

MAURY REGIONAL HOSPITAL

***Audited Combined Financial Statements
(and Other Information)***

Years Ended June 30, 2011 and 2010



MAURY REGIONAL HOSPITAL

Audited Combined Financial Statements

Years Ended June 30, 2011 and 2010

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INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of
Maury Regional Hospital:

We have audited the accompanying combined balance sheets of Maury Regional Hospital (the Hospital), a part of the primary government of Maury County, Tennessee, as of June 30, 2011 and 2010 and the related combined statements of revenue, expenses and changes in net assets and cash flows for the years then ended. These combined financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and 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 audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal controls over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Maury Regional Hospital as of June 30, 2011 and 2010, 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.

Maury Regional Hospital has not presented a Management Discussion and Analysis (MD&A) as required by Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Government Units*. The MD&A is required supplemental information but not a component of the audited combined financial statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 12, 2011 on our consideration of the Hospital's internal control over financial reporting and on 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 controls 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.

Perishing Yuley & Associates PC

Knoxville, Tennessee
October 12, 2011

MAURY REGIONAL HOSPITAL

Combined Balance Sheets

	<i>June 30,</i>	
	<i>2011</i>	<i>2010</i>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 15,219,864	\$ 34,846,832
Certificates of deposit	3,624,301	4,987,211
Investments	514,529	-
Patient accounts receivable, net of estimated allowance for doubtful accounts of approximately \$28,700,000 in 2011 and \$22,500,000 in 2010	32,677,216	28,805,056
Inventories	5,046,752	5,105,451
Prepaid expenses	3,490,160	3,179,010
Other receivables	1,118,346	1,130,794
TOTAL CURRENT ASSETS	61,691,168	78,054,354
ASSETS LIMITED AS TO USE	32,767,160	4,510,579
PROPERTY, PLANT AND EQUIPMENT, net	118,048,697	121,199,400
OTHER ASSETS		
Debt issue costs, net of accumulated amortization of \$255,765 in 2011 and \$213,831 in 2010	214,088	256,022
Other	1,105,390	483,378
TOTAL OTHER ASSETS	1,319,478	739,400
TOTAL ASSETS	\$ 213,826,503	\$ 204,503,733

	<i>June 30,</i>	
	<i>2011</i>	<i>2010</i>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current portion of long-term debt	\$ 4,905,385	\$ 4,627,180
Accounts payable and accrued expenses	6,845,552	9,321,222
Accrued salaries and wages	4,107,816	4,557,718
Accrued compensated absences	4,598,316	4,313,344
Accrued workers' compensation	3,848,982	3,842,792
Estimated amounts due to third party payors, net	4,166,103	4,379,952
Interest payable	111,781	153,833
TOTAL CURRENT LIABILITIES	28,583,935	31,196,041
OTHER LONG-TERM LIABILITIES, including estimated amounts due to third party payors and retirement benefits	7,789,688	2,183,427
LONG-TERM DEBT		
Bonds payable	24,624,668	28,636,698
Other long-term debt	1,086,967	1,817,133
	25,711,635	30,453,831
Less current portion	(4,905,385)	(4,627,180)
TOTAL LONG-TERM DEBT	20,806,250	25,826,651
COMMITMENTS AND CONTINGENCIES - Note J		
NET ASSETS		
Invested in capital assets, net of related debt	92,337,062	90,745,569
Unrestricted	64,309,568	54,552,045
TOTAL NET ASSETS	156,646,630	145,297,614
TOTAL LIABILITIES AND NET ASSETS	\$ 213,826,503	\$ 204,503,733

