

Paulding County Hospital

**Financial Report
with Additional Information
December 31, 2006**



Mary Taylor, CPA
Auditor of State

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, Paulding County, prepared by Plante & Moran, PLLC, for the audit period January 1, 2006 through December 31, 2006. 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.

Mary Taylor

Mary Taylor, CPA
Auditor of State

April 19, 2007

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Paulding County Hospital

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Independent Auditor's Report

To the Board of Directors
Paulding County Hospital

We have audited the accompanying financial statements of the business-type activities of Paulding County Hospital (a component unit of Paulding County) as of and for the years ended December 31, 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 financial statements referred to above present fairly, in all material respects, the financial position of Paulding County Hospital at December 31, 2006 and 2005 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 26, 2007 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 26, 2007



Paulding County Hospital

Management's Discussion and Analysis

Management's Discussion and Analysis

The discussion and analysis of Paulding County Hospital's (the "Hospital") financial statements provide an overview of the Hospital's financial activities for the year ended December 31, 2006. Management is responsible for the completeness and fairness of the financial statements and the related footnote disclosures along with the discussion and analysis.

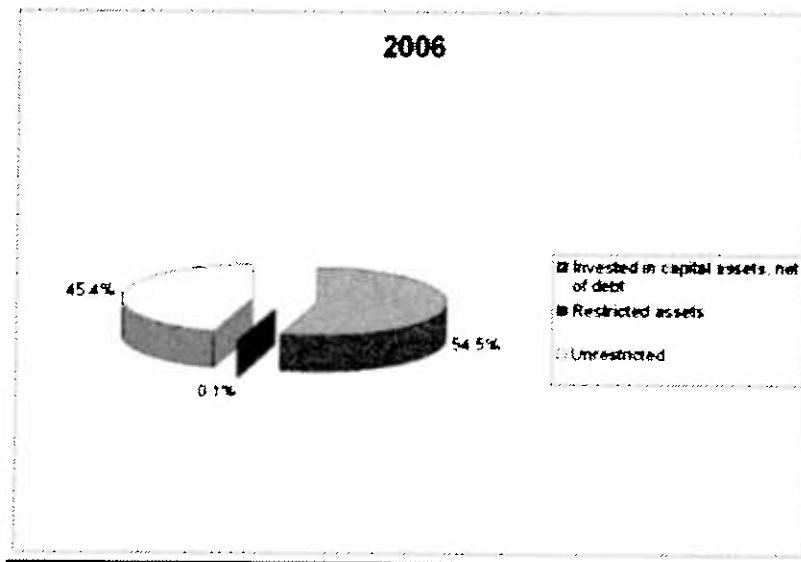
Using this Annual Report

The Hospital's financial statement consists of three statements - the balance sheet, the statement of revenues, expenses, and changes in net assets, and the 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, 2006. The current assets increased by \$781,316 or 20.9 percent from the prior year, compared to \$112,414 or 3.1 percent last year. In total, the Hospital's net assets increased \$340,895 or 2.6 percent from the previous year, compared to \$400,654 or 3.2 percent last year.

The following chart provides a breakdown of net assets by category for the year ended December 31, 2006:



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.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

Condensed Financial Information

The following is a comparative analysis of the major components of the balance sheet of the Hospital as of December 31, 2006, 2005, and 2004:

	Year Ended December 31			Change for 2006	
	2006	2005	2004	Amount	Percent
Assets					
Current assets	\$ 4,523,025	\$ 3,741,709	\$ 3,629,295	\$ 781,316	20.9%
Non-current assets	3,745,730	3,610,964	3,796,850	134,766	3.7%
Capital assets	9,525,023	9,812,630	8,768,757	(287,607)	-2.9%
Total assets	17,793,778	17,165,303	16,194,902	628,475	3.7%
Liabilities					
Current liabilities	2,448,064	2,080,277	2,092,816	367,787	17.7%
Long-term liabilities	1,759,982	1,852,274	1,320,200	(92,292)	-5.0%
Other liabilities	363,197	351,112	300,900	12,085	3.4%
Total liabilities	4,571,243	4,283,663	3,713,916	287,580	6.7%
Net assets:					
Invested in capital assets, net of debt	7,345,951	7,583,504	7,069,157	(237,553)	-3.1%
Restricted assets	13,799	13,782	13,768	17	0.1%
Unrestricted	5,862,785	5,284,354	5,396,061	578,431	10.9%
Total net assets	13,222,535	12,881,640	12,480,986	340,895	2.6%
Total Liabilities and Net Assets	\$ 17,793,778	\$ 17,165,303	\$ 16,194,902	\$ 628,475	3.7%

