

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Years Ended June 30, 2009 and 2008

BURK · PEARLMAN
NEBBEN & HUGGINS, PLLC
CERTIFIED PUBLIC ACCOUNTANTS

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

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INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of
Rhea Medical Center (a component unit of Rhea County, Tennessee)

We have audited the accompanying financial statements of Rhea Medical Center (a component unit of Rhea County, Tennessee) as of and for the years ended June 30, 2009 and 2008, which collectively comprise the Medical Center's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Rhea Medical Center's (a component unit of Rhea County, Tennessee) 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 misstatements. 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 Rhea Medical Center (a component unit of Rhea County, Tennessee) as of June 30, 2009 and 2008, and the results of its operations 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 November 19, 2009, on our consideration of Rhea Medical Center's (a component unit of Rhea County, Tennessee) internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages 3 through 8 is not a required part of the accompanying financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The schedules listed as supplementary in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements of Rhea Medical Center (a component unit of Rhea County, Tennessee). Such information has been subjected to the auditing procedures applied in the audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Burk, Pearlman, Nelson & Higgins, PLLC
Chattanooga, Tennessee
November 19, 2009

RHEA MEDICAL CENTER
A COMPONENT UNIT OF RHEA COUNTY, TENNESSEE
MANAGEMENT'S DISCUSSION AND ANALYSIS

Our discussion and analysis of Rhea Medical Center's (the Medical Center's) financial performance provides an overview of the Medical Center's financial activities for the fiscal years ended June 30, 2009 and 2008. Please read it in conjunction with the Medical Center's financial statements, which begin on page 9.

Financial Highlights

- The Medical Center's net assets increased in each of the past two years with a \$1,194,937 or 8% increase in 2009 and a \$1,332,842 or 10% increase in 2008. The Medical Center reported operating income in both 2009 and 2008. Operating revenues increased 3% over 2008, while operating expenses increased at a rate of 4% in 2009.

Using This Annual Report

The Medical Center's financial statements consist of three statements – a Balance Sheet; a Statement of Revenues, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Medical Center, including resources held by the Medical Center.

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

One of the most important questions asked about the Medical Center's finances is, "Is the Medical Center as a whole better 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 about the Medical Center's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Medical Center's net assets and changes in them. Net assets, which is the difference between assets and liabilities, is one way to measure the Medical Center's financial health, or financial position. Over time, increases or decreases in the Medical Center's net assets indicate whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the Medical Center's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the Medical Center.

RHEA MEDICAL CENTER
A COMPONENT UNIT OF RHEA COUNTY, TENNESSEE
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

The Statement of Cash Flows

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

The Medical Center's Net Assets

The Medical Center's net assets are the difference between its assets and liabilities reported in the Balance Sheet on page 9 and 10. The Medical Center's net assets increased in each of the past two years with a \$1,194,937 or 8% increase in 2009 and a \$1,332,842 or 10% increase in 2008. See Exhibit One for an illustration.

Exhibit One: Assets, Liabilities, and Net Assets

	<u>2009</u>	<u>2008</u>
Assets:		
Current assets	\$13,131,430	\$10,119,566
Capital assets, net,	30,473,409	31,872,274
Non-current cash and investments	255,812	253,558
Other assets	399,390	399,376
Total assets	<u>\$44,260,041</u>	<u>\$42,644,774</u>
Liabilities		
Current liabilities	\$3,791,971	\$ 2,433,772
Long-term debt outstanding	23,924,882	24,857,518
Other liabilities	19,219	24,452
Total liabilities	<u>\$27,736,072</u>	<u>\$27,315,742</u>
Net assets:		
Invested in capital assets, net of related debt	\$5,616,264	\$ 6,784,618
Unrestricted	10,671,112	8,315,308
Unrestricted-Board Designated	236,593	229,106
Total Net Assets	<u>\$16,523,969</u>	<u>\$15,329,032</u>

RHEA MEDICAL CENTER
A COMPONENT UNIT OF RHEA COUNTY, TENNESSEE
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Assets increased by \$1,615,267 or 4% during 2009. A significant component of the change in the Medical Center's assets is the increase in current assets. Current assets increased \$3,011,864 due to a \$2,703,259 increase in cash (See Statements of Cash Flows for a detail of the changes in cash). The increase in current assets was partially offset by a \$1,398,865 decrease in capital assets. Higher depreciation expense related to the new facility and the associated new equipment increased accumulated depreciation by \$1,884,082 (See Note A to the financial statements for an explanation of the Medical Center's capitalization policies and Note F for a detail of capital assets). Liabilities increased by \$420,330. Current liabilities increased \$1,358,199 due to a \$702,125 increase in current maturities of long-term debt and a \$425,936 increase in estimated third-party settlements (See Note C to the financial statements for a summary of the basis of reimbursement with major third party payors). The long-term debt portion of debt decreased by \$932,636 due to the maturing of debt (See Note H to the financial statements for a detail of long-term debt).

Operating Results and Changes in the Medical Center's Net Assets

The Medical Center's net assets increased by \$1,194,937 or 8% in 2009 and \$1,332,842 or 10% increase in 2008, as shown in Exhibit 2. The increase in 2009 is primarily due to the increases discussed above. Operating income decreased in 2009 by \$244,223 or 14% and decreased in 2008 by \$87,953 or 5%, respectively.

RHEA MEDICAL CENTER
A COMPONENT UNIT OF RHEA COUNTY, TENNESSEE
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Exhibit 2: Operating Results and Changes in Net Assets

	<u>2009</u>	<u>2008</u>
OPERATING REVENUES:		
Net patient service revenue	\$22,500,915	\$22,030,134
Other revenue	<u>381,360</u>	<u>211,545</u>
TOTAL OPERATING REVENUES	<u>22,882,275</u>	<u>22,241,679</u>
OPERATING EXPENSES:		
Salaries and benefits	11,293,526	10,904,964
Medical supplies and drugs	1,826,692	1,571,789
Other supplies	667,763	736,542
Insurance	468,947	537,037
Depreciation	1,890,330	1,638,616
Other expenses	<u>5,202,111</u>	<u>5,075,602</u>
TOTAL OPERATING EXPENSES	<u>21,349,369</u>	<u>20,464,550</u>
OPERATING INCOME	<u>1,532,906</u>	<u>1,777,129</u>
NONOPERATING REVENUES (EXPENSES)		
Interest income	28,697	106,184
Interest expense	(404,966)	(640,725)
Noncapital contribution	560	35,954
Noncapital grants	<u>37,740</u>	<u>54,300</u>
TOTAL NONOPERATING REVENUES (EXPENSES)	<u>(337,969)</u>	<u>(444,287)</u>
EXCESS OF REVENUES OVER EXPENSES AND INCREASE IN NET ASSETS	1,194,937	1,332,842
Net assets at beginning of year	<u>15,329,032</u>	<u>13,996,190</u>
Net assets at end of year	<u>\$16,523,969</u>	<u>\$15,329,032</u>

RHEA MEDICAL CENTER
A COMPONENT UNIT OF RHEA COUNTY, TENNESSEE
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Operating Income

The first component of the overall change in the Medical Center's net assets is its operating income – generally the difference between net patient service revenues and the expenses incurred to perform those services. In the past two years, the Medical Center has reported operating income.

