

**Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center**

Financial Report

06.30.2006

McGladrey & Pullen
Certified Public Accountants

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Henry County Soldiers' and Sailors'
 Memorial Hospital
 d/b/a Henry County Health Center

County Board of Supervisors, Hospital Board of Trustees and
 Hospital Officials
 June 30, 2006

Name	Title	Term Expires
County Board of Supervisors:		
Mark Lindeen	Chairperson	December 2006
Gary See	Co-chairperson	December 2008
Tom Young	Member	December 2008
Hospital Board of Trustees:		
Marvin Day	Chair	December 2006
Jan Towne	Chair-elect	December 2010
Kent Severson	Secretary/Treasurer	December 2010
David Roth	Trustee	December 2006
Richard Garrels	Trustee	December 2008
Carmen Heaton	Trustee	December 2006
Lee Benjamin	Trustee	December 2006
Hospital Officials:		
Dan Sheehan	President/Chief Executive Officer	
David Muhs	Chief Financial Officer	
Ann Corrigan, R.N.	VP of Patient Care Services	

McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report

To the Board of Trustees
Henry County Soldiers' and Sailors' Memorial Hospital
d/b/a Henry County Health Center
Mt. Pleasant, Iowa

We have audited the accompanying basic financial statements of Henry County Soldiers' and Sailors' Memorial Hospital, d/b/a Henry County Health Center (Hospital), as of and for the years ended June 30, 2006 and 2005, as listed in the table of contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our 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 basic financial statements referred to above present fairly, in all material respects, the financial position of Henry County Health Center as of June 30, 2006 and 2005, and the changes in its financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 28, 2006 on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

The management's discussion and analysis on pages 4 through 10 and budgetary comparison schedule on page 30 are not a required part of the basic financial statements, but are supplementary 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 supplementary information. However, we did not audit the information and express no opinion on it.

McGladrey & Pullen, LLP

Burlington, Iowa
July 28, 2006

**Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center**

**Management's Discussion and Analysis
Year Ended June 30, 2006**

Management's discussion and analysis of Henry County Health Center's (Hospital) financial performance provides an overall review of the Hospital's activities for the fiscal years ended June 30, 2006 and 2005. The intent of this discussion is to provide an overview of the Hospital's performance and should be read in conjunction with the Hospital's financial statements and notes thereto.

Henry County Health Center is a critical access hospital, operating with 25 acute-care beds and 49 long-term care beds and is located in Mount Pleasant, Iowa. Prior to May 1, 2004, the Hospital operated with 50 acute-care beds and 49 long-term care beds. Henry County Health Center primarily serves the citizens of Henry County.

Financial Highlights

The assets of the Hospital exceeded its liabilities by \$26,325,184 and \$22,348,497 as of June 30, 2006 and 2005, respectively.

The Hospital's total assets increased by \$4,361,169 or 11.2% from June 30, 2005 and increased by \$561,007 or 1.5% from June 30, 2004.

The Hospital's total liabilities increased by \$384,482 or 2.3% from June 30, 2005 and decreased by \$1,960,534 or 10.6% from June 30, 2004.

Overview of Financial Statements

The audited financial statements include the following financial statements: a Balance Sheet, a Statement of Revenue, Expenses and Changes in Net Assets, and a Statement of Cash Flows plus the Notes to Basic Financial Statements.

Our financial position is measured in terms of resources (assets) we own and obligations (liabilities) we owe at a given date. This information is reported in the Balance Sheet, which reflects the Hospital's assets in relation to its debts to bondholders, suppliers, employees, and other creditors. The excess of our assets over our liabilities is reported as Net Assets.

Information regarding the results from operations during the year is reported in the Statement of Revenue, Expenses and Changes in Net Assets. This statement shows how much our net assets increased or decreased during the year as a result of our operations, nonoperating activities, and other changes.

The Statement of Cash Flows discloses the flow of cash resources into and out of the Hospital during the year. It identifies all cash received during the year from operating activities, contributions and other sources, and how we applied those funds (for example, payment of expenses, repayment of debt, purchases of new property and equipment and additions and deletions to the investment accounts).

The Notes to Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Management's Discussion and Analysis
Year Ended June 30, 2006

Condensed Statements of Revenue, Expenses and Changes in Net Assets

A summary version of the Statements of Revenue, Expenses and Changes in Net Assets for the years ended June 30, 2006, 2005, and 2004 follows:

	2006	2005	2004
Net patient revenue	\$ 26,235,000	\$ 24,320,000	\$ 19,578,000
Other operating revenue	1,631,000	1,582,000	1,414,000
Total operating revenue	27,866,000	25,902,000	20,992,000
Nonoperating revenue	942,000	451,000	412,000
Total revenue	28,808,000	26,353,000	21,404,000
Expenses:			
Salaries and wages	10,021,000	9,571,000	8,975,000
Purchased services and other	11,864,000	10,915,000	9,819,000
Depreciation	2,069,000	2,323,000	2,241,000
Interest and amortization	877,000	1,023,000	1,081,000
Total operating expenses	24,831,000	23,832,000	22,116,000
Change in net assets	3,977,000	2,521,000	(712,000)
Net assets:			
Beginning	22,348,000	19,827,000	20,539,000
Ending	\$ 26,325,000	\$ 22,348,000	\$ 19,827,000

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Management's Discussion and Analysis
Year Ended June 30, 2006

Operations

Year Ended June 30, 2006: Net patient revenue was up \$1,915,000 to \$26,235,000 in 2006 from \$24,320,000 in 2005, a 7.8% increase. Outpatient volume increased from 127,391 visits to 143,293 in 2006. Actual acute patient days decreased 101 days to 4,526 days in 2006 compared to 4,627 days in 2005. Medicare revenue as a percent of total revenue decreased from 49.2% of total patient revenue in 2005 to 48.5% of total patient revenue in 2006. The year ended June 30, 2006 was the Hospital's second full year under the new federal reimbursement Critical Access Hospital, which provides reimbursement of 101% of allowable costs for patient care.