Current assets increased as a result of increased net patient accounts receivable reflecting \$1,095,114 in additional net patient services revenues.

Capital assets decreased as a result of depreciation on assets purchased over the last six years.

Noncurrent assets increased as a result of better investment rates from prior years.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

	Year Ended December 31			Change for 2006	
	2006	2005	2004	Amount	Percent
Operating Revenue					
Net patient service revenue	\$ 17,324,345	\$ 16,239,557	\$ 14,677,596	\$ 1,084,788	6.7%
Other	218,667	208,341	179,365	10,326	5.0%
Total operating revenue	17,543,012	16,447,898	14,856,961	1,095,114	6.7%
Operating Expenses					
Salaries and wages	8,093,955	7,730,211	7,186,360	363,744	4.7%
Employee benefits and payroll taxes	2,538,017	2,264,271	2,021,653	273,746	12.1%
Medical supplies and drugs	3,754,375	3,029,832	2,721,400	724,543	23.9%
Professional services and consultant fees	474,574	362,780	377,846	91,794	24.0%
Purchased services	1,284,562	1,633,019	1,600,297	(348,457)	-21.3%
Depreciation and amortization	1,227,502	1,069,433	861,848	158,069	14.8%
Total operating expenses	17,372,985	16,109,546	14,769,404	1,263,439	7.8%
Operating Income	170,027	338,352	87,557	(168,325)	-49.7%
Other Income (Expense)					
Investment income	174,744	121,810	59,062	52,934	43.5%
Contributions	29,735	15,995	49,997	13,740	85.9%
Interest earnings on restricted assets	17	14	14	3	21.4%
Interest expense	(71,735)	(76,426)	(29,990)	4,691	-6.1%
Other income	38,107	909	(49,167)	37,198	4092.2%
Total other income	170,868	62,302	29,916	108,566	174.3%
Increase in Net Assets	\$ 340,895	\$ 400,654	\$ 117,473	\$ (59,759)	-14.9%
Net Assets - Beginning of year	\$ 12,881,640	\$ 12,480,986	\$ 12,363,513		
Net Assets - End of year	\$ 13,222,535	\$ 12,881,640	\$ 12,480,986		

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.