The primary components of the operating income in 2009 are:

- Net patient service revenue increased by \$470,781 or 2% in 2009. Patient revenue before deductions increased \$2,836,807 or 7%. The increase in patient revenue was due to a 221 day or 5% increase in patient days and a 293 case or 110% increase in surgical cases. The increase in volumes is due to the recruitment of a general surgeon that started practice in July 2008. The increases in patient revenue were offset by contractual adjustments and bad debts (See Note C to the financial statements for a summary of the basis of reimbursement with major third party payors). Contractual adjustments increased \$2,076,963 or 14% due to a payor mix shift from payors with lower deduction amounts such as Blue Cross and other commercial payors to payors with higher deductions such as Medicare and TennCare. Bad debt expense increased by \$330,073 or 10%. The increase in bad debts is due to a \$371,922 or 12% increase in self pay revenue. The local economy and unemployment rate has impacted the number of patients without insurance.
- Other revenue increased by \$169,815 or 80% in 2009. The increase was due to a \$167,517 insurance premium rebate.
- Salaries and related benefits increased by \$388,562 or 4%. The majority of the increase is related to annual staff raises. Salaries and benefits for surgical services increased \$119,779 due to the additional surgical cases discussed above.
- Medical supplies and drugs increased by \$254,903 or 16% due to the increased cost of surgical supplies as a result of the increase in surgical cases discussed above.
- Depreciation expense increased by \$251,714 in 2009 due to a full year of depreciation being recorded on the new facility and new equipment (See Note F to the financial statements for a summary of changes in capital assets).

Nonoperating Revenues

Nonoperating revenues for 2009 includes \$404,966 in interest expense. Due to the financing of the new facility as discussed in Note H of the financial statements, interest expense decreased \$235,759 or 37% due to lower interest rates in 2009. Interest income decreased by \$77,487 or 73% in 2009 due to lower interest rates.

RHEA MEDICAL CENTER
A COMPONENT UNIT OF RHEA COUNTY, TENNESSEE
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

The Medical Center's Cash Flows

Changes in the Medical Center's cash flows are consistent with changes in prepaid assets; property, plant, and equipment, net; repayments of debt; operating income and nonoperating income, as discussed earlier.

Capital Asset and Debt Administration

Capital Assets. As of June 30, 2009, the Medical Center had \$30,473,409 invested in capital assets, net of accumulated depreciation, as detailed in Note F to the financial statements. During fiscal year 2009, the Medical Center purchased equipment and other depreciable assets of \$485,217 (reduced by \$1,884,082 in related depreciation expense on the balance sheet).

Debt. In 2007 the Medical Center entered a capital lease to purchase a MRI machine. The MRI lease has an outstanding principle balance of \$531,606 at June 30, 2009. In 2007, the Medical Center entered a capital lease to purchase a CT system. The CT system lease has an outstanding principle balance of \$225,539 at June 30, 2009. In 2006, the Medical Center obtained funding of up to \$24,100,000 to construct a replacement facility as detailed in Note H to the financial statements.

Other Economic Factors

The current economic situation that the country is facing could have a negative impact on the local economy. If companies in Rhea County lay off employees then the Medical Center could see an increase in uninsured patients which would lead to higher bad debt expense and charity care.

Due to both the national and local shortages of healthcare professionals, the Medical Center faces stiff competition in retaining and the recruitment of new employees. Management focuses on this issue in a number of ways including by meeting with local healthcare education programs to encourage student outplacement, offering scholarships to students in healthcare careers, monitoring compensation trends and adjusting compensation as necessary.

Contacting the Medical Center's Financial Management

This financial report is designed to provide our patients, suppliers, creditors and other stakeholders with a general overview of the Medical Center's finances and to show the Medical Center's accountability for the money it receives. Any questions about this report or requests for additional financial information should be directed to Rhea Medical Center, Department of Finance, 9400 Rhea County Highway, Dayton, Tennessee 37321.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

BALANCE SHEETS

June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
ASSETS		
CURRENT ASSETS		
Cash	\$7,532,959	\$4,829,700
Patient accounts receivable, net of estimated uncollectibles of \$1,470,000 in 2009 and \$1,140,000 in 2008	3,794,618	3,641,095
Estimated third-party payor settlements	897,571	997,063
Inventories	457,505	419,556
Prepaid expenses	86,212	79,599
Other assets	<u>362,565</u>	<u>152,553</u>
TOTAL CURRENT ASSETS	<u>13,131,430</u>	<u>10,119,566</u>
NONCURRENT CASH AND INVESTMENTS		
Internally designated for capital acquisitions	236,593	229,106
Patient trust funds	18,297	22,956
Activity funds	<u>922</u>	<u>1,496</u>
TOTAL NONCURRENT CASH AND INVESTMENTS	<u>255,812</u>	<u>253,558</u>
CAPITAL ASSETS		
Land	2,362,514	2,362,514
Construction in progress	--	30,306
Depreciable capital assets, net of accumulated depreciation	<u>28,110,895</u>	<u>29,479,454</u>
TOTAL CAPITAL ASSETS, net	<u>30,473,409</u>	<u>31,872,274</u>
OTHER ASSETS		
Bond issuance costs	149,956	156,204
Other assets	<u>249,434</u>	<u>243,172</u>
TOTAL OTHER ASSETS	<u>399,390</u>	<u>399,376</u>
TOTAL ASSETS	<u>\$44,260,041</u>	<u>\$42,644,774</u>

See accompanying notes to financial statements.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