Operating expenses for 2006 were up \$999,000 or 4.2% over 2005. Salaries and wages were up \$450,000 or 4.7% due to general wage increases and overtime demands. Purchased services and other expenses were up \$950,000 or 8.7% from 2006 mainly attributable to new and advanced oncology drugs.

Operating income totaled \$3,034,800 for the year ended June 30, 2006. This resulted in an increase of \$964,000 compared to the prior year operating income of \$2,071,000 in 2005.

Year Ended June 30, 2005: Net patient revenue was up \$4,742,000 to \$24,320,000 in 2005 from \$19,578,000 in 2004, a 24% increase. Outpatient volume increased from 109,784 visits to 127,391 in 2005. Actual acute patient days decreased 544 days to 4,627 days in 2005 compared to 5,171 days in 2004. Medicare revenue as a percent of total revenue increased from 48.4% of total patient revenue in 2004 to 49.2% of total patient revenue in 2005. The year ended June 30, 2005 was the Hospital's first full year under the new federal reimbursement Critical Access Hospital, which provides reimbursement of 101% of allowable costs for patient care.

Operating expenses for 2005 were up \$1,716,000 or 8% over 2004. Salaries and wages were up \$594,000 or 7% due to general wage increases and overtime demands. Purchased services and other expenses were up \$1,099,000 or 11% from 2004 mainly attributable to new and advanced oncology drugs.

Operating income totaled \$2,071,000 for the year ended June 30, 2005. This resulted in an increase of \$3,129,000 compared to the prior year loss of \$1,058,000 in 2004.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Management's Discussion and Analysis
Year Ended June 30, 2006

Condensed Balance Sheets

Condensed versions of the Balance Sheets as of June 30, 2006, 2005, and 2004 follows:

	June 30,		
	2006	2005	2004
Assets:			
Current assets	\$ 8,584,000	\$ 8,237,000	\$ 7,185,000
Assets limited as to use, noncurrent	12,387,000	8,633,000	8,591,000
Capital assets	18,329,000	18,616,000	19,364,000
Other assets	3,993,000	3,446,000	3,231,000
Total assets	\$ 43,293,000	\$ 38,932,000	\$ 38,371,000
Liabilities:			
Current liabilities	\$ 3,998,000	\$ 3,294,000	\$ 3,689,000
Long-term debt	12,970,000	13,290,000	14,855,000
Total liabilities	\$ 16,968,000	\$ 16,584,000	\$ 18,544,000
Net Assets:			
Invested in capital assets, net of related debt	\$ 5,469,000	\$ 5,501,000	\$ 3,854,000
Restricted:			
Endowment	-	6,000	6,000
Under loan agreement	4,686,000	2,111,000	2,652,000
Unrestricted	16,170,000	14,730,000	13,315,000
Total net assets	\$ 26,325,000	\$ 22,348,000	\$ 19,827,000

The Hospital's financial position remains strong, with current assets in excess of current liabilities by \$4,586,000 in 2006 and by \$4,943,000 in 2005. Also, significant investment reserves are available to service debt requirements as well as provide for future equipment and capital needs.

For 2006, long-term debt consists of revenue bonds issued in 2000 and 2002. The Hospital continues to make all annual and semi-annual debt service payments in compliance with these bond indentures. There are no current plans to issue additional debt or defease any existing debt. Please see the Notes to Basic Financial Statements for additional information.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Management's Discussion and Analysis
Year Ended June 30, 2006

Condensed Statements of Cash Flows

Cash flows from operating activities remains strong in 2006 and all years presented, even with the loss from operations in 2004. The Hospital has no plans to issue additional bonds or acquire any significant capital assets outside the normal course of business.

	Year Ended June 30,		
	2006	2005	2004
Cash provided by operating activities	\$ 6,851,000	\$ 4,692,000	\$ 2,239,000
Cash (used in) capital and related financing activities	(3,279,000)	(4,812,000)	(2,355,000)
Cash provided by non-capital financing activities	451,000	434,000	491,000
Cash provided by (used in) investing activities	(2,749,000)	950,000	(533,000)
Net increase (decrease) in cash	1,274,000	1,264,000	(158,000)
Cash and cash equivalents:			
Beginning	2,562,000	1,298,000	1,456,000
Ending	<u>\$ 3,836,000</u>	<u>\$ 2,562,000</u>	<u>\$ 1,298,000</u>

Budgetary Highlights

Cash revenue/receipts did not meet the budget projection by \$1,626,007 during the year ended June 30, 2006. Expenditures were under budget by \$3,999,425 for the year ended June 30, 2006.

Cash revenue/receipts did not meet the budget projection by \$4,926,511 during the year ended June 30, 2005. Expenditures were under budget by \$3,591,093 for the year ended June 30, 2005.

The budget was amended in April of 2004 from budgeted expenditures of \$20,535,254 to \$25,119,399 to move from a cash basis to an accrual basis. Expenditures were under budget by \$2,937,000 for the year ended June 30, 2004.

Cash revenue/receipts did not meet the amended budget projection by \$987,611 during the year ended June 30, 2004. This was mostly attributable to reclassification of bad debt expenses as a reduction of net patient revenue. Expenditures were under budget by \$2,936,844.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Management's Discussion and Analysis
Year Ended June 30, 2006

Capital Assets

At June 30, 2006, the Hospital had \$18,329,000 invested in capital assets. This represents a 2% decrease in comparison to June 30, 2005. This is due to a combination of more assets being fully depreciated and the fact that capital expenditures were \$2,161,000, compared to annual depreciation in 2006 totaling \$2,335,464.

At June 30, 2005, the Hospital had \$18,616,000 invested in capital assets. This represents a 4% decrease in comparison to June 30, 2004. This is principally due to the fact that capital expenditures were \$1,960,000 compared to annual depreciation in 2005 totaling \$2,593,026.