MAURY REGIONAL HOSPITAL

Combined Statements of Revenue, Expenses and Changes in Net Assets

	<i>Year Ended June 30,</i>	
	<i>2011</i>	<i>2010</i>
OPERATING REVENUE		
Net patient service revenue, net of estimated provision for bad debts of approximately \$28,720,000 in 2011 and \$31,560,000 in 2010	\$ 265,048,059	\$ 252,285,547
Other operating revenue	5,688,257	5,578,651
TOTAL OPERATING REVENUE	270,736,316	257,864,198
OPERATING EXPENSES		
Salaries, employee benefits and contract labor	148,144,914	145,944,517
Supplies	47,438,501	43,998,068
Purchased services	18,880,640	18,602,536
Professional fees	7,454,792	6,324,695
Repairs and maintenance	3,121,029	2,631,398
Utilities	5,198,079	4,959,102
Leases	4,230,939	3,894,054
Insurance	1,634,243	1,659,421
Other expenses	6,224,790	6,203,546
Depreciation and amortization	17,463,032	16,632,885
TOTAL OPERATING EXPENSES	259,790,959	250,850,222
INCOME FROM OPERATIONS	10,945,357	7,013,976
NONOPERATING REVENUE (EXPENSES)		
Contributions and grants	676,871	628,788
Investment income	697,704	375,950
Interest expense	(1,087,502)	(1,492,981)
Other	20,665	57,039
TOTAL NONOPERATING REVENUE (EXPENSES)	307,738	(431,204)
EXCESS OF REVENUE OVER EXPENSES	11,253,095	6,582,772
Minority interest in losses of subsidiaries	95,921	214,890
CHANGE IN NET ASSETS	11,349,016	6,797,662
NET ASSETS, BEGINNING OF YEAR	145,297,614	138,499,952
NET ASSETS, END OF YEAR	\$ 156,646,630	\$ 145,297,614

MAURY REGIONAL HOSPITAL

Combined Statements of Cash Flows

	<i>Year Ended June 30,</i>	
	<i>2011</i>	<i>2010</i>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from patients and insurance programs	\$ 266,230,389	\$ 263,706,658
Payments to vendors for supplies and other	(96,911,134)	(89,144,506)
Payments to and on behalf of employees	(147,965,732)	(145,153,336)
Other receipts	5,238,454	6,587,824
NET CASH PROVIDED BY OPERATING ACTIVITIES	26,591,977	35,996,640
CASH FLOWS FROM NONCAPITAL FINANCIAL ACTIVITIES:		
Contributions and grants	676,871	628,788
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition of property, plant and equipment	(14,579,937)	(7,337,407)
Proceeds from sale of equipment	666,367	431,787
Proceeds from issuance of long-term debt	266,400	-
Payments on long-term debt	(4,841,566)	(7,023,685)
Interest paid on long-term debt	(1,296,584)	(1,512,037)
NET CASH USED IN CAPITAL AND RELATED FINANCING ACTIVITIES	(19,785,320)	(15,441,342)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Interest income received on cash and investments	697,704	375,950
Proceeds from maturities of certificates of deposit	8,611,512	1,714,026
Purchase of certificates of deposit	(7,248,602)	(6,100,686)
Purchases of investments	(21,365,773)	(4,260,579)
Investment in joint venture	(400,000)	-
Contribution from minority shareholder	-	73,500
NET CASH USED IN INVESTING ACTIVITIES	(19,705,159)	(8,197,789)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(12,221,631)	12,986,297
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	34,846,832	21,860,535
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 22,625,201	\$ 34,846,832

	<i>Year Ended June 30,</i>	
	<i>2011</i>	<i>2010</i>
RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE COMBINED BALANCE SHEET CLASSIFICATIONS		
Cash and cash equivalents	\$ 15,219,864	\$ 34,846,832
Assets limited as to use	7,405,337	-
	<u>\$ 22,625,201</u>	<u>\$ 34,846,832</u>
RECONCILIATION OF INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Income from operations	\$ 10,945,357	\$ 7,013,976
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Depreciation and amortization	17,463,032	16,632,885
Estimated provision for uncollectible accounts	28,721,811	31,558,791
Changes in:		
Patient accounts receivable	(32,593,971)	(24,912,849)
Inventories	58,699	(773,591)
Prepaid expenses	(311,150)	(1,382,151)
Estimated amounts due to third party payors	(213,849)	4,775,169
Other assets	(449,803)	1,009,173
Accounts payable and accrued expenses	(2,475,670)	1,284,056
Accrued salaries and wages	(449,902)	411,172
Accrued compensated absences	284,972	318,171
Accrued workers' compensation	6,190	(171,589)
Other long-term liabilities	5,606,261	233,427
TOTAL ADJUSTMENTS	<u>15,646,620</u>	<u>28,982,664</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 26,591,977</u>	<u>\$ 35,996,640</u>

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements

Years Ended June 30, 2011 and 2010

NOTE A--ORGANIZATION

Maury Regional Hospital (the Hospital) is operated and maintained by Maury County, Tennessee, under authority of and in compliance with the provisions of Chapter 125 of the Tennessee Private Acts of 1996. The federal, state, and local governments participated in the cost of constructing and equipping the Hospital under the Hill-Burton Act. For financial reporting purposes, the Hospital is considered an enterprise fund of Maury County, Tennessee (the County).

The Hospital's primary mission is to provide healthcare services to the residents of southern and middle Tennessee, including Giles, Hickman, Lawrence, Lewis, Marshall, Maury, Perry, Wayne, and Williamson counties.