BALANCE SHEETS

June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current maturities of long-term debt	\$932,263	\$230,138
Accounts payable	913,512	827,661
Accrued payroll	681,052	634,803
Other accrued expenses	328,149	230,111
Estimated third-party payor settlements	<u>936,995</u>	<u>511,059</u>
TOTAL CURRENT LIABILITIES	<u>3,791,971</u>	<u>2,433,772</u>
LONG-TERM DEBT, net of current maturities	<u>23,924,882</u>	<u>24,857,518</u>
OTHER LIABILITIES		
Patient trust funds	18,297	22,956
Activity funds	<u>922</u>	<u>1,496</u>
TOTAL OTHER LIABILITIES	<u>19,219</u>	<u>24,452</u>
TOTAL LIABILITIES	<u>27,736,072</u>	<u>27,315,742</u>
NET ASSETS		
Invested in capital assets net of related debt	5,616,264	6,784,618
Unrestricted	10,671,112	8,315,308
Unrestricted-board designated	<u>236,593</u>	<u>229,106</u>
TOTAL NET ASSETS	<u>16,523,969</u>	<u>15,329,032</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$44,260,041</u>	<u>\$42,644,774</u>

See accompanying notes to financial statements.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
OPERATING REVENUE		
Net patient service revenue	\$22,500,915	\$22,030,134
Other revenue	<u>381,360</u>	<u>211,545</u>
 TOTAL OPERATING REVENUE	 <u>22,882,275</u>	 <u>22,241,679</u>
OPERATING EXPENSES		
Salaries and benefits	11,293,526	10,904,964
Medical supplies and drugs	1,826,692	1,571,789
Other supplies	667,763	736,542
Insurance	468,947	537,037
Depreciation and amortization	1,890,330	1,638,616
Other expenses	<u>5,202,111</u>	<u>5,075,602</u>
 TOTAL OPERATING EXPENSES	 <u>21,349,369</u>	 <u>20,464,550</u>
 OPERATING INCOME	 <u>1,532,906</u>	 <u>1,777,129</u>
NONOPERATING REVENUES (EXPENSES)		
Interest income	28,697	106,184
Interest expense	(404,966)	(640,725)
Noncapital contribution	560	35,954
Noncapital grants	<u>37,740</u>	<u>54,300</u>
 TOTAL NONOPERATING REVENUES (EXPENSES), net	 <u>(337,969)</u>	 <u>(444,287)</u>
EXCESS OF REVENUES OVER EXPENSES AND INCREASE IN NET ASSETS		
Net assets at beginning of year	<u>15,329,032</u>	<u>13,996,190</u>
 Net assets at end of year	 <u>\$16,523,969</u>	 <u>\$15,329,032</u>

See accompanying notes to financial statements.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

STATEMENTS OF CASH FLOWS

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from patients and third-party payors	\$19,416,648	\$17,551,200
Cash payments to suppliers for goods and services	(7,398,710)	(5,916,344)
Cash payments to employees for services	(8,634,855)	(8,456,026)
Other revenue	<u>381,360</u>	<u>211,545</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>3,764,443</u>	<u>3,390,375</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Noncapital grants and contributions	<u>38,300</u>	<u>90,254</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Interest paid on debt	(404,966)	(640,725)
Purchase of property and equipment	(485,217)	(5,789,753)
Payments on long-term debt	(230,511)	(334,293)
Proceeds from loan agreement	=	<u>5,222,614</u>
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(1,120,694)</u>	<u>(1,542,157)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received	28,697	106,184
Purchases of investments	<u>(7,487)</u>	<u>(10,546)</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>21,210</u>	<u>95,638</u>
Net increase in cash	2,703,259	2,034,110
Cash at beginning of year	<u>4,829,700</u>	<u>2,795,590</u>
Cash at end of year	<u>\$7,532,959</u>	<u>\$4,829,700</u>

See accompanying notes to financial statements.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

STATEMENTS OF CASH FLOWS
(Continued)

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income	\$1,532,906	\$1,777,129
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	1,890,330	1,638,616
Provision for bad debts	3,686,316	3,356,243
Change in assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	(3,839,839)	(3,651,028)
Estimated third-party payor settlements	99,492	(826,250)
Inventories	(37,949)	(89,789)
Prepaid expenses	(6,613)	1,238,026
Other assets	(216,274)	(26,249)
Increase (decrease) in:		
Accounts payable	85,851	(46,852)
Accrued payroll	46,249	75,008
Other accrued expenses	98,038	(52,822)
Estimated third-party payor settlements	<u>425,936</u>	<u>(1,657)</u>
	<u>\$3,764,443</u>	<u>\$3,390,375</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Capital lease	\$--	<u>\$808,468</u>

See accompanying notes to financial statements.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES

Reporting entity. Rhea Medical Center (the Medical Center) is a public corporation. It was created on February 7, 1957, by an act of the State of Tennessee General Assembly to operate, control, and manage the general short-term hospital, intermediate care nursing home, and various health clinics. The Rhea County, Tennessee Board of County Commissioners appoints the Board of Trustee members of the Medical Center, and the Medical Center may not issue debt without the County's approval. For these reasons, the Medical Center is considered to be a component unit of Rhea County and is included as a discretely presented component unit in the basic financial statements of Rhea County, Tennessee (the County).

Enterprise fund accounting. The Medical Center uses the enterprise fund method of accounting whereby revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

Accounting standards. Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Medical Center 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.

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

Net patient service revenue. Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. The 2009 net patient service revenue decreased \$61,853 due to prior year retroactive adjustments in excess of amounts previously estimated.

Revenue from the Medicare and Medicaid programs accounted for approximately 34 and 26 percent, respectively, for the year ended June 30, 2009, and 30 and 26 percent, respectively, for the year ended June 30, 2008, of the Medical Center's net patient service revenue. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Charity care. The Medical Center 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 Medical Center does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

Operating revenues and expenses. The Medical Center'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 – the Medical Center's principal activity. Nonexchange revenues, including interest, grants, and contributions are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Income taxes. The Medical Center, as a component unit of Rhea County, Tennessee, is exempt from federal and state income taxes.