At June 30, 2004, the Hospital had \$19,364,000 invested in capital assets. This represents a 9% decrease in comparison to June 30, 2003. This is principally due to the fact that capital expenditures were \$705,000 compared to annual depreciation in 2004 totaling \$2,509,000.

	June 30,		
	2006	2005	2004
Capital assets not being depreciated:			
Land	\$ 788,000	\$ 788,000	\$ 788,000
Construction in progress	28,000	27,000	-
Capital assets net of depreciation:			
Land improvements	213,000	244,000	307,000
Buildings	12,518,000	13,011,000	13,480,000
Fixed equipment	1,745,000	1,997,000	2,241,000
Major movable equipment	3,037,000	2,549,000	2,548,000
Total capital assets, net	\$ 18,329,000	\$ 18,616,000	\$ 19,364,000

Long-Term Debt

Long-term debt consists of two revenue bond issues, described in more detail in the Notes to Basic Financial Statements. At June 30, 2006 the Hospital had \$13,290,000 in bonds outstanding, versus \$13,610,000 at June 30, 2005 and \$15,510,000 at June 30, 2004. The decrease is attributable to bond principal payments made in 2006 and 2005.

Economic Factors

Fiscal 2006 and 2005 provided Henry County Health Center an increase in net reimbursement from third-party payors due to the election to become a Critical Access Hospital. Investments rebounded from the prior year and showed an increase in return.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Management's Discussion and Analysis
Year Ended June 30, 2006

Economic Factors (Continued)

Inflation continued in 2006 and 2005 with supply and equipment costs increasing at market rates and the pressure on nursing and other salary costs being driven by the shortage of supply of these health care professionals. Investments stabilized during 2005, recouping some of the loss recognized in 2004.

On May 1, 2004 the Hospital was designated a Critical Access Hospital operating with 25 beds. This critical access status has increased in net patient revenue.

Financial Information Contact

The Hospital's financial statements are designed to provide a general overview of the Hospital's finances for all those with an interest in the Hospital's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Henry County Health Center, 407 S. White Street, Mt. Pleasant, Iowa 52641.

Henry County Soldiers' and Sailors'
 Memorial Hospital
 d/b/a Henry County Health Center

Balance Sheets
 June 30, 2006 and 2005

Assets	2006	2005
Current Assets:		
Cash and cash equivalents (Note 3)	\$ 2,957,680	\$ 2,109,805
Assets whose use is limited or restricted (Note 3)	386,353	387,836
Patient receivables, net (Note 4)	3,175,683	3,708,519
Other receivables (Note 5)	333,912	285,419
Current portion of long-term receivable (Note 6)	42,449	89,488
Inventories	616,738	568,880
Prepaid expenses	643,357	655,505
Restricted assets:		
Property tax receivable	427,486	425,677
Other receivables	-	6,155
Total current assets	8,583,658	8,237,284
Noncurrent Assets:		
Investments (Note 3)	1,956,468	1,587,270
Other long-term assets (Notes 5 and 6)	1,607,129	1,363,579
Assets whose use is limited or restricted (Note 3)	12,387,027	8,633,107
Capital assets, net (Notes 7 and 8)	18,329,179	18,616,467
Deferred financing costs	429,869	494,454
Total noncurrent assets	34,709,672	30,694,877
	\$ 43,293,330	\$ 38,932,161

See Notes to Basic Financial Statements.

Liabilities and Net Assets	2006	2005
Current Liabilities:		
Current maturities of long-term debt (Note 8)	\$ 320,000	\$ 320,000
Accounts payable (Note 5)	1,466,514	872,034
Accrued expenses (Note 4)	1,224,146	1,250,953
Contractual payables, Medicare, Medicaid and Blue Cross	560,000	425,000
Restricted liability, deferred revenue	427,486	425,677
Total current liabilities	3,998,146	3,293,664
 Long-Term Debt, net of current maturities (Note 8)	 12,970,000	 13,290,000
Total liabilities	16,968,146	16,583,664
 Commitments and Contingencies (Notes 10 and 11)		
 Net Assets:		
Invested in capital assets, net of related debt	5,469,048	5,500,921
Restricted:		
Taxes receivable	-	6,155
Under bond agreements	4,685,878	2,111,372
Unrestricted	16,170,258	14,730,049
	26,325,184	22,348,497
	\$ 43,293,330	\$ 38,932,161

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Statements of Revenue, Expenses, and Changes in Net Assets
Years Ended June 30, 2006 and 2005

	2006	2005
Operating revenue:		
Net patient service revenue (Notes 2 and 8)	\$ 26,234,712	\$ 24,319,704
Other operating revenue, other than tax revenue (Note 5)	1,203,113	1,156,602
Total operating revenue other than tax aid	27,437,825	25,476,306
Operating expenses:		
Nursing services	7,276,677	6,921,168
Other professional services	8,577,449	8,278,671
General services and administration (Note 11)	6,031,457	5,286,040
Interest and amortization	877,140	1,022,742
Depreciation (Note 7)	2,068,698	2,323,283
Total operating expenses	24,831,421	23,831,904
Operating income before county tax revenue	2,606,404	1,644,402
County tax revenue	428,370	426,387
Operating income	3,034,774	2,070,789
Nonoperating revenue:		
Investment earnings from funds whose use is limited or restricted	438,747	280,413
Net decrease in fair value of investments	(159,513)	(82,223)
Gain from equity investments	361,886	86,834
Other investment earnings	164,835	61,491
Unrestricted gifts	16,586	7,959
Rental activities, net	119,372	96,278
Change in net assets	3,976,687	2,521,541
Net assets:		
Beginning	22,348,497	19,826,956
Ending	\$ 26,325,184	\$ 22,348,497

See Notes to Basic Financial Statements.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Statements of Cash Flows
Years Ended June 30, 2006 and 2005