The combined financial statements include the accounts of the following operating entities:

Maury Regional Medical Center (MRMC), located in Columbia, Tennessee, has been in operation since 1953 and presently has a 275-bed capacity with 20 beds designated for skilled nursing care, and also includes five medical office buildings in its service area.

Marshall Medical Center is an acute care hospital, located in Lewisburg, Tennessee, which was acquired by the Hospital in 1995 and, effective January 1, 2005, was designated a Critical Access Hospital with 25 licensed beds.

Wayne Medical Center is an acute care hospital with an 80-bed capacity located in Waynesboro, Tennessee, and has been leased by the Hospital since 1995 (see Note I).

Additionally, the combined financial statements include the following blended component units that provide healthcare services that support the Hospital's mission:

Family Health Group (FHG) is a nonprofit corporation which acquires, owns, operates, and manages physician practices in the Hospital's service area. During 2010, the Hospital had an 80% interest in the profits and losses of FHG. During 2011, the Hospital acquired the remaining interest and became the sole member.

South Central Heart Group, Inc. (SCHG), *Thoracic and Cardiovascular Associates of Tennessee, Inc. (TCAT)*, and *Pulmonary and Critical Care Associates, Inc.* are taxable nonprofit corporations that operate physician practices in the Hospital's service area. The Hospital is the sole member of each practice. During 2011, SCHG and TCAT were dissolved and became divisions of MRMC.

Maury Regional Ambulatory Care Center, Inc. (the Ambulatory Care Center) is a nonprofit corporation that provides medical care to non-emergent patients in the Hospital's service area. The Hospital is the sole member of the Ambulatory Care Center.

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE A--ORGANIZATION - Continued

Spring Hill Imaging Center, LLC (the Imaging Center) owns and operates an outpatient center that provides diagnostic and radiology services to patients in the Hospital's service area. The Imaging Center is owned 51% by the Hospital and a minority interest in the cumulative losses has been recognized as a receivable which represents the interests of physician and other investors.

Maury Regional Healthcare Foundation is a not-for-profit organization formed in 2007 to coordinate the fundraising activities of the Hospital.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting: The Hospital utilizes the enterprise fund method of accounting. Revenue and expenses are recorded on the accrual basis. In December 2010, the Governmental Accounting Standards Board (GASB) issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) Pronouncements*. This Statement incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which do not conflict with or contradict GASB pronouncements: FASB Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the AICPA Committee on Accounting Procedure. This Statement also supersedes Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*. The requirements of this Statement are effective for periods beginning after December 15, 2011, however, earlier application is permitted and the Hospital adopted the provisions of this Statement during fiscal year 2011. The adoption did not have a material impact on the combined financial statements.

Recently Issued or Effective Accounting Pronouncements: In June 2010, the GASB issued Statement No. 59, *Financial Instruments Omnibus*. The Statement is effective for years beginning after June 15, 2010 and updates current standards regarding the financial reporting of financial instruments and external investment pools. The requirements of this Statement will improve financial reporting by providing more complete information, by improving consistency of measurements, and by providing clarifications of existing standards. The requirements of this Statement were adopted by the Hospital in fiscal year 2011 and the adoption did not have a material impact on the combined financial statements.

In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*. The Statement is effective for financial statement periods beginning after June 15, 2012 and amends Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for*

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

State and Local Governments. This Statement modifies certain requirements for inclusion of component units in the financial reporting entity and amends the criteria for reporting component units as if they were part of the primary government in certain circumstances. Management of the Hospital is evaluating the impact of this Statement on the combined financial statements.

In January 2010, FASB issued Accounting Standard Update 2010-06, *Improving Disclosures about Fair Value Measurements*, as it relates to FASB Accounting Standards Codification (ASC) 820. This Update provides amendments to FASB ASC 820, *Fair Value Measurements*, that requires both new disclosures and further clarifies existing disclosures. This Update is effective for years beginning after December 15, 2009, except for disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements, which is effective for years beginning after December 15, 2010. The requirements of this update which were adopted in fiscal year 2011 did not have a material impact on the combined financial statements.

In August 2010, FASB issued Accounting Standard Update 2010-23, *Measuring Charity Care for Disclosure*, that amends Topic 954, *Health Care Entities*. This Update provides amendments that require cost to be used as the measurement basis for charity care disclosure purposes and that cost be identified as the direct and indirect costs of providing the charity care. The amendments in this Update also require disclosure of the method used to identify or determine such costs. This Update is effective for fiscal years beginning after December 15, 2010 and should be applied retrospectively to all periods. Management of the Hospital is evaluating the impact of this Statement on the combined financial statements.