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

Accounts receivable. Accounts receivable are stated at the amount the Medical Center expects to collect. The Medical Center maintains allowances for doubtful accounts for estimated losses resulting from the inability of its patients to make required payments. Management considers the following factors when determining the collectibility of specific patient accounts: payor credit-worthiness, past transaction history with the payor, current economic industry trends, and changes in payor payment terms. If the financial condition of the Medical Center's payors or patients were to deteriorate, adversely affecting their ability to make payments, additional allowances would be required. Based on management's assessment, the Medical Center provides for estimated uncollectible amounts through a charge to earnings and a credit to an allowance. Balances that remain outstanding after the Medical Center has used reasonable collection efforts are written off through a charge to the allowance and a credit to accounts receivable.

Noncurrent cash and investments. Internally designated for capital acquisition is cash and investments designated by the Board of Trustees for the creation of a health education library. Patients' personal assets and funds held by the Medical Center in an activity fund for the benefit of the patients are held in an agency capacity and are not available for Medical Center use. An offsetting asset and liability are recorded on the balance sheet.

Capital assets. Assets with a useful life of greater than one year and a cost of greater than \$5,000 are recorded as capital assets and are stated at cost. Depreciation is calculated over the estimated useful lives using the straight-line method. Expenditures for maintenance, repairs, renewals and betterments that do not significantly extend the useful lives of the assets are expensed as incurred. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the books, and any resulting gain or loss is reflected in income for the period.

A summary of estimated useful lives follows.

	<u>Estimated Useful Lives</u>
Land improvements	10 - 15 years
Buildings and improvements	10 – 50 years
Major moveable equipment	5 – 25 years
Fixed equipment	10 – 25 years

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

Costs of borrowing. Except for capital assets acquired through gifts, contributions, or capital grants, interest cost on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. No interest was capitalized during 2009. Interest capitalized for 2008 was \$124,557.

Deposits. The Medical Center considers currency on hand and demand deposits with financial institutions to be cash. The Medical Center considers all highly liquid investments with original maturities of three months or less to be cash equivalents. State statutes authorize the Medical Center to invest in obligations of the U.S. Treasury, bank certificates of deposit, state approved repurchase agreements, and pooled investment funds, state or local bonds, rated A or higher by a nationally recognized rating service. There were no cash equivalents at June 30, 2009 and 2008.

Bond issuance costs. The costs incurred in connection with the issuance of the bonds will be amortized using the straight-line method over the term of the bonds.

Risk management. The Medical Center is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Net assets. Net assets of the Medical Center are classified in four components. *Net assets invested in capital assets net of related debt* consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted expendable net assets* are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Medical Center. *Restricted nonexpendable net assets* equal the principal portion of permanent endowments. *Unrestricted net assets* are remaining net assets that do not meet the definition of *invested in capital assets net of related debt or restricted*. There were no restricted assets at June 30, 2009 or 2008.

NOTE B - DEPOSITS AND INVESTMENTS

Custodial credit risk - deposits. Custodial risk is the risk that in the event of a bank failure, the Medical Center's deposits may not be returned to it. The Medical Center's bank balance of deposits was \$7,581,669 and \$5,148,931 at June 30, 2009 and 2008, respectively. The bank balances held in cash accounts and a repurchase agreement are either insured by the Federal Deposit Insurance Corporation or collateralized by the Tennessee Bank Collateral Pool and are not subject to custodial risk.

Interest rate risk. For an investment, this is the risk that a change in interest rates will affect the fair market value of investments held. The investment is a certificate of deposit with a local financial institution that matures on August 18, 2009, with a 2.14% fixed rate of interest. The short maturity (182 days) of the CD protects the Medical Center from interest rate risk.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

Custodial risk - investments. The Medical Center's investment is subject to custodial risk as follows:

<u>Investments</u>	<u>2009</u>	<u>2008</u>
Insured by the FDIC	\$236,593	\$100,000
Collateralized	--	<u>129,106</u>
	<u>\$236,593</u>	<u>\$229,106</u>

The Medical Center currently has no formal policy addressing interest rate or custodial risk, except to comply with State statutes.

The carrying amounts of deposits and investments shown above are included in the Medical Center's balance sheet as follows:

	<u>2009</u>	<u>2008</u>
Carrying amount		
Deposits	\$7,550,178	\$4,852,152
Investments	236,593	229,106
Cash on hand	<u>2,000</u>	<u>2,000</u>
	<u>\$7,788,771</u>	<u>\$5,083,258</u>
Included in the following balance sheet captions		
Cash	7,532,959	\$ 4,829,700
Internally designated for capital acquisition	236,593	229,106
Patient trust funds	18,297	22,956
Activity funds	<u>922</u>	<u>1,496</u>
	<u>\$7,788,771</u>	<u>\$5,083,258</u>

NOTE C - NET PATIENT SERVICE REVENUE

The Medical Center has agreements with third-party payors that provide for payments to the Medical Center at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Medical Center's established rates for services and amounts reimbursed by third-party payors. The Hospital obtained critical access status effective February 1, 2005. A summary of the basis of reimbursement with major third-party payors follows.

Medicare. Inpatient acute care services, outpatient services, inpatient nonacute services, and medical education costs related to Medicare beneficiaries are paid based upon a cost reimbursement methodology. The Medical Center is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Medical Center and review by the Medicare fiscal intermediary.

TennCare. Inpatient acute care services and outpatient service costs related to TennCare program beneficiaries are paid based upon a cost reimbursement methodology. The Medical Center is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Medical Center and review by the TennCare fiscal intermediary.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

Medicaid – Intermediate Care. The Medicaid program reimburses the Medical Center for services rendered to Medicaid nursing home beneficiaries based on a prospective per diem rate established by the Medicaid program. The per diem rate established by Medicaid is based on the prior years' cost, subject to a maximum per diem rate set by the State of Tennessee.

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

NOTE D - INVENTORIES

Inventories on June 30, 2009 and 2008, consist of the following.

	<u>2009</u>	<u>2008</u>
Pharmacy	\$144,415	\$112,885
General supplies	92,722	91,087
Dietary	11,998	10,653
Laboratory	37,989	29,934
X-ray	19,686	18,593
Surgery	<u>150,695</u>	<u>156,404</u>
	<u>\$457,505</u>	<u>\$419,556</u>

NOTE E - INTERNALLY DESIGNATED FOR CAPITAL ACQUISITIONS CASH AND INVESTMENTS

During 2004, the Medical Center received an unrestricted contribution from an anonymous private donor. The Board of Trustees has designated the money, invested in a CD at a local bank, for the creation of a health education library.