	2006	2005
Cash Flows from Operating Activities:		
Cash received from patients and third-party payors	\$ 27,892,548	\$ 25,177,710
Cash payments for supplies and other expenses	(12,292,470)	(11,800,866)
Cash payments for salaries and wages	(9,952,011)	(9,841,862)
Other receipts	1,203,113	1,156,602
Net cash provided by operating activities	6,851,180	4,691,584
Cash Flows from Capital and Related Financing Activities:		
Principal payments on long-term borrowing	(320,000)	(1,900,000)
Payments of interest	(814,037)	(958,221)
Acquisition and construction of capital assets	(2,161,232)	(1,960,134)
Proceeds from sale of capital assets	15,400	6,199
Net cash (used in) capital and related financing activities	(3,279,869)	(4,812,156)
Cash Flows from Non-Capital Financing Activities:		
Cash received from county tax revenue	434,635	426,497
Unrestricted gifts	16,586	7,959
Net cash provided by non-capital financing activities	451,221	434,456
Cash Flows from Investing Activities:		
Disbursements on long-term receivables	(7,199)	(38,879)
Collection of long-term receivables	9,072	89,438
Other receivables	-	50,480
Purchase of investment securities	(7,761,462)	(6,076,792)
Proceeds from sale and maturity of investment securities	3,959,541	6,078,064
Investment income from board-designated funds	438,747	280,413
Other investment income	225,569	202,983
Rental activities, net	386,138	364,941
Net cash provided by (used in) investing activities	(2,749,594)	950,648
Increase in cash and cash equivalents	1,272,938	1,264,532
Cash and Cash Equivalents:		
Beginning	2,562,468	1,297,936
Ending, including cash and cash equivalents in long-term investments and assets whose use is limited or restricted 2006 \$883,908; 2005 \$452,663	\$ 3,835,406	\$ 2,562,468

(Continued)

Henry County Soldiers' and Sailors'
 Memorial Hospital
 d/b/a Henry County Health Center

Statements of Cash Flows (Continued)
 Years Ended June 30, 2006 and 2005

	2006	2005
Reconciliation of Operating Income to Net Cash		
Provided by Operating Activities:		
Operating income	\$ 3,034,774	\$ 2,070,789
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation	2,068,698	2,323,283
Amortization	64,585	76,811
Interest expense	812,555	945,931
Loss on disposal of property and equipment	97,656	108,338
County tax revenue	(428,370)	(426,387)
Change in assets and liabilities:		
Patient receivables	532,836	(138,894)
Inventories	(47,858)	7,228
Prepaid expense	12,148	(218,715)
Accounts payable	594,480	356,309
Accrued expenses, other than interest	(25,324)	(301,698)
Contractual payables	135,000	(111,411)
Net cash provided by operating activities	\$ 6,851,180	\$ 4,691,584

See Notes to Basic Financial Statements.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Notes to Basic Financial Statements

Note 1. Description of Reporting Entity and Significant Accounting Policies

Henry County Soldiers' and Sailors' Memorial Hospital d/b/a Henry County Health Center (Hospital), is a Critical Access Hospital, operating with 25 acute-care beds and 49 long-term care beds. The Hospital also has related health care ancillary and outpatient services. The Hospital is organized under Chapter 347 of the Code of Iowa as amended and, accordingly, receives county tax aid from Henry County, Iowa.

Financial reporting entity: Accounting principles generally accepted in the United States of America require the financial reporting entity to include (1) the primary government, (2) organizations for which the primary government is financially accountable and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading. The Hospital was organized in 1919 under Chapter 347 of the Iowa Code. The Hospital is a municipal corporation governed by a Board of Trustees, which is elected by the public and has the exclusive responsibility and accountability for the decisions it makes. It has the right to sue and to be sued and has the right to buy, sell, lease or mortgage property in its own name. Based upon this criteria, the Henry County Soldiers' and Sailors' Memorial Hospital is considered a primary government and there are no agencies or entities which should be presented with the Hospital.

A summary of the Hospital's significant accounting policies follows:

Basis of accounting: The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Revenue is recognized when earned and expenses are recorded when the liability is incurred.

In reporting its financial activities, the Hospital applies all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as following Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements.

Cash and cash equivalents: For purposes of reporting cash flows, the Hospital classifies checking and savings accounts and certificates of deposit with an original maturity of three months or less as cash equivalents.

Patient receivables: Patient receivables, where a third-party payor is responsible for paying the amount, are carried at a net amount determined by the original charge for the service provided, less an estimate made for contractual adjustments or discounts provided to third-party payors.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Notes to Basic Financial Statements

Note 1. Description of Reporting Entity and Significant Accounting Policies (Continued)

Patient receivables due directly from the patients are carried at the original charge for the service provided, less amounts covered by third-party payors and less an estimated allowance for doubtful receivables based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by identifying troubled accounts, by historical experience applied to an aging of accounts and by considering the patient's financial history, credit history and current economic conditions. The Hospital does not charge interest on patient receivables. Patient receivables are written off as bad debt expense when deemed uncollectible. Recoveries of receivables previously written off are recorded as a reduction of bad debt expense when received.

Receivables or payables related to estimated settlements on various risk contracts that the Hospital participates in are reported as third-party payor receivables or payables.

Property tax receivable: Property tax receivable is recognized on the levy or lien date, which is the date that the tax asking is certified by the County Board of Supervisors. The property tax receivable represents taxes certified by the Board of Supervisors to be collected in the next fiscal year for the purposes set out in the budget for the next fiscal year. By statute, the Board of Supervisors is required to certify the budget in March of each year for the subsequent fiscal year. However, by statute, the tax asking and budget certification for the following fiscal year becomes effective on the first day of that year. Although the property tax receivable has been recorded, the related revenue is deferred and will not be recognized as revenue until the year for which it is levied.

Assets whose use is limited or restricted: Assets whose use is limited or restricted, include assets set aside by the Board of Trustees over which the Board retains control and may at its discretion subsequently use for other purposes and assets held by a trustee under indenture agreements.

Inventories: Inventories are stated at the lower of cost (first-in, first-out method) or market.