Also, in August 2010, FASB issued Accounting Standard Update 2010-24, *Presentation of Insurance Claims and Related Insurance Recoveries*, which provides amendments that clarify that a health care entity should not net insurance recoveries against a related claim liability. Additionally, the amount of the claim liability should be determined without consideration of insurance recoveries. Prior to this Update, health care entities were permitted to net insurance recoveries against the accrual of malpractice claims or similar liabilities. This Update is effective for fiscal years beginning after December 15, 2010, and a cumulative-effect adjustment should be recognized in opening net assets in the period of adoption if a difference exists between any liabilities and insurance receivables recorded as a result of applying the amendments in this Update. Management of the Hospital is evaluating the impact of this Update on the combined financial statements but does not anticipate any material impact on operations or net assets upon adoption.

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

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Cash and Cash Equivalents: Cash and cash equivalents includes cash on hand, deposits in banks and investments with a maturity of three months or less when purchased, excluding any amounts whose use is limited by Board designation.

Inventories: Inventories consist principally of medical and surgical supplies and are reported at the lower of cost or market, with cost determined by the average cost method.

Patient Accounts Receivable: Patient accounts receivable are reported net of both an estimated allowance for contractual adjustments and an estimated allowance for uncollectible accounts. The contractual allowance represents the difference between established billing rates and estimated reimbursement from Medicare, TennCare and other third party payor programs. Current operations are charged with a provision for bad debts estimated based upon the age of the account, prior experience and any unusual circumstances which affect the collectibility. The Hospital's policy does not require collateral or other security for patient accounts receivable and the Hospital routinely accepts assignment of, or is otherwise entitled to receive, patient benefits payable under health insurance programs, plans or policies.

Investments and Assets Limited as to Use: Investments and assets limited as to use in debt and equity securities are reported at fair value based on quoted market prices. Interest, dividends, and gains and losses (realized and unrealized) are included in investment income. During 2011, the Board designated certain assets as limited as to use for future capital improvements. Assets limited as to use consists of money market deposits, certificates of deposits, and investments. Certain investments and deposits reported in the 2010 financial statements have been reclassified to reflect this designation for consistency purposes.

Property, Plant and Equipment: Property, plant and equipment is reported at cost or fair value at date of gift, if donated. The Hospital has established a capitalization threshold of \$1,000. Depreciation is calculated by the straight-line method to allocate the cost of the assets (other than land) over their estimated useful lives which ranges from 3 to 20 years for equipment and 10 to 40 years for buildings and land improvements. Equipment held under capital lease obligations is amortized using the straight-line method over the shorter of the estimated useful life or the lease term. This amortization is included with depreciation expense and as part of accumulated depreciation in the combined financial statements. Interest costs incurred on applicable borrowings outstanding during the construction period of capital assets is capitalized as part of the cost of acquiring the asset and is amortized on the same basis as the related capital asset. Costs of maintenance and repairs are charged to expense when incurred. The Hospital periodically reviews property, plant, and equipment for indications of potential impairment. Management does not believe any impairment exists as of June 30, 2011.

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Debt Issue Costs: Debt issue costs are capitalized and amortized using the straight-line method over the life of the related obligation.

Compensated Absences: The Hospital's employees earn paid time off at varying rates depending on years of service. An accrual for paid time off is recorded in the period in which the employee earns the right to the compensation. Employees also earn sick leave benefits based on varying rates depending on years of service and may accumulate sick leave up to a specified maximum. Employees are not paid for accumulated sick leave if they leave before retirement. However, employees who retire after the age of sixty may convert accumulated sick leave to termination payments. The estimated amount of sick leave which will ultimately be payable as termination payments is reported as a noncurrent liability in the combined financial statements. Due to uncertainties in this estimate, it is at least reasonably possible that management's estimate could change in 2012.

Net Assets: *Net assets invested in capital assets, net of related debt* consist of capital assets net of accumulated depreciation and reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Unrestricted net assets* are remaining net assets that do not meet the definition of invested in capital assets, net of related debt.

Net Patient Service Revenue: Net patient service revenue is reported as services are rendered at estimated net realizable amounts, including estimated retroactive revenue adjustments under reimbursement agreements with third party payors. Estimated settlements under third party reimbursement agreements are accrued in the period the related services are rendered and adjusted in future periods as final settlements are determined. An estimated provision for bad debts is included in net patient service revenue.