NOTE F - CAPITAL ASSETS

A summary of changes in capital assets follows.

	<u>2008</u>	<u>Additions</u>	<u>Retirements</u>	<u>2009</u>
Land	\$2,362,514	\$--	\$--	\$2,362,514
Land improvements	65,951	--	--	65,951
Buildings and improvements	27,475,984	--	--	27,475,984
Major moveable equipment	10,784,798	515,523	--	11,300,321
Fixed equipment	941,525	--	--	941,525
Construction in progress	<u>30,306</u>	<u>(30,306)</u>	--	--
Totals at historical cost	<u>41,661,078</u>	<u>485,217</u>	--	<u>42,146,295</u>
Less accumulated depreciation for:				
Land improvements	57,186	1,537	--	58,723
Buildings and improvements	3,979,614	704,304	--	4,683,918
Major moveable equipment	4,979,155	1,165,191	--	6,144,346
Fixed equipment	<u>772,849</u>	<u>13,050</u>	--	<u>785,899</u>
Total accumulated depreciation	<u>9,788,804</u>	<u>1,884,082</u>	--	<u>11,672,886</u>
Property and equipment, net	<u>\$31,872,274</u>	<u>\$(1,398,865)</u>	\$--	<u>\$30,473,409</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

	<u>2007</u>	<u>Additions</u>	<u>Retirements</u>	<u>2008</u>
Land	\$2,362,514	\$--	\$--	\$2,362,514
Land improvements	79,066	--	13,115	65,951
Buildings and improvements	5,075,155	22,461,843	61,014	27,475,984
Major moveable equipment	7,600,151	4,561,734	1,377,087	10,784,798
Fixed equipment	1,272,258	--	330,733	941,525
Construction in progress	<u>20,707,872</u>	<u>1,784,276</u>	<u>22,461,842</u>	<u>30,306</u>
Totals at historical cost	<u>37,097,016</u>	<u>28,807,853</u>	<u>24,243,791</u>	<u>41,661,078</u>
Less accumulated depreciation for:				
Land improvements	68,764	1,537	13,115	57,186
Buildings and improvements	3,429,768	610,860	61,014	3,979,614
Major moveable equipment	5,351,016	1,005,226	1,377,087	4,979,155
Fixed equipment	<u>1,088,837</u>	<u>14,745</u>	<u>330,733</u>	<u>772,849</u>
Total accumulated depreciation	<u>9,938,385</u>	<u>1,632,368</u>	<u>1,781,949</u>	<u>9,788,804</u>
Property and equipment, net	<u>\$27,158,631</u>	<u>\$27,175,485</u>	<u>\$22,461,842</u>	<u>\$31,872,274</u>

Amortization of assets acquired under capital lease obligations is included in depreciation expense.

Buildings and improvements includes capitalized interest of \$464,765 at June 30, 2009 and 2008. A portion of the original Medical Center building is being used for the Nursing Home. Building improvements and equipment with a carrying value of \$1,168,626 are idle at June 30, 2009.

NOTE G - OTHER ASSETS

The Medical Center pays various fees and expenses to and on behalf of physicians who are recruited to practice at the Medical Center. These expenses are recorded as assets and are amortized over the terms of the physicians' contracts. At June 30, 2009 and 2008, respectively, the assets totaled \$586,366 and \$370,596, net of accumulated amortization.

Other assets also include various lease deposits and prepayments totaling \$25,633 and \$25,129 at June 30, 2009 and 2008, respectively.

NOTE H - LONG-TERM DEBT

	<u>2009</u>	<u>2008</u>
Loan agreement	\$24,100,000	\$24,100,000
Capital lease obligation #1 at an imputed interest rate of 9.6%	225,539	302,394
Capital lease obligation #2 at an imputed interest rate of 4.1%	<u>531,606</u>	<u>685,262</u>
	24,857,145	25,087,656
Less current maturities of long-term debt	<u>932,263</u>	<u>230,138</u>
Long-term debt, net of current maturities	<u>\$23,924,882</u>	<u>\$24,857,518</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

On December 11, 1997, the County authorized the Medical Center to borrow from them up to \$1,100,000 for continuing expansion and renovation projects. At June 30, 2001, no further draws were permitted. The outstanding principal matured on December 11, 2000, and was renewed for an additional three years. When it matured on December 11, 2003, it was renewed for an additional three years, with no further extensions available. The debt is due in annual installments of at least one-ninth of the principal outstanding. The notes carry a variable interest rate from 3.90% to 4.55%. The notes are unsecured. The notes were paid off in July 2007.

The Public Building Authority of the County of Montgomery, Tennessee issued its "Adjustable Rate Pooled Financing Revenue Bonds, Series 2004" on July 1, 2004, and loaned \$24,100,000 of the proceeds to the Medical Center under a loan agreement with terms substantially identical to terms of the Bonds. The bonds mature on various dates from May 25, 2010 through May 25, 2033.

Principal payments will be made annually as they become due. Interest payments are due monthly. Interest is calculated daily as set forth in the loan agreement (.39% at June 30, 2009).

The loan agreement is secured by the Medical Center property and equipment.

Capital lease obligation #1 requires monthly installments of \$7,657, including interest, until February 2012. The obligation is secured by a CT system with a cost of \$398,580 and a carrying value of \$205,933 at June 30, 2009.

Capital lease obligation #2 requires monthly installments of \$14,970, including interest, until August 2012. The obligation is secured by an MRI system with a cost of \$808,468 and a carrying value of \$512,030 at June 30, 2009.

Scheduled payments on long-term debt are as follows.