Investments and investment earnings: Investments in equity securities with readily determinable fair values and all debt securities are reported at fair value as determined by quoted market prices. Investment income or loss, including realized and unrealized gains and losses on investments, interest and dividends, is included in the nonoperating revenue. The calculation of realized gains and losses is independent of a calculation of the net change in the fair value of investments. Realized gains and losses on investments that have been held for more than one fiscal year and sold in the current year were included as a change in the fair value of investments reported in prior years and the current year. The investments in joint ventures and cooperative arrangements with other health care entities are accounted for by the equity method of accounting, under which the net income or loss of the affiliates is recognized as income or expense and distributions are treated as reductions to the investment account. The Hospital has a 25% interest in Southeastern Renal Dialysis, L.C.; a 50% interest in Superior Ambulance, L.C.; a 33% interest in Crossroads Health Partners, L.C.; a 50% interest in Southeastern Health Group, L.C.; and a 49% interest in Henry County Medical Software, L.L.C.

Capital assets: Capital assets are carried at cost including interest capitalized during construction activities. Depreciation of capital assets is computed by the straight-line method over estimated useful lives ranging from 3 to 40 years.

Henry County Soldiers' and Sailors'
Memorial Hospital
d/b/a Henry County Health Center

Notes to Basic Financial Statements

Note 1. Description of Reporting Entity and Significant Accounting Policies (Continued)

Deferred financing costs: Deferred financing costs are amortized over the period the obligation is outstanding using the interest method.

Paid time off and short-term disability: The Hospital accrues a liability for paid time off in the year in which it is earned.

Short-term disability does not vest and, therefore, no liability has been accrued. The payment for short-term disability is based on 70% of the regular earnings of the employee and is available for up to eight weeks.

Self-insured employee health benefits: The estimated losses from self-insured claims, including incurred but unreported claims, are accrued as the losses occur.

Income taxes: Under the Code of Iowa, Chapter 347, the Hospital is an instrumentality of the County of Henry, Iowa. As such, the Hospital is exempt from paying income taxes.

Net patient service revenue: Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Net patient service revenue is reported net of provision for bad debts.

Operating income: The Hospital distinguishes operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from the primary purpose of the Hospital, which is to provide medical services to the region. Operating revenue consists of net patient services, cafeteria and special meals, Wellness Center membership, and other miscellaneous services as well as county tax revenue. Operating expenses consist of salaries and benefits, purchased services, supplies, provision for doubtful accounts, depreciation and amortization and interest. All revenue and expenses not meeting these criteria are considered nonoperating.

Net assets: Net asset classifications are defined as follows:

Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including any restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition, construction or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

Restricted – This component of net assets consists of constraints placed on net assets through external constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt," above.

Henry County Soldiers' and Sailors'
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d/b/a Henry County Health Center

Notes to Basic Financial Statements

Note 1. Description of Reporting Entity and Significant Accounting Policies (Continued)

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 revenue. The Hospital maintains records to identify and monitor the level of charity care it provides. Based on the equivalent revenue for the services provided, charity care totaled approximately \$247,000 and \$125,000 for the years ended June 30, 2006 and 2005, respectively.

Note 2. Net Patient Service Revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors through June 30, 2006 is as follows.

Medicare – Effective May 1, 2004, the Hospital was designated as a Critical Access Hospital. This designation provides for inpatient and outpatient services to be reimbursed on a cost basis methodology. The Hospital is reimbursed at a reasonable cost methodology at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits by the third-party Medicare fiscal intermediary.

The Hospital's Medicare cost reports have been audited and finalized by the Medicare fiscal intermediary through June 30, 2005.

Medicaid – Inpatient acute-care services rendered under the Medicaid program are also paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Outpatient services rendered to Medicaid program beneficiaries are reimbursed primarily under a prospective payment category of service. The Hospital's Medicaid cost reports have been finalized by the Medicaid fiscal intermediary through June 30, 2005.

Blue Cross – Inpatient services rendered to Blue Cross subscribers are reimbursed at prospectively determined rates per day of hospitalization.

A summary of net patient service revenue is as follows:

	2006	2005
Gross patient service revenue	\$ 38,676,411	\$ 36,290,144
Less discounts, allowances, charity care and estimated contractual adjustments under third-party reimbursement programs	11,426,099	10,602,240
Less provision for bad debts	1,015,600	1,368,200
	<u>\$ 26,234,712</u>	<u>\$ 24,319,704</u>

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 3. Cash, Investments and Assets Whose Use is Limited or Restricted

State statutes authorize the Hospital to invest in notes, savings accounts, certificates of deposit, bonds, prime eligible bankers acceptances, commercial paper rated within the two highest classifications of prime, perfected repurchase agreements, or other evidence of indebtedness which are obligations of or guaranteed by the U.S. government or its agencies. The statutes also require all of the Hospital's bank deposit accounts to be protected by insurance, surety bond or collateral, and that securities pledged as collateral be held in safekeeping by the state treasurer or in a financial institution other than that furnishing the collateral.

Custodial credit risk: Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Hospital's investment policy requires the fund to be deposited into banking institutions that have the ability to collateralize any deposits made in excess of the Federal Deposit Insurance Corporation's insurance limits.

As of June 30, 2006, the carrying amount of the Hospital's deposits was \$3,984,368 and the bank balance was \$4,037,072. All bank deposit account balances of the Hospital are fully insured or collateralized by securities held by the Hospital's agent in the Hospital's name.

The Hospital's investments are categorized as follows to give an indication of the level of credit assumed by the Hospital (1) insured or registered, or the securities are held by the Hospital or its agent in the Hospital's name, (2) uninsured and unregistered, with the securities held by the counterparty's trust department or agent in the Hospital's name, and (3) uninsured and unregistered with the securities held by the counterparty or its agent but not in the Hospital's name.