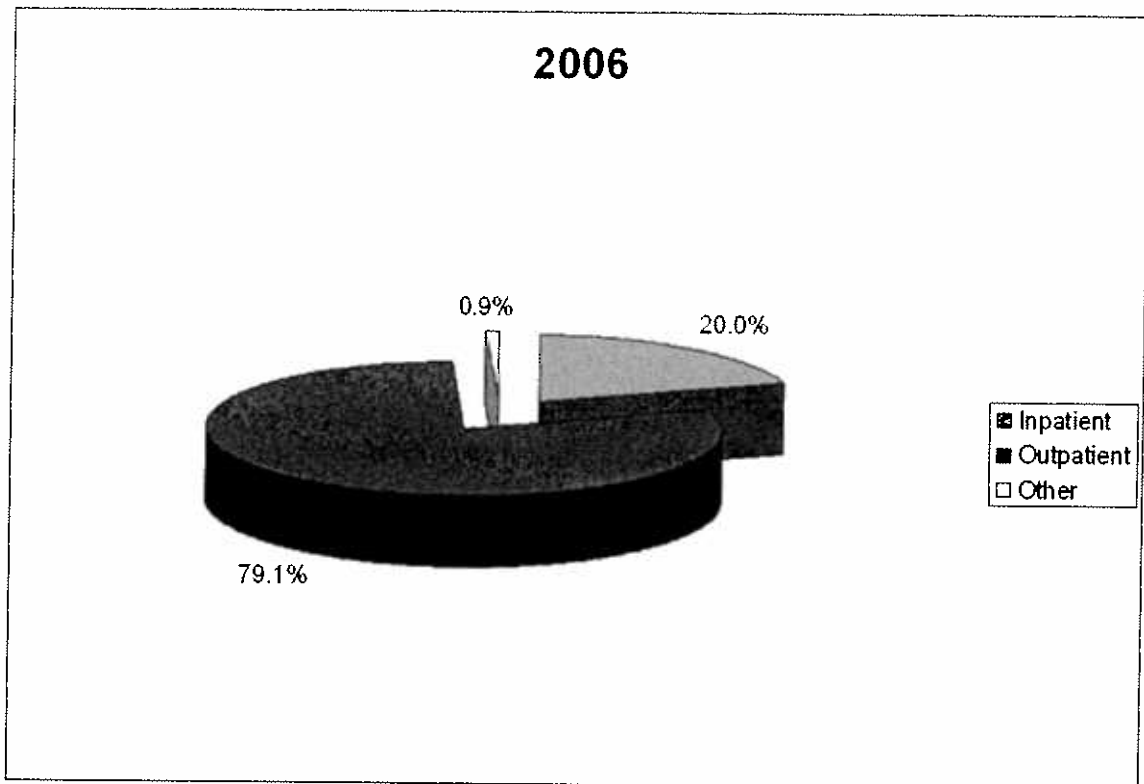
Operating revenue changes were a result of the following factors:

- Net patient service revenue increased 6.7 percent. This was attributable to a 10.0 percent increase in gross outpatient revenues and a 4.0 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 have varied over the past three years from 27.2 percent in 2004, 28.2 percent in 2005, and now 28.1 percent in 2006 as a percentage gross revenue.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

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



Operating Expenses

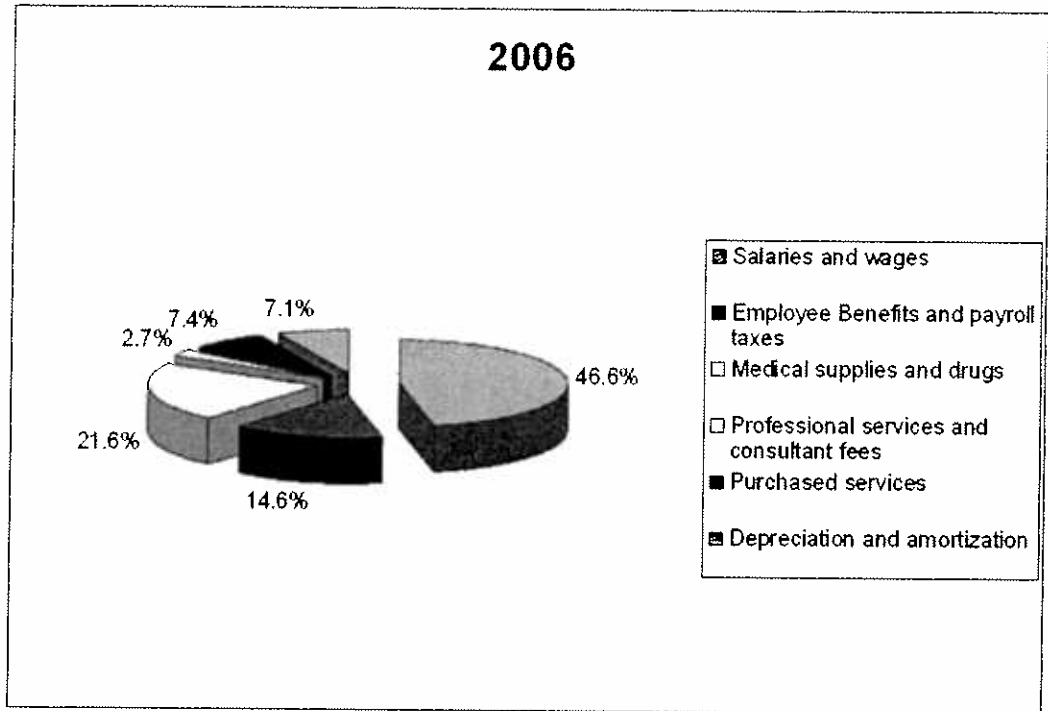
Operating expenses are all the costs necessary to perform and conduct the services and primary purposes of the Hospital. The operating expense changes were the result of the following factors:

- Salary cost increased 4.7 percent as a result of higher surgical patient volumes and wage rate increases.
- Employee benefits increased 12.1 percent reflecting increased self-funded health insurance claims, increased Ohio Public Employers Retirement System premiums, and an increase in Bureau of Workers Compensation premiums.
- Medical supply and drug expenses increased by 23.9 percent as a result of increased costs and patient volumes.
- Professional services increased by 24 percent reflecting the need for additional Obstetric Physician coverage.
- Purchased services decreased by 21.3 percent attributable to a decrease in contract maintenance and consulting.
- Depreciation expense increased 14.8 percent reflecting additions to property, plant and equipment over the past few years.

Paulding County Hospital

Management's Discussion and Analysis (Continued)

The following is a graphic illustration of operating expenses by type:



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

Paulding County Hospital

Management's Discussion and Analysis (Continued)

	2006	2005	2004	2006 Increase (Decrease)
Net cash from:				
Operating and Non-Operating Activities	\$ 917,268	\$ 499,993	\$ 1,739,120	\$ 417,275
Investing Activities	\$ 118,893	\$ 73,605	\$ 47,983	\$ 45,288
Noncapital and Financing activities	\$ 29,735	\$ 15,995	\$ 49,997	\$ 13,740
Capital and related financing activities	\$ (1,062,015)	\$ (1,660,332)	\$ (1,171,013)	\$ 598,317
Net increase (decrease) in cash	\$ 3,881	\$ (1,070,739)	\$ 666,087	\$ 1,074,620
Cash - Beginning of the year	\$ 3,953,427	\$ 5,024,166	\$ 4,358,079	\$ (1,070,739)
Cash - End of year	\$ 3,957,308	\$ 3,953,427	\$ 5,024,166	\$ 3,881

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

Cash provided by operating and nonoperating activities increased \$417,275 from the prior year as a result of increased patient accounts receivable and changes in third-party settlement obligations. Capital and related financing activities increased by \$598,317, reflecting the issuance of debt during 2006 for the purchase of a new CT scanner, IV, and infusion pumps.

Capital Assets and Debt Administration

Capital Assets - At December 31, 2006, the Hospital had \$9.5 million invested in capital assets, net of accumulated depreciation of \$11.8 million. Depreciation and amortization totaled \$1,227,502 for the current year, compared to \$1,069,433 and \$861,848 for 2005 and 2004, respectively. Details of these assets for the past three years are shown below:

	2006	2005	2004	2006 Increase (Decrease)
Land	\$ 30,609	\$ 30,609	\$ 30,609	\$ -
Land improvements	71,202	84,237	63,301	(13,035)
Buildings and improvements	6,620,160	6,926,799	5,119,501	(306,639)
Furniture, fixtures, and equipment	2,609,064	2,770,985	1,400,595	(161,921)
Construction in Process	193,988	-	2,154,751	193,988
Total	\$ 9,525,023	\$ 9,812,630	\$ 8,768,757	\$ (287,607)

Paulding County Hospital

Management's Discussion and Analysis (Continued)

Debt - At year end, the Hospital had \$2,635,415 in debt outstanding as compared to \$2,733,798 and \$2,087,536 for 2005 and 2004, respectively. The table below summarizes these amounts by type of debt instrument:

	2006	2005	2004	2006 Increase (Decrease)
Lease Obligations	\$ 19,455	\$ 71,958	\$ 318,470	\$ (52,503)
Note Payable	2,159,617	2,157,168	1,381,130	2,449
Compensated Absences	456,343	504,672	387,936	(48,329)
Long-Term Liabilities	<u>\$ 2,635,415</u>	<u>\$ 2,733,798</u>	<u>\$ 2,087,536</u>	<u>\$ (98,383)</u>

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.