<u>Year Ending June 30</u>	<u>Long Term Debt</u>		<u>Capital Lease Obligations</u>	
	<u>Principal</u>	<u>Interest*</u>	<u>Principal</u>	<u>Interest</u>
2010	\$691,000	\$91,295	\$241,263	\$30,257
2011	713,000	88,514	252,930	18,591
2012	735,000	85,648	234,327	6,566
2013	758,000	82,692	28,625	157
2014	781,000	79,646	--	--
2015-2019	4,283,000	349,140	--	--
2020-2024	4,990,000	257,517	--	--
2025-2029	5,815,000	150,755	--	--
2030-2033	<u>5,334,000</u>	<u>31,996</u>	--	--
	<u>\$24,100,000</u>	<u>\$1,217,203</u>	<u>\$757,145</u>	<u>\$55,571</u>

*Future interest payments are based on the loan amounts outstanding and interest rates in effect at June 30, 2009, and do not necessarily represent the payments that will be required.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

Activity for long-term debt for 2009 and 2008 follows:

	<u>Balance at June 30, 2008</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance at June 30, 2009</u>	<u>Amounts Due Within One Year</u>
Bonds payable	\$24,100,000	\$--	\$--	\$24,100,000	\$691,000
Capital lease #1	302,394	--	76,855	225,539	80,985
Capital lease #2	<u>685,262</u>	--	<u>153,656</u>	<u>531,606</u>	<u>160,278</u>
Total long-term debt	<u>\$25,087,656</u>	<u>\$--</u>	<u>\$230,511</u>	<u>\$24,857,145</u>	<u>\$932,263</u>

	<u>Balance at June 30, 2007</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance at June 30, 2008</u>	<u>Amounts Due Within One Year</u>
Amounts due to Rhea County, a related party					
RC note 2	\$138,512	\$--	\$138,512	\$ --	--
Bonds payable	18,877,386	5,222,614	--	24,100,000	--
Capital lease #1	374,969	--	72,575	302,394	76,474
Capital lease #2	--	<u>808,468</u>	<u>123,206</u>	<u>685,262</u>	<u>153,664</u>
Total long-term debt	<u>\$19,390,867</u>	<u>\$6,031,082</u>	<u>\$334,293</u>	<u>\$25,087,656</u>	<u>\$230,138</u>

NOTE I - ACCRUED LEAVE

Medical Center employees are paid for vacation and absence due to sickness by a prescribed formula based on length of service. The costs of these compensated absences are accrued as earned. The accumulated vacation and sick leave benefits accrued totaled \$276,802 and \$263,728 for 2009 and 2008, respectively, and are included with accrued payroll in current liabilities.

NOTE J - CHARITY CARE

The amount of charges forgone for services and supplies furnished under the Medical Center's charity care policy during the years ended June 30, 2009 and 2008, was \$311,636 and \$379,219, respectively.

NOTE K - PENSION PLANS

Effective January 1, 1990, Rhea County Government and related entities including the Medical Center joined the Tennessee Consolidated Retirement System (TCRS), a multiple-employer Public Employee Retirement System (PERS). All full-time personnel employed at or after January 1, 1990, are required to participate in the Tennessee Consolidated Retirement System Pension Plan. The Medical Center contributes the employer's share of pension contributions of 3%, and the employees are required to contribute 5% of their salaries to the plan. Past service costs as of January 1, 1990, were required to be funded upon entering the plan. The Medical Center has chosen to amortize these costs over a thirty-year period by increasing its contribution rate, which is currently 8.72%. Contributions by the Medical Center totaled \$591,574 and \$601,734 in 2009 and 2008, respectively. Information in regard to funding status, contribution requirements, and trends appear in the financial statements of Rhea County and cannot be separately identified for the Medical Center.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE L – NET WORKING CAPITAL

Net working capital at June 30, 2009 and 2008, was \$9,339,459 and \$7,685,794, respectively.

NOTE M - DESIGNATED NET ASSETS

Net assets reported in 2009 and 2008 include \$236,593 and \$229,106, respectively, which has been designated by the Medical Center's Board of Trustees for capital acquisitions. Designated funds remain under the control of the Board of Trustees, which may at its discretion later use the funds for other purposes.

NOTE N - COMMITMENTS AND CONTINGENCIES

Operating leases. Leases that do not meet the criteria for capitalization are classified as operating leases with related rentals charged to operations as incurred.

Rental expense included in operations amounted to \$180,920 and \$153,970 in 2009 and 2008, respectively.

Professional liability insurance. The Medical Center is insured for professional liability under a claims-made policy with an independent insurance carrier. The policy covers all claims reported to the carrier during the coverage period. Premiums are determined by a variety of factors related to the Medical Center.

Management agreement. A management agreement between the Medical Center and Quorum Health Resources, Inc., (Quorum) was signed on April 24, 2009, with effective dates of March 1, 2009 through February 28, 2016. The annual fee is \$266,917 for the contract year beginning March 1, 2009, increases annually by a factor equal to the lower of five percent or the percentage increase in the Consumer Price Index, and is payable in equal monthly installments. Management services in addition to the fixed fee services are provided by Quorum as needed at varying rates. The total management fees paid to Quorum were \$256,104 and \$252,286 in 2009 and 2008, respectively.

The management services provided pursuant to the fixed fee include budget assistance, accounting supervision, human resources consultations, and access to a Quorum sponsored volume purchasing program. Certain 'administrative fees' may be paid to Quorum by outside vendors that sell goods and services to the Medical Center. The administrative fee payable to Quorum by these outside vendors is equal to 3% or less of the purchase price of the goods or services purchased from the vendor by the Medical Center. The contract provides that these fees shall be disclosed to the Medical Center annually in writing.

Quorum also provides certain 'key personnel' to the Medical Center who are Quorum employees. The Medical Center reimburses Quorum for the costs and expenses (including but not limited to salaries, taxes, fringe benefits, and business expenses) of providing these key personnel as invoiced by Quorum. These reimbursements are in addition to the fixed annual management fee described above. The amount paid to Quorum for administrative compensation and other services was \$363,162 and \$349,019 for 2009 and 2008, respectively.

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

NOTES TO FINANCIAL STATEMENTS
(Continued)

Litigation. The Medical Center is subject to claims and suits which arise in the ordinary course of business. In the opinion of management, the ultimate resolution of such pending legal proceedings has been adequately provided for in its financial statements, and will not have a material effect on the Medical Center's results of operations or financial position.

NOTE O - CONCENTRATIONS OF CREDIT RISK

The Medical Center is located in Rhea County, Tennessee. The Medical Center grants credit 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 at June 30, 2009 and 2008, follows.

	<u>2009</u>	<u>2008</u>
Medicare	21%	24%
Medicaid/TennCare	11	15
Blue Cross	8	10
Commercial	11	11
Private pay	<u>49</u>	<u>40</u>
	<u>100%</u>	<u>100%</u>

NOTE P - SUBSEQUENT EVENTS

On July 1, 2009, the Medical Center sold the nursing home license and equipment to an unrelated party. The purchaser also entered into an agreement to lease the Nursing Home building for \$24,000 per month, on a month to month basis for approximately three years.