	Category			Fair Value
	1	2	3	
U.S. Treasury securities	\$ 10,136,034	\$ -	\$ -	\$ 10,136,034
U.S. government agencies securities	2,579,906	-	-	2,579,906
	<u>\$ 12,715,940</u>	<u>\$ -</u>	<u>\$ -</u>	<u>12,715,940</u>
Investments not subject to risk categorization, money market mutual funds				986,945
				<u>\$ 13,702,885</u>

The Hospital invests in money market funds which are SEC registered external investment pools. The fair value of the position in the external investment pool is the same as the value of the pool shares. During the years ended June 30, 2006 and 2005, the Hospital's cash and investments did not vary in level of risk from those at year-end.

Henry County Soldiers' and Sailors'
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d/b/a Henry County Health Center

Notes to Basic Financial Statements

Note 3. Cash, Investments and Assets Whose Use is Limited or Restricted (Continued)

Authorized Investments: Under the provisions of the Hospital's investment policy, the Board of Trustees designates certain Hospital personnel to invest or deposit in the following types of investments: (1) interest-bearing savings accounts, interest-bearing money market accounts, and interest-bearing checking accounts at any bank, savings and loan association or credit union in the State of Iowa. Each bank must be on the most recent approved bank list as distributed by the Treasurer of the State of Iowa or as amended as necessary by notice inserted in the monthly mailing by the Rate Setting Committee. Deposits in any one financial institution shall not exceed the stated amount on the bank resolution approved by the Board of Trustees; (2) obligations of the United States government, its agencies and instrumentalities; (3) certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions approved and secured pursuant to Chapter 453 of the Code of Iowa and (4) membership units in entities providing services to Henry County Health Center upon special authorization of the Board of Trustees.

Disclosures Relating to Interest Rate Risk: Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the Hospital manages its exposure to interest rate risk is by purchasing a combination of short-term and long-term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time.

Information about the sensitivity of the fair values of the Hospital's investments to market interest rate fluctuations is provided by the following table that shows the distribution of the Hospital's investments by maturity.

	Total	Remaining Maturity (in Months)					
		12 Months or Less	24 Months or Less	36 Months or Less	48 Months or Less	60 Months or Less	96 Months or Less
Money Market Mutual Funds	\$ 986,945	\$ 986,945	\$ -	\$ -	\$ -	\$ -	\$ -
Certificates of Deposit	1,130,000	-	-	-	630,000	-	500,000
U.S. Treasury Securities	10,136,034	2,001,250	2,736,836	2,231,195	-	2,926,265	240,488
U.S. Government Agencies Securities	623,438	623,438	-	-	-	-	-
	<u>\$12,876,417</u>	<u>\$ 3,611,633</u>	<u>\$ 2,736,836</u>	<u>\$ 2,231,195</u>	<u>\$ 630,000</u>	<u>\$ 2,926,265</u>	<u>\$ 740,488</u>

Disclosures Relating to Credit Risk: Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The Hospital's money market funds are rated AA- by the S&P 500 and the remaining investments are unrated.

Investments whose use is not limited by the Hospital as of June 30, 2006 and 2005 are as follows:

	2006	2005
U.S. government agencies securities	\$ 1,956,468	\$ 1,587,270

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 3. Cash, Investments and Assets Whose Use is Limited or Restricted (Continued)

The composition of assets whose use is limited or restricted as of June 30, 2006 and 2005 is as follows:

	2006	2005
By the Board of Trustees for:		
Capital improvements:		
Money market funds	\$ 524,590	\$ 106,718
U.S. Treasury securities	6,939,474	6,290,663
U.S. government agencies securities	623,438	512,190
Total assets whose use is limited	8,087,502	6,909,571
Restricted under bond agreements:		
Reserve account:		
Money market funds	-	360
Certificates of deposit	1,130,000	630,000
U.S. Treasury securities	-	379,876
U.S. government agencies securities	-	128,048
	1,130,000	1,138,284
Sinking fund account:		
Money market funds	359,318	345,585
U.S. Treasury securities	3,196,560	627,503
	3,555,878	973,088
Total restricted under bond agreements	4,685,878	2,111,372
Total assets whose use is limited or restricted	12,773,380	9,020,943
Less assets whose use is limited or restricted that are required for current liabilities	386,353	387,836
Long-term portion	\$ 12,387,027	\$ 8,633,107

Payments made in connection with the Hospital's debt service are held by the trustee until disbursed to the bondholders or as a bond reserve for the protection of bondholders. The current portion of assets whose use is limited or restricted is based on the classification of liabilities to be liquidated by those assets.

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 4. Composition of Patient Receivables

Patient receivables as of June 30, 2006 and 2005 consist of the following:

	2006	2005
Patient accounts	\$ 5,452,825	\$ 6,073,519
Less estimated third-party contractual adjustments and unapplied interim payments	1,240,000	1,240,000
Less allowance for doubtful accounts	1,037,142	1,125,000
	<u>\$ 3,175,683</u>	<u>\$ 3,708,519</u>

The Hospital grants credit without collateral to its patients, most of who are area residents and are insured under third-party payor agreements. The approximate mix of receivables from patients and third-party payors as of June 30, 2006 and 2005 is as follows:

	2006	2005
Medicare	21%	20%
Patients	24	23
Other third-party payors	21	28
Blue Cross	26	22
Medicaid	8	7
	<u>100%</u>	<u>100%</u>

Note 5. Related Parties

The Hospital is affiliated with Southeastern Renal Dialysis, L.C. (Southeastern); Superior Ambulance, L.C.; Crossroads Health Partners, L.C.; Southeastern Health Group, L.C.; and Henry County Medical Software, L.L.C. (Software) limited liability companies.

The Hospital performs certain management and accounting functions for these affiliates which resulted in other operating income totaling \$71,672 and \$80,950 for the years ended June 30, 2006 and 2005, respectively. The Hospital also leases real estate to Southeastern under a month-to-month agreement. Rent income related to this agreement totaled \$41,714 and \$32,800 for the years ended June 30, 2006 and 2005, respectively. These transactions and cash advances to the affiliates resulted in accounts receivable totaling \$6,405 and \$8,400 as of June 30, 2006 and 2005, respectively.