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 4.0 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 has 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.

Paulding County Hospital

Balance Sheet

	December 31, 2006	December 31, 2005
Assets		
Current Assets		
Cash and cash equivalents (Note 2)	\$ 320,046	\$ 389,500
Accounts receivable (Note 3)	3,047,058	2,436,327
Notes receivable	80,271	47,396
Third-party settlements (Note 8)	218,096	168,703
Prepaid expenses and other	328,347	204,678
Inventory	529,207	495,105
Total current assets	4,523,025	3,741,709
Assets Limited as to Use (Notes 2 and 4)	3,745,730	3,610,964
Capital Assets - Net (Note 5)	9,525,023	9,812,630
Total assets	\$ 17,793,778	\$ 17,165,303
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt (Note 6)	\$ 419,090	\$ 376,852
Accounts payable	725,353	540,945
Accrued liabilities and other (Note 7)	1,303,621	1,162,480
Total current liabilities	2,448,064	2,080,277
Long-term Debt (Note 6)	1,759,982	1,852,274
Other Liabilities (Note 6)	363,197	351,112
Total liabilities	4,571,243	4,283,663
Net Assets		
Invested in capital assets - Net of related debt	7,345,951	7,583,504
Restricted - Expendable for education and other purposes	13,799	13,782
Unrestricted	5,862,785	5,284,354
Total net assets	13,222,535	12,881,640
Total liabilities and net assets	\$ 17,793,778	\$ 17,165,303

Paulding County Hospital

Statement of Revenues, Expenses, and Changes in Net Assets

	Year Ended	
	December 31, 2006	December 31, 2005
Operating Revenues		
Net patient service revenue	\$ 17,324,345	\$ 16,239,557
Other	218,667	208,341
Total operating revenues	17,543,012	16,447,898
Operating Expenses		
Salaries and wages	8,093,955	7,730,211
Employee benefits and payroll taxes	2,538,017	2,264,271
Medical supplies and drugs	3,754,375	3,029,832
Professional services and consultant fees	474,574	382,780
Purchased services	1,284,562	1,633,019
Depreciation and amortization	1,227,502	1,069,433
Total operating expenses	17,372,985	16,109,546
Operating Income	170,027	338,352
Other Income (Expense)		
Investment income	174,744	121,810
Contributions	29,735	15,995
Interest earnings on restricted assets	17	14
Interest expense	(71,735)	(76,426)
Other income	38,107	909
Total other income	170,868	62,302
Increase in Net Assets	340,895	400,654
Net Assets - Beginning of year	12,881,640	12,480,986
Net Assets - End of year	\$ 13,222,535	\$ 12,881,640

Paulding County Hospital

Statement of Cash Flows

	Year Ended	
	December 31, 2006	December 31, 2005
Cash Flows from Operating Activities		
Cash received from patients and third-party payors	\$ 16,664,221	\$ 15,319,397
Cash payments to suppliers for services and goods	(5,442,726)	(5,372,698)
Cash payments to employees for services	(10,483,773)	(9,753,006)
Other operating receipts	179,546	306,300
Net cash provided by operating activities	917,268	499,993
Cash Flows from Noncapital Financing Activities -		
Unrestricted contributions received	29,735	15,995
Cash Flows from Investing Activities		
Investment income	113,330	106,588
Advances to physicians - Net of forgiveness	(32,875)	(34,018)
Other	38,438	1,035
Net cash provided by investing activities	118,893	73,605
Cash Flows from Capital and Related Financing Activities		
Proceeds from issuance of debt	347,758	1,037,705
Principal payments on notes payable	(345,308)	(261,668)
Interest paid on long-term debt - Net of amount capitalized	(71,735)	(76,426)
Purchase of capital assets	(959,965)	(2,131,432)
Proceeds from sale of capital assets	19,739	18,000
Principal payments on capital leases	(52,504)	(246,511)
Net cash used in capital and related financing activities	(1,062,015)	(1,660,332)
Net Increase (Decrease) in Cash and Cash Equivalents	3,881	(1,070,739)
Cash and Cash Equivalents - Beginning of year	3,953,427	5,024,166
Cash and Cash Equivalents - End of year	\$ 3,957,308	\$ 3,953,427
Balance Sheet Classification of Cash and Cash Equivalents		
Cash and cash equivalents	\$ 320,046	\$ 389,500
Restricted cash and cash equivalents	3,637,262	3,563,927
Total cash and cash equivalents	\$ 3,957,308	\$ 3,953,427
Supplemental Cash Flow Information - Cash paid for interest	\$ 71,735	\$ 76,426