The Medical Center noted no transactions that would provide evidence about material conditions that did not exist at the balance sheet date but arose subsequently, through the date these financial statements were available to be issued, November 19, 2009.

SUPPLEMENTARY INFORMATION

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

SCHEDULE 1 - PATIENT SERVICE REVENUE

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
DAILY PATIENT SERVICES		
Routine care	\$6,737,389	\$6,660,307
Intensive care unit	<u>162,297</u>	<u>169,660</u>
TOTAL DAILY PATIENT SERVICES	<u>6,899,686</u>	<u>6,829,967</u>
OTHER NURSING SERVICES		
Operating and recovery rooms	1,748,850	947,036
Emergency room	6,582,852	6,333,528
Central supply	<u>1,731,501</u>	<u>1,112,578</u>
TOTAL OTHER NURSING SERVICES	<u>10,063,203</u>	<u>8,393,142</u>
OTHER PROFESSIONAL SERVICES		
Laboratory	5,725,167	5,545,252
Electrocardiology	369,600	402,099
Radiology	2,290,806	2,217,421
Cardiac rehab	107,431	74,701
Pharmacy	2,560,098	2,361,106
Anesthesiology	431,837	113,905
Physical therapy	1,580,536	1,488,386
Occupational therapy	349,723	184,870
Respiratory therapy	1,053,326	909,854
Intravenous therapy	529,673	545,239
Nuclear medicine	2,477,718	2,258,256
Vascular studies	347,793	326,269
CT scans	7,985,677	8,180,493
Bone densitometry	111,308	90,290
Industrial nursing	213,479	290,192
MRI	<u>117,937</u>	<u>125,739</u>
TOTAL OTHER PROFESSIONAL SERVICES	<u>26,252,109</u>	<u>25,114,072</u>
TOTAL PATIENT SERVICE REVENUE	<u>\$43,214,998</u>	<u>\$40,337,181</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
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SCHEDULE 2 - PROVISION FOR CONTRACTUAL ADJUSTMENTS AND BAD DEBTS

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Medicare and Medicaid	\$12,369,649	\$10,675,540
Blue Cross	2,637,304	2,430,164
Employee discounts	32,526	22,933
Other policy discounts	1,988,288	1,822,167
Bad debts	<u>3,686,316</u>	<u>3,356,243</u>
TOTAL CONTRACTUAL ADJUSTMENTS	<u>\$20,714,083</u>	<u>\$18,307,047</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

SCHEDULE 3 - OTHER OPERATING REVENUE

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Patient histories	\$887	\$360
Rental revenue	113,291	92,122
Cafeteria revenue	56,336	52,269
Vending revenue	2,980	3,492
Insurance rebate	167,517	--
Miscellaneous revenue	<u>40,349</u>	<u>63,302</u>
TOTAL OTHER OPERATING REVENUE	<u>\$381,360</u>	<u>\$211,545</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
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SCHEDULE 4 - SALARIES AND BENEFITS

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
NURSING SERVICES		
Nursing	\$2,628,045	\$2,604,694
Intensive care unit	117,370	102,950
Operating and recovery rooms	406,931	287,152
Emergency room	1,159,559	1,249,876
Central supply	<u>29,036</u>	<u>37,041</u>
TOTAL NURSING SERVICES	<u>4,340,941</u>	<u>4,281,713</u>
OTHER PROFESSIONAL SERVICES		
Laboratory	501,152	481,458
Radiology	501,086	489,088
Cardiac rehab	67,644	44,328
Pharmacy	176,709	181,940
Respiratory therapy	312,082	285,249
Nuclear medicine	276,655	252,562
CT scans	55,011	55,042
Clinic	47,909	38,621
Industrial nursing	158,895	178,483
MRI	<u>60,459</u>	<u>53,436</u>
TOTAL OTHER PROFESSIONAL SERVICES	<u>2,157,602</u>	<u>2,060,207</u>
GENERAL SERVICES		
Dietary	430,748	432,024
Building operation and maintenance	153,887	167,873
Housekeeping	285,643	266,750
Laundry	15,489	15,613
Medical records	220,068	225,710
Materials management	40,840	38,985
Activities	<u>83,146</u>	<u>75,620</u>
TOTAL GENERAL SERVICES	<u>1,229,821</u>	<u>1,222,575</u>
ADMINISTRATIVE AND FISCAL SERVICES		
Administrative and business office	<u>3,565,162</u>	<u>3,340,469</u>
TOTAL SALARIES AND BENEFITS	<u>\$11,293,526</u>	<u>\$10,904,964</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

SCHEDULE 5 - MEDICAL SUPPLIES AND DRUGS

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
NURSING SERVICES		
Nursing	\$56,767	\$63,302
Intensive care unit	113	26
Operating and recovery rooms	109,592	--
Emergency room	50,751	54,626
Central supply	<u>536,769</u>	<u>373,227</u>
 TOTAL NURSING SERVICES	 <u>753,992</u>	 <u>491,181</u>
OTHER PROFESSIONAL SERVICES		
Laboratory	367,966	379,771
Radiology	10,191	12,510
Cardiac rehab	2,475	3,191
Pharmacy	458,674	465,889
Physical therapy	8,238	4,799
Respiratory therapy	44,183	43,070
MRI	14,384	5,901
Intravenous therapy	21,668	17,969
Nuclear medicine	79,902	76,500
CT scans	64,954	70,307
Clinic	65	169
Industrial nursing	--	<u>532</u>
 TOTAL OTHER PROFESSIONAL SERVICES	 <u>1,072,700</u>	 <u>1,080,608</u>
 TOTAL MEDICAL SUPPLIES AND DRUGS	 <u>\$1,826,692</u>	 <u>\$1,571,789</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