Southeastern performs inpatient hemodialysis services for the Hospital which totaled \$25,000 for each of the years ended June 30, 2006 and 2005 and resulted in accounts payable to the affiliate totaling \$2,505 and \$9,306 as of June 30, 2006 and 2005, respectively.

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 6. Other Long-Term Assets

Other long-term assets held by the Hospital as of June 30, 2006 and 2005 are as follows:

	2006	2005
Investments in joint ventures and cooperative arrangements with other health care entities	\$ 1,036,893	\$ 811,326
Physician receivables	231,453	222,381
Notes receivable	381,232	419,360
	<u>1,649,578</u>	<u>1,453,067</u>
Less current portion	42,449	89,488
	<u>\$ 1,607,129</u>	<u>\$ 1,363,579</u>

Note 7. Capital Assets

The composition of the capital assets and the related accumulated depreciation is as follows:

	June 30, 2005	Additions	Transfers and Disposals	June 30, 2006
Capital assets, not being depreciated:				
Land	\$ 788,325	-	-	\$ 788,325
Construction in progress	26,888	27,917	26,888	27,917
Total capital assets, not being depreciated	<u>815,213</u>	<u>27,917</u>	<u>26,888</u>	<u>816,242</u>
Capital assets, being depreciated:				
Land improvements	1,483,099	12,680	-	1,495,779
Buildings	23,005,850	601,452	220,009	23,387,293
Fixed equipment	7,284,194	-	173,535	7,110,659
Major movable equipment	10,025,930	1,546,071	931,546	10,640,455
Total capital assets, being depreciated	<u>41,799,073</u>	<u>2,160,203</u>	<u>1,325,090</u>	<u>42,634,186</u>
Less accumulated depreciation for:				
Land improvements	1,239,232	44,129	-	1,283,361
Buildings	9,994,913	1,025,000	150,583	10,869,330
Fixed equipment	5,287,006	231,381	152,719	5,365,668
Major movable equipment	7,476,668	1,034,954	908,732	7,602,890
Total accumulated depreciation	<u>23,997,819</u>	<u>2,335,464</u>	<u>1,212,034</u>	<u>25,121,249</u>
Total capital assets, being depreciated, net	17,801,254	(175,261)	113,056	17,512,937
Organization capital assets, net	<u>\$ 18,616,467</u>	<u>\$ (147,344)</u>	<u>\$ 139,944</u>	<u>\$ 18,329,179</u>

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 7. Capital Assets (Continued)

	June 30, 2004	Additions	Transfers and Disposals	June 30, 2005
Capital assets, not being depreciated:				
Land	\$ 788,325	\$ -	\$ -	\$ 788,325
Construction in progress	-	26,888	-	26,888
Total capital assets, not being depreciated	788,325	26,888	-	815,213
Capital assets, being depreciated:				
Land improvements	1,483,098	-	-	1,483,099
Buildings	22,455,871	549,979	-	23,005,850
Fixed equipment	7,371,510	5,060	92,375	7,284,194
Major movable equipment	9,629,218	1,378,207	981,495	10,025,930
Total capital assets, being depreciated	40,939,697	1,933,246	1,073,870	41,799,073
Less accumulated depreciation for:				
Land improvements	1,175,698	63,534	-	1,239,232
Buildings	8,976,325	1,018,588	-	9,994,913
Fixed equipment	5,130,834	244,025	87,853	5,287,006
Major movable equipment	7,081,269	1,266,879	871,480	7,476,668
Total accumulated depreciation	22,364,126	2,593,026	959,333	23,997,819
Total capital assets, being depreciated, net	18,575,571	(659,780)	114,537	17,801,254
Organization capital assets, net	\$ 19,363,896	\$ (632,892)	\$ 114,537	\$ 18,616,467

Depreciation expense for the years ended June 30, 2006 and 2005 includes depreciation expense on rental activities of \$266,766 and \$269,743, respectively, which is classified as nonoperating revenue.

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 8. Long-Term Debt

Long-term debt activity as of and for the years ended June 30, 2006 and 2005 is as follows:

	June 30, 2005	Borrowings	Payments	June 30, 2006	Due Within One Year
Series 2000 (A) (C)	\$ 7,960,000	\$ -	\$ (165,000)	\$ 7,795,000	\$ 205,000
Series 2002 (B) (C)	5,650,000	-	(155,000)	5,495,000	115,000
	<u>\$ 13,610,000</u>	<u>\$ -</u>	<u>\$ (320,000)</u>	<u>\$ 13,290,000</u>	<u>\$ 320,000</u>

	June 30, 2004	Borrowings	Payments	June 30, 2005	Due Within One Year
Series 1990B	\$ 1,595,000	\$ -	\$ (1,595,000)	\$ -	\$ -
Series 2000 (A) (C)	8,095,000	-	(135,000)	7,960,000	165,000
Series 2002 (B) (C)	5,820,000	-	(170,000)	5,650,000	155,000
	<u>\$ 15,510,000</u>	<u>\$ -</u>	<u>\$ (1,900,000)</u>	<u>\$ 13,610,000</u>	<u>\$ 320,000</u>