Paulding County Hospital

Statement of Cash Flows (Continued)

A reconciliation of operating income to net cash from operating activities is as follows:

	Year Ended	
	December 31, 2006	December 31, 2005
Reconciliation of Operating Income to Net Cash from Operating Activities		
Operating income	\$ 170,027	\$ 338,352
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation	1,227,502	1,069,433
Provision for bad debts	873,125	486,240
Changes in assets and liabilities:		
Increase in patient accounts receivable	(1,483,856)	(1,276,242)
Increase in inventories	(34,102)	(60,489)
(Increase) decrease in prepaid expenses and other receivables	(123,669)	32,636
Increase (decrease) in accounts payable	184,408	(92,853)
Increase in other accrued expenses	153,226	133,074
Increase in third-party settlement receivables	(49,393)	(130,158)
Net cash provided by operating activities	<u>\$ 917,268</u>	<u>\$ 499,993</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 1 - 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, 2006 and 2005

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's 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, 2006 and 2005

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

Classification of Net Assets - Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures. 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, 2006 and 2005

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, the treasurer, or the 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).

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 2 - Deposits and Investments (Continued)

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

Active Funds - Active funds are 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 - Inactive funds are 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 - Interim funds are 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 from 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, 2006 and 2005

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 Hospital 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:

	<u>2006</u>	<u>2005</u>
Deposits	\$ 320,046	\$ 389,500
Certificates of deposit	<u>3,637,262</u>	<u>3,563,927</u>
Total	<u>\$ 3,957,308</u>	<u>\$ 3,953,427</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 2 - Deposits and Investments (Continued)

	<u>2006</u>	<u>2005</u>
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)	\$ 3,890,678	\$ 3,500,026
Amount of deposits covered by federal depository insurance	<u>(713,904)</u>	<u>(713,782)</u>
Amount of deposits collateralized	<u>\$ 3,176,774</u>	<u>\$ 2,786,244</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:

	<u>2006</u>	<u>2005</u>
Gross patient accounts receivable	\$ 4,936,613	\$ 4,053,512
Less:		
Uncollectible accounts	(730,867)	(647,424)
Contractual adjustments	<u>(1,158,688)</u>	<u>(969,761)</u>
Net patient accounts receivable	<u>\$ 3,047,058</u>	<u>\$ 2,436,327</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:

	<u>Percent</u>	
	<u>2006</u>	<u>2005</u>
Medicare	35	40
Medical Mutual of Ohio	12	12
Medicaid	7	5
Other third-party payors	31	28
Patient pay	<u>15</u>	<u>15</u>
Total	<u>100</u>	<u>100</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

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:

	<u>2006</u>	<u>2005</u>
Restricted by contributors for construction, education, and other purposes - Deposits in financial institutions	\$ 13,904	\$ 13,782
Designated by the board for capital improvements:		
Deposits in financial institutions	3,623,358	3,550,145
Accrued interest receivable	<u>108,468</u>	<u>47,037</u>
Total assets limited as to use	<u>\$ 3,745,730</u>	<u>\$ 3,610,964</u>

Note 5 - Capital Assets

Capital asset activity for the year ended December 31, 2006 was as follows:

	<u>2005</u>	<u>Additions</u>	<u>Transfers</u>	<u>Retirements</u>	<u>2006</u>	<u>Depreciable Life - Years</u>
Land	\$ 30,609	\$ -	\$ -	\$ -	\$ 30,609	5-25
Land improvements	196,212	-	-	-	196,212	5-50
Building and improvements	11,988,709	225,099	-	-	12,213,808	5-20
Fixed equipment	1,378,202	-	-	-	1,378,202	5-20
Moveable equipment	4,855,632	540,878	-	(20,070)	5,376,440	5
Moveable equipment - Capital leases	1,976,948	-	-	-	1,976,948	
Construction in progress	-	193,988	-	-	193,988	
Total	<u>20,426,312</u>	<u>959,965</u>	<u>-</u>	<u>(20,070)</u>	<u>21,366,207</u>	
Capital assets being depreciated:						
Land improvements	111,975	13,035	-	-	125,010	
Building and improvements	5,061,910	531,736	-	-	5,593,646	
Fixed equipment	1,376,154	911	-	-	1,377,065	
Moveable equipment	2,965,922	681,820	-	-	3,647,742	
Moveable equipment - Capital leases	<u>1,097,721</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,097,721</u>	
Total	<u>10,613,682</u>	<u>1,227,502</u>	<u>-</u>	<u>-</u>	<u>11,841,184</u>	
Net carrying amount	<u>\$ 9,812,630</u>	<u>\$ (267,537)</u>	<u>\$ -</u>	<u>\$ (20,070)</u>	<u>\$ 9,525,023</u>	

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 5 - Capital Assets (Continued)

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

	2004	Additions	Transfers	Retirements	2005	Depreciable Life - Years
Land	\$ 30,609	\$ -	\$ -	\$ -	\$ 30,609	
Land improvements	163,553	15,251	17,408	-	196,212	5-25
Building and improvements	9,664,279	323,696	2,000,734	-	11,988,709	5-50
Fixed equipment	1,378,938	-	-	(736)	1,378,202	5-20
Moveable equipment	3,931,988	1,792,485	136,609	(1,005,450)	4,855,632	5-20
Moveable equipment - Capital leases	1,976,948	-	-	-	1,976,948	5
Construction in progress	2,154,751	-	(2,154,751)	-	-	
Total	19,301,066	2,131,432	-	(1,006,186)	20,426,312	
Less accumulated depreciation:						
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	\$ 8,768,757	\$ 1,061,999	\$ -	\$ (18,126)	\$ 9,812,630	

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
- Notes payable over 60 months, with monthly payments of \$6,444, including interest at 4.25 percent, collateralized by deposits and revenues of the Hospital

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 6 - Long-term Debt (Continued)

Long-term debt activity for the year ended December 31, 2006 was as follows:

	<u>2005</u>	<u>Additions</u>	<u>Deductions</u>	<u>2006</u>	<u>Current Portion</u>
Leases, bonds, and loans payable:					
Leases payable	\$ 71,959	\$ -	\$ (52,504)	\$ 19,455	\$ 19,455
Notes payable	2,157,167	347,758	(345,308)	2,159,617	399,635
Compensated absences	504,672	219,387	(267,716)	456,343	93,146
Total long-term liabilities	<u>\$ 2,733,798</u>	<u>\$ 567,145</u>	<u>\$ (665,528)</u>	<u>\$ 2,635,415</u>	<u>\$ 512,236</u>

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

	<u>2004</u>	<u>Additions</u>	<u>Deductions</u>	<u>2005</u>	<u>Current Portion</u>
Leases, bonds, and loans payable:					
Lease 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>

The following is a schedule by years of note principal and interest and future minimum lease payments as of December 31, 2006:

	<u>Note Principal</u>	<u>Note Interest</u>	<u>Leases Payable</u>
2007	\$ 399,635	\$ 66,424	\$ 19,659
2008	413,257	52,803	-
2009	427,612	38,448	-
2010	290,798	25,157	-
2011	198,120	17,007	-
2012-2016	430,195	19,639	-
Total payments	<u>\$ 2,159,617</u>	<u>\$ 219,478</u>	19,659
Less amount representing interest			<u>(204)</u>
Net present value			<u>\$ 19,455</u>

