital lease	\$ 1,976,948	\$ 1,976,948
Less accumulated amortization	(1,261,619)	(1,097,721)
Net carrying amount	\$ 715,329	\$ 879,227

Note 7 - Accrued Liabilities

The details of accrued liabilities at December 31, 2005 and 2004 are as follows:

	2005	2004
Payroll and related items	\$ 509,209	\$ 437,459
Compensated absences	153,560	87,036
Workers' compensation premiums	225,503	177,228
Health insurance claims	129,164	124,449
Other	145,044	253,446
Total accrued liabilities	\$ 1,162,480	\$ 1,079,618

Note 8 - Cost Report Settlements

Approximately 57 percent of the Hospital's revenues from patient services are received from the Medicare and Medicaid programs. The Hospital has agreements with these payors that provide for reimbursement to the Hospital at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Hospital's established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursement with third-party payors follows.

- **Medicare** - Effective January 1, 2001, the Hospital received full accreditation from the Center for Medicare and Medicaid Services for the critical access hospital designation. As a critical access hospital, the Hospital will receive reasonable, cost-based reimbursement for both inpatient and outpatient services provided to Medicare beneficiaries.
- **Medicaid** - Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Capital costs relating to Medicaid patients are paid on a cost-reimbursement method. The Hospital is reimbursed for outpatient services on an established fee-for-service methodology.

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 8 - Cost Report Settlements (Continued)

The Medicaid payment system in Ohio is a prospective one, whereby rates for the following state fiscal year beginning July 1 are based upon filed cost reports for the preceding calendar year. The continuity of this system is subject to the uncertainty of the fiscal health of the State of Ohio, which can directly impact future rates and the methodology currently in place. Any significant changes in rates, or the payment system itself, could have a material impact on the future Medicaid funding to providers.

Cost report settlements result from the adjustment of interim payments to final reimbursement under these programs and are subject to audit by fiscal intermediaries. Although these audits may result in some changes in these amounts, they are not expected to have a material effect on the accompanying financial statements.

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

Note 9 - Net Patient Service Revenue

Net patient service revenue consists of the following:

	2005	2004
Patient revenue:		
Inpatient services:		
Routine services	\$ 900,139	\$ 736,946
Ancillary services	4,014,419	2,885,036
Outpatient ancillary services	18,379,805	17,132,933
Total patient revenue	23,294,363	20,754,915
Less:		
Provision for bad debt	486,240	425,060
Charity care	174,698	154,883
Contractual adjustments under third-party reimbursement programs	6,393,868	5,497,376
Total revenue deductions	7,054,806	6,077,319
Total	\$ 16,239,557	\$ 14,677,596

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 10 - Defined Benefit Pension Plan

Plan Description - The Hospital contributes to the Ohio Public Employees' Retirement System of Ohio (OPERS). OPERS administers three separate pension plans: The Traditional Pension Plan (TP) - a cost-sharing multiple-employer defined benefit pension plan; the Member-Directed Plan (MD) - a defined contribution plan; and the Combined Plan (CO) - a cost-sharing multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan. OPERS provides retirement, disability, survivor and death benefits, annual cost of living adjustments, and postretirement health care benefits to qualifying members of both the Traditional and the Combined Plans; however, health care benefits are not statutorily guaranteed. Members of the Member-Directed Plan do not qualify for ancillary benefits, including postemployment health care coverage. Chapter 145 of the Ohio Revised Code assigns authority to establish and amend benefit provisions to the OPERS board of trustees (the board). OPERS issues a stand-alone financial report. Interested parties may obtain a copy by making a written request to Ohio Public Employees' Retirement System, 277 East Town Street, Columbus, Ohio 43215-4642 or by calling 614-222-6705 or 1-800-222-PERS (7377).