- (A) The Hospital issued \$9,000,000 of Hospital Revenue Capital Loan Notes in 2000. The proceeds of these bonds were used to pay a portion of the cost of constructing and equipping an addition to the Hospital facility. The Series 2000 notes bear interest at rates ranging from 5.9% to 7% payable semi-annually. Annual principal payments are due in amounts ranging from \$205,000 to \$1,545,000 through June 2019.
- (B) The Hospital issued \$6,055,000 of Hospital Revenue Capital Loan Refunding Notes, Series 2002. The proceeds of these bonds were used to achieve a current refunding of its Hospital Revenue Notes, Series 1993 and for paying bond issuance costs incurred. The net proceeds of \$6,001,999 (after paying \$169,811 in issuance costs, a premium of \$116,810) and a transfer from prior debt service funds of \$55,000 were used to pay the outstanding \$5,850,000 of the Series 1993 bonds. The Hospital refunded the 1993 Series bonds to achieve interest cost savings on the bonds. The Hospital reduced its total debt service payments over the next 14 years by approximately \$803,000 and obtained an economic gain (difference between the present value of the debt service payments on the old and new debt) of approximately \$550,000. The Series 2002 notes bear interest at rates ranging from 3.5% to 5.25%. Annual principal payments are due in amounts ranging from \$115,000 to \$750,000 through June 2017.
- (C) The Series 2000 and 2002 bonds grant a security interest in all revenue either accrued or received in connection with operations of the Hospital. The terms of the trust indenture require the Hospital to comply with certain covenants. The covenants provide for restrictions as to financial reporting, restrictions on the sale of the health care facilities and require the Hospital to maintain a sinking fund account and to maintain a specified debt service coverage ratio.

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 8. Long-Term Debt (Continued)

Future annual debt service requirements for long-term debt are as follows:

	Principal	Interest	Total
Year ending June 30:			
2007	\$ 320,000	\$ 796,238	\$ 1,116,238
2008	355,000	780,118	1,135,118
2009	855,000	760,918	1,615,918
2010	900,000	711,753	1,611,753
2011	950,000	663,288	1,613,288
2012 to 2016	5,600,000	2,370,665	7,970,665
2017 to 2021	4,310,000	609,150	4,919,150
	\$ 13,290,000	\$ 6,692,130	\$ 19,982,130

Note 9. Pension Plan

Henry County Health Center (Hospital) contributes to the Iowa Public Employees Retirement System (IPERS), which is a cost-sharing multiple-employer, defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits, which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa 50306-9117.

Plan members are required to contribute 3.70% of their annual covered salary and the Hospital is required to contribute 5.75% of annual covered payroll. Contribution requirements are established by State statute. The Hospital's contribution to IPERS for the years ended June 30, 2006, 2005, and 2004 were \$561,360, \$533,083 and \$504,680, respectively, equal to the required contributions for each year.

Note 10. Professional and General Liability Insurance and Risk Management

The Hospital insures its professional and general liability on a claims-made basis through a commercial insurer. Coverage limits are \$1,000,000 per claim and \$3,000,000 in the aggregate. The premiums for this coverage amount to \$75,256 and \$72,784 for the years ended June 30, 2006 and 2005, respectively.

The Hospital is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. These risks, except for employee health benefits, are covered by commercial insurance purchased from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three years.

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 10. Professional and General Liability Insurance and Risk Management (Continued)

Laws and regulations:

The health care industry is subject to numerous laws and regulations of federal, state and local governments. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not limited to, accreditation, licensure, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in exclusion from government health care program participation, together with the imposition of significant fines and penalties, as well as significant repayment for past reimbursement for patient services received. While the Hospital is subject to similar regulatory reviews, management believes the outcome of any such regulatory review will not have a material adverse effect on the Hospital's financial position.

Note 11. Self-Insured Employee Health Benefits

The Hospital is self-insured for employee health benefits with employees paying a portion of the claims. The Hospital has purchased a stop-loss policy, which pays any amounts over 120% of projected total claims or claims in excess of \$55,000 per claimant. Liabilities are reported as accrued expenses when it is probable that a loss has occurred.

Changes in the provision for reported and unreported claims under the plan during the years ended June 30, 2006 and 2005 are summarized as follows:

	2006	2005
Unpaid claims provision, beginning	\$ 100,000	\$ 167,121
Provision for current year reported and unreported claims	457,462	429,312
Claims paid and related administrative expenses	(457,462)	(496,433)
Unpaid claims provision, ending	<u>\$ 100,000</u>	<u>\$ 100,000</u>

Note 12. Deferred Compensation Plan

The Hospital offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan is available to all Hospital employees and permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

The plan complies with IRC Section 457(g), which requires the plan to hold its assets in trust. Under these requirements, the Hospital does not own the amounts deferred by employees and therefore the liability and corresponding investment is not reflected in the financial statements. The plan assets totaled \$1,985,961 and \$1,782,252 as of June 30, 2006 and 2005, respectively.

Henry County Soldiers' and Sailors'
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Notes to Basic Financial Statements

Note 13. Pending Pronouncements

The GASB has also issued several Statements not yet implemented by the Hospital. The Statements are as follows:

GASB No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, will be effective for the Hospital beginning with its year ending June 30, 2007. This Statement establishes uniform financial reporting standards for other postemployment benefit plans and supercedes GASB No. 26, *Financial Reporting for Postemployment Healthcare Plans Administered by Defined Benefit Pension Plans*.

GASB No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, will be effective for the Hospital beginning with its year ending June 30, 2008. This Statement establishes standards for the measurement, recognition, and display of other postemployment benefits expenses and related liabilities or assets, note disclosures and, if applicable, required supplementary information in the financial reports.

The Hospital's management has not yet determined the effect these Statements will have on the Hospital's financial statements.

Henry County Soldiers' and Sailors'
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Required Supplementary Information, Budgetary Comparison Schedule
 Year Ended June 30, 2006

In accordance with the Code of Iowa, the Board of Trustees annually adopts a budget on the accrual basis following required public notice and hearings for all funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

The following is a comparison between reported amounts and the Hospital's budget:

	Accrual Basis	Final Published Budget	Original Published Budget
Amount to be raised by taxation	\$ 428,370	\$ 425,677	\$ 425,677
Other revenue/receipts	28,379,738	30,005,745	30,005,745
	28,808,108	30,431,422	30,431,422
Expenses/disbursements	(24,831,421)	(28,830,846)	(28,830,846)
	3,976,687	1,600,576	1,600,576
Net assets:			
Beginning of year	22,348,497	21,710,754	15,847,891
End of year	\$ 26,325,184	\$ 23,311,330	\$ 17,448,467