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 6 - Long-term Debt (Continued)

The carrying value of equipment under capital lease obligations at December 31 is as follows:

	2006	2005
Cost of equipment under capital lease	\$ 240,760	\$ 240,760
Less accumulated amortization	(222,608)	(174,456)
Net carrying amount	\$ 18,152	\$ 66,304

Note 7 - Accrued Liabilities

The details of accrued liabilities at December 31, 2006 and 2005 are as follows:

	2006	2005
Payroll and related items	\$ 654,558	\$ 509,209
Compensated absences	93,146	153,560
Workers' compensation premiums	239,245	225,503
Health insurance claims	166,601	129,164
Other	150,071	145,044
Total accrued liabilities	\$ 1,303,621	\$ 1,162,480

Note 8 - Cost Report Settlements

Approximately 55 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, 2006 and 2005

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 - 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. 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).

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 9 - Defined Benefit Pension Plan (Continued)

Funding Policy - The Ohio Revised Code provides statutory authority for member and employer contributions. For 2005, member and employer contribution rates were consistent across all three plans (TP, MD, and CO) and are actuarially determined. The 2005 member contribution rate for members of local government units was 8.50 percent of their annual covered salary. The 2005, 2004, and 2003 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, 2006, 2005, and 2004 were approximately \$1,126,007, \$1,031,341, and \$957,456, 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 under the TP and CO plans, 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 Post-Employment 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 2005 and 2004 employer contribution rate for local government employer units was 13.55 percent of covered payroll. Of this amount, 4.0 percent was the portion that was used to fund health care during both 2005 and 2004. The portion of the employer's contribution used to fund postemployment benefits for 2005 and 2004 was \$304,455 and \$282,644, respectively.

The Ohio Revised Code provides the statutory authority requiring public employers to fund postretirement health care through their contributions to OPERS.

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 2004 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, 2004.

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 9 - Defined Benefit Pension Plan (Continued)

The number of active contributing participants in the traditional and combined plans at December 31, 2005 was 376,109. The number of active contributing participants for both plans used in the December 31, 2004 actuarial valuation was 355,287. As of December 31, 2004, the actuarial value of the retirement system's net assets available for OPEB was \$10.8 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$29.5 billion and \$18.7 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. In addition to the HCPP, OPERS has taken additional action to improve the solvency of the Health Care Fund in 2005 by creating a separate investment pool for health care assets. As an additional component of the HCPP, member and employer contribution rates increased as of January 1, 2006, which will allow additional funds to be allocated to the health care plan.

The 2006 information has not been published by OPERS as of the date of this report; therefore, this footnote represents the information available in 2005.

Note 10 - 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.

Paulding County Hospital

Notes to Financial Statements December 31, 2006 and 2005

Note 10 - Risk Management (Continued)

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 12 for discussion of self-insured health programs.

Note 11 - 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.

Note 12 - 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 \$1,281,032. The plan policy year ends on December 31. Claims, charged to operations when incurred, were approximately \$1,035,000 and \$905,000 for the years ended December 31, 2006 and 2005, respectively.

Reconciliation of accrued health insurance at December 31, 2006 and 2005 consists of the following:

Balance at January 1, 2005	\$ 124,449
Health insurance expense	905,000
Payments made	<u>(900,285)</u>
Balance at December 31, 2005	129,164
Health insurance expense	1,035,000
Payments made	<u>(997,563)</u>
Balance at December 31, 2006	<u>\$ 166,601</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, 2006 and have issued our report thereon dated January 26, 2007. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Paulding County Hospital's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Paulding County Hospital's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

To the Board of Directors
Paulding County Hospital

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*.

We noted certain matters that we reported to management of Paulding County Hospital in a separate letter dated January 26, 2007.

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, 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 26, 2007



Mary Taylor, CPA
Auditor of State

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 10, 2007**