SCHEDULE 6 - OTHER SUPPLIES

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
NURSING SERVICES		
Nursing	\$5,950	\$8,766
Operating and recovery rooms	3,143	3,657
Emergency room	12,520	13,360
Central supply	<u>656</u>	<u>1,100</u>
TOTAL NURSING SERVICES	<u>22,269</u>	<u>26,883</u>
OTHER PROFESSIONAL SERVICES		
Laboratory	4,186	3,966
Radiology	3,904	3,998
Cardiac rehab	984	402
Pharmacy	2,419	1,070
Physical therapy	2,550	1,630
Respiratory therapy	763	741
Nuclear medicine	742	567
CT scans	7,190	17,478
Clinic	1,322	616
Industrial nursing	<u>11,438</u>	<u>24,099</u>
TOTAL OTHER PROFESSIONAL SERVICES	<u>35,498</u>	<u>54,567</u>
GENERAL SERVICES		
Dietary	397,381	395,185
Building operation and maintenance	40,878	39,189
Housekeeping	70,103	72,919
Laundry	1,756	4,885
Medical records	3,027	6,400
Professional building	2,099	--
Activities	2,798	2,809
Gift shop	<u>28,713</u>	<u>41,261</u>
TOTAL GENERAL SERVICES	<u>546,755</u>	<u>562,648</u>
ADMINISTRATIVE AND FISCAL SERVICES		
Administrative and business office	<u>63,241</u>	<u>92,444</u>
TOTAL OTHER SUPPLIES	<u>\$667,763</u>	<u>\$736,542</u>

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

SCHEDULE 7 - OTHER EXPENSES

Years Ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
NURSING SERVICES		
Nursing	\$589,628	\$638,032
Intensive care unit	3,269	19,183
Operating and recovery rooms	86,569	77,124
Emergency room	80,933	180,835
Central supply	<u>173</u>	<u>5,967</u>
TOTAL NURSING SERVICES	<u>760,572</u>	<u>921,141</u>
OTHER PROFESSIONAL SERVICES		
Laboratory	173,348	181,968
Radiology	115,064	128,325
Cardiac rehab	9,726	6,643
Pharmacy	56,025	44,474
Anesthesiology	87,809	53,729
Physical therapy	573,878	528,081
Occupational therapy	111,600	68,062
Respiratory therapy	19,886	68,797
Nuclear medicine	136,131	65,970
CT scans	65,946	139,484
Clinic	91,772	6,859
Bone densitometry	5,467	6,207
Industrial nursing	<u>28,880</u>	<u>44,953</u>
TOTAL OTHER PROFESSIONAL SERVICES	<u>1,475,532</u>	<u>1,343,552</u>
GENERAL SERVICES		
Dietary	32,187	45,307
Building operation and maintenance	941,646	877,772
Housekeeping	9,322	26,393
Laundry	106,615	126,835
Medical records	65,562	45,571
Materials management	--	1,259
Professional building	27,686	22,394
Activities	<u>4,510</u>	<u>3,297</u>
TOTAL GENERAL SERVICES	<u>1,187,528</u>	<u>1,148,828</u>
ADMINISTRATIVE AND FISCAL SERVICES		
Administrative and business office	<u>1,778,479</u>	<u>1,662,081</u>
TOTAL OTHER EXPENSES	<u>\$5,202,111</u>	<u>\$5,075,602</u>

REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Trustees of
Rhea Medical Center (a component unit of Rhea County, Tennessee)

We have audited the financial statements of Rhea Medical Center (a component unit of Rhea County, Tennessee) (the Medical Center) as of and for the year ended June 30, 2009 and have issued our report thereon dated November 19, 2009. 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 the Medical Center'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 Medical Center's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Medical Center's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

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 Medical Center'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 Medical Center's financial statements that is more than inconsequential will not be prevented or detected by the Medical Center's internal control. We consider the deficiencies 2009-1 and 2009-2 described in the accompanying schedule of findings and responses to be significant deficiencies in internal control over financial reporting.

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 Medical Center'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 and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rhea Medical Center's (a component unit of Rhea County, Tennessee) 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*.

This report is intended solely for the information of the Board of Trustees, management, the State of Tennessee, and the Rhea County Government and is not intended and should not be used by anyone other than these specified parties.

Burd, Reulman, Netherly, Huggins, PLLC

Chattanooga, Tennessee
November 19, 2009

RHEA MEDICAL CENTER (A COMPONENT UNIT OF
RHEA COUNTY, TENNESSEE)

SCHEDULE OF FINDINGS AND RESPONSES

Year Ended June 30, 2009

PRIOR YEAR FINDINGS

None

CURRENT YEAR FINDINGS AND RESPONSES

Finding 2009-1:

Condition: Management's estimate of the allowance for uncollectible accounts was not sufficient at June 30, 2009.

Criteria: The allowance for uncollectible accounts must be sufficient to cover all known and potential bad debts.

Effect: The allowance for uncollectible accounts was understated and required an audit entry to correct.

Recommendation: Management should review the methods and assumptions used to calculate the estimate.

View of Responsible Officials: The officials concur with the finding. The estimate now incorporates the payor source as well as the aging of the accounts receivable, which gives a more accurate estimate.

Planned Corrective Action: Management's response is located on page 35.

Finding 2009-2:

Condition: A deficiency in internal control allowed a journal entry to be recorded after the final review of the financial statements by management but before audit.

Criteria: Journal entries should be properly authorized and recorded. Journal entries should not be made after final review by management.

Effect: The financial statements were materially misstated, and an audit journal entry was required to correct them.

Recommendation: Management should take steps to ensure that all journal entries are properly approved and recorded.

Views of Responsible Officials: The officials concur with the finding. Controls are being implemented to prevent entries from being posted without proper approval or after a month has been approved and presented to the Board of Directors.

Planned Corrective Action: Management's response is located on page 35.

RHEA MEDICAL CENTER

HOSPITAL NURSING HOME PROFESSIONAL BUILDING

November 19, 2009

Tennessee Department of Audit
Division of County Audit
Suite 1500
James K. Polk State Office Building
Nashville, TN 37243-1402

Rhea Medical Center (A Component Unit of Rhea County, Tennessee) submits the following plan for corrective action regarding reportable conditions associated with our internal controls and compliance for the year ended June 30, 2009.

The "Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards" issued by Burk, Pearlman, Nebben & Huggins, PLLC, on November 19, 2009, referenced instances of noncompliance and reportable conditions. The corrective action taken on these items is as follows:

Finding 2009-1

Our estimate of the allowance for uncollectible accounts was not sufficient at June 30, 2009.

Corrective Action Plan:

We concur with the recommendation. Our process of estimating the allowance now includes weighting the payor type as well as the aging of the accounts receivable detail. We believe this provides a more accurate estimate of uncollectible accounts.

Finding 2009-2

A deficiency in internal control allowed a journal entry to be recorded after the financial statements were reviewed and approved by management.

Corrective Action Plan:

We are implementing additional controls to prevent journal entries from being entered into the general ledger after the month has been reviewed and approved by management.

Sincerely,



Harv Sanders
CFO