Funding Policy - The Ohio Revised Code provides statutory authority for member and employer contributions. For 2004, member and employer contribution rates were consistent across all three plans (TP, MD, and CO), and are actuarially determined. The 2004 member contribution rate for members of local government units was 8.50 percent of their annual covered salary. The 2004 employer contribution rate for local government units was 13.55 percent of covered payroll. The Hospital's contributions to OPERS for the years ended December 31, 2005, 2004, and 2003 were \$1,031,341, \$957,456, and \$924,584, respectively. Required employer contributions for all plans are equal to 100 percent of employer charges and must be extracted from the employer's records.

Postretirement Benefits - In order to qualify for postretirement health care coverage, age and service retirees must have 10 or more years of qualifying Ohio service credit. Health care coverage for disability recipients and primary survivor recipients is available. The health care coverage provided by the Retirement System is considered an Other Postemployment Benefit (OPEB), as described in GASB Statement No. 12. A portion of each employer's contribution to OPERS is set aside for the funding of postretirement health care. The Ohio Revised Code provides statutory authority for employer contributions. The 2004 and 2003 employer contribution rate for local government employer units was 13.55 percent of covered payroll. Of this amount, 4.0 percent and 5.0 percent was the portion that was used to fund health care during 2004 and 2003, respectively. The portion of the employer's contribution used to fund postemployment benefits for 2004 and 2003 was \$282,644 and \$341,171, respectively. The Ohio Revised Code provides the statutory authority requiring public employers to fund post-retirement health care through their contributions to OPERS.

Note 10 - Defined Benefit Pension Plan (Continued)

An entry age normal actuarial cost method of valuation is used in determining the present value of OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of the unfunded actuarial accrued liability. All investments are carried at market value. For actuarial valuation purposes, a smoothed market approach is used. Under this approach, assets are adjusted to reflect 25 percent of unrealized market appreciation or depreciation on investment assets annually. The investment return assumption rate for 2003 was 8.00 percent. An annual increase of 4.00 percent, compounded annually, is the base portion of the individual pay increase assumption. This assumes no change in the number of active employees. Additionally, annual pay increases over and above the 4.00 percent base increase were assumed to range from 0.50 percent to 6.30 percent. Health care costs were assumed to increase at the projected wage inflation rate plus an additional factor ranging from 1.00 percent to 6.00 percent for the next eight years. In subsequent years (nine and beyond), health care costs were assumed to increase at 4.00 percent (the projected wage inflation rate) annually. These assumptions and calculations are based on the system's latest actuarial review performed as of December 31, 2003.

The number of active contributing participants in the Traditional and Combined Plans during 2004 was 369,885. As of December 31, 2003, the actuarial value of the Retirement System's net assets available for OPEB was \$10.5 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$26.9 billion and \$16.4 billion, respectively.

Health Care Plan - On September 9, 2004, the OPERS retirement board adopted a Health Care Preservation Plan (HCPP) with an effective date of January 1, 2007. The HCPP restructures the OPERS's health care coverage to improve the financial solvency of the fund in response to skyrocketing health care costs.

Under the HCPP, retirees eligible for health care coverage will receive a graded monthly allocation based on their years of service at retirement. The plan incorporates a cafeteria approach, offering a broad range of health care options that allow benefit recipients to use their monthly allocation to purchase health care coverage customized to meet their individual needs. If the monthly allocation exceeds the cost of the options selected, the excess is deposited into a retiree medical account that can be used to fund future health care expenses.

The 2005 information has not been published by OPERS as of the date of this report; therefore, this footnote represents the information available in 2004.

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 11 - Risk Management

Based on the nature of its operations, the Hospital is at times subject to pending or threatened legal actions, which arise in the normal course of its activities.

The Hospital was insured against medical malpractice claims under a claims-made policy, whereby only the claims reported to the insurance carrier during the policy period are covered regardless of when the incident giving rise to the claim occurred. Under the terms of the policy, the Hospital bears the risk of the ultimate costs of any individual claims exceeding \$1,000,000 or aggregate claims exceeding \$3,000,000 for claims asserted in the policy year. In addition, the Hospital has an umbrella policy with an additional \$5,000,000 of coverage.

Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on the occurrences during the policy term, but reported subsequent to the policy term, will be uninsured.

While there is pending litigation against the Hospital, management is not aware of any such medical malpractice claims, either asserted or unasserted, that would exceed the policy limits. The cost of this insurance policy represents the Hospital's cost for such claims for the year, and it has been charged to operations as a current expense. There have been no claims settled in the last three years that have exceeded insured limits.

The Hospital is exposed to various risks of loss related to property and general losses and employee injuries (workers' compensation). The Hospital has purchased commercial insurance for claims. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three years. See Note 13 for discussion of self-insured health programs.

Note 12 - Deferred Compensation Plan

All full-time employees of the Hospital may participate in a deferred compensation plan created by the State of Ohio under the provisions of Internal Revenue Code (IRC) Section 457, *Deferred Compensation Plans with Respect to Service for State and Local Governments*. Under the plan, employees may elect to defer a portion of their salaries and avoid paying taxes on the deferred portion until the withdrawal date. The deferred compensation amount is not available for withdrawal by employees until termination, retirement, death, or unforeseeable emergency.

Compensation assets deferred under a plan, all property, rights, and all income attributable to those amounts, property, or rights are held in trust at the state level for the benefit of the participants.

Paulding County Hospital

Notes to Financial Statements December 31, 2005 and 2004

Note 13 - Self-insurance

The Hospital is partially self-insured under a plan covering all employees for employee health insurance. The plan is covered by a stop-loss policy that covers claims over \$35,000 per employee or total claims in excess of \$760,515. The plan policy year ends on December 31. Claims, charged to operations when incurred, were approximately \$909,000 and \$836,000 for the years ended December 31, 2005 and 2004, respectively.

Reconciliation of accrued health insurance at December 31, 2005 and 2004 consists of the following:

Balance at January 1, 2004	\$ 174,213
Health insurance expense	886,000
Payments made	<u>(935,764)</u>
Balance at December 31, 2004	124,449
Health insurance expense	905,000
Payments made	<u>(900,285)</u>
Balance at December 31, 2005	<u>\$ 129,164</u>

Note 14 - Other Income (Expense)

At December 31, 2001, the Hospital maintained \$1.48 million of investments at a local bank. In February 2002, it was discovered the bank was defrauded of most of its assets. The Hospital was only insured for \$100,000 (FDIC) and was collateralized on additional amounts totaling \$95,620. Due to the uncertainty of recovering any of the funds beyond insured and collateralized amounts, the Hospital wrote down the uninsured portion of investments totaling \$1.29 million at December 31, 2001. The Hospital has recovered the insured and collateralized amounts as of December 31, 2004, as well as an additional \$512,869 of uninsured amounts, which were previously written down at December 31, 2001.

The details of other nonoperating gains (losses) at December 31, 2005 and 2004 are as follows:

	2005	2004
Recovery on uninsured investments	\$ -	\$ 21,531
Loss on disposal of capital assets	(126)	(40,671)
Other	<u>1,035</u>	<u>(30,027)</u>
Total other nonoperating gains (losses)	<u>\$ 909</u>	<u>\$ (49,167)</u>

Additional Information

Report on Internal Control and Compliance

To the Board of Directors
Paulding County Hospital

We have audited the financial statements of Paulding County Hospital (a component unit of Paulding County) as of and for the year December 31, 2005, and have issued our report thereon dated January 20, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance and Other Matters

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

Internal Control Over Financial Reporting

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

We noted certain matters that we reported to management of Paulding County Hospital in a separate letter dated January 20, 2006.

To the Board of Directors
Paulding County Hospital

This report is intended solely for the information and use of the auditor of the State of Ohio, the board of directors of Paulding County Hospital, and management and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Plante & Moran, PLLC

January 20, 2006



**Auditor of State
Betty Montgomery**

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PAULDING COUNTY HOSPITAL

PAULDING COUNTY

CLERK'S CERTIFICATION

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

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
MAY 4, 2006**