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

Operating Activities: The Hospital defines operating activities as reported on the Combined Statements of Revenue, Expenses and Changes in Net Assets as those that generally result from exchange transactions, such as payments for providing services and payments for goods and services received. Non-exchange transactions, including contributions and grants, as well as interest income and interest expense, are considered non-operating revenue and expenses.

Contributions and Grants: Revenues from contributions and grants are recognized when all eligibility requirements, including time requirements are met. Contributions and grants may be restricted for specific operating purposes or for capital purposes. Amounts that are unrestricted or

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

that are restricted to a specific operating purpose are reported as nonoperating revenue. Amounts restricted to capital acquisitions are reported after nonoperating revenue and expenses.

Income Taxes: The Hospital is a not-for-profit entity in accordance with Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. The Hospital meets the Internal Revenue Service definition of a governmental unit and is exempt from filing a Form 990 based on Internal Revenue Procedure 95-48. Certain combined entities are taxable for federal purposes and account for income taxes in accordance with FASB ASC 740, *Income Taxes*. Due to current year and prior year operating losses, no tax expense or benefit has been recognized in the accompanying combined financial statements.

Subsequent Events: The Hospital evaluated all events or transactions that occurred after June 30, 2011 through October 12, 2011, the date the combined financial statements were available to be issued. Management did not note any subsequent events that required recognition or disclosure in the combined financial statements at June 30, 2011.

Reclassifications: Certain reclassifications have been made to the 2010 combined financial statements to conform with the 2011 presentation.

NOTE C--PATIENT SERVICE REVENUE AND ACCOUNTS RECEIVABLE

The Hospital has agreements with various third party payors that provide for payments to the Hospital at amounts different from established rates. The difference between the rates charged and the estimated payments from third party payors is recorded as a reduction of gross patient service charges. Revenue for patient service charges have been adjusted to the amounts estimated to be receivable under third party payor arrangements. Amounts recorded under these contractual arrangements are subject to review and final determination by various program intermediaries. Management believes that adequate provision has been made for any adjustments which may result from such reviews. However, due to uncertainties in the estimates, it is at least reasonably possible that management's estimates will change in 2012. Net patient service revenue for the years ended June 30, 2011 and 2010 was increased by approximately \$900,000 and \$1,050,000, respectively, due to adjustments of estimates or final settlements of prior periods.

A summary of the payment arrangements with significant third party payors follows:

Medicare: Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid primarily on a prospective basis. These rates vary according to a patient classification system that is based on clinical diagnosis, procedures utilized and other factors. The Medicare program continues to reimburse certain other services based on a per diem or on a

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE C--PATIENT SERVICE REVENUE AND ACCOUNTS RECEIVABLE - Continued

percentage of cost up to predetermined limits. The Hospital also receives additional payments from the Medicare program for providing services to a disproportionate share of Medicaid (TennCare) and other low income patients. Approximately \$9,300,000 and \$9,500,000 of net patient accounts receivable are due from the Medicare program at June 30, 2011 and 2010, respectively.

TennCare: The State of Tennessee's Medicaid waiver program (TennCare) provides coverage through several managed care organizations. TennCare reimbursement for both inpatient and outpatient services is based upon prospectively determined rates and per diem amounts. Approximately \$2,500,000 and \$1,900,000 of net patient accounts receivable are from payors under the TennCare program at June 30, 2011 and 2010, respectively. During 2011 and 2010, the Hospital received additional distributions under the TennCare Essential Access, federal matching and other programs totaling approximately \$3,090,000 and \$1,350,000, respectively. Future distributions under these programs are not guaranteed.

Other: The Hospital has also 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, discounts from established charges, and prospectively determined per diem amounts.

A reconciliation of the amount of services provided to patients at established rates to net patient service revenue is as follows:

	<i>Year Ended June 30</i>	
	<i>2011</i>	<i>2010</i>
Patient service charges	\$ 695,178,988	\$ 658,588,796
Estimated contractual adjustments	(388,577,494)	(361,995,480)
Estimated provision for bad debts	(28,721,811)	(31,558,791)
Charity care	(12,831,624)	(12,748,978)
	<u>\$ 265,048,059</u>	<u>\$ 252,285,547</u>

NOTE D--CASH, CASH EQUIVALENTS, CERTIFICATES OF DEPOSIT, INVESTMENTS AND ASSETS LIMITED AS TO USE

The carrying amount of deposits and investments included in the Hospital's balance sheets is as follows:

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE D--CASH, CASH EQUIVALENTS, CERTIFICATES OF DEPOSIT, INVESTMENTS AND ASSETS LIMITED AS TO USE - Continued

	<u>2011</u>	<u>2010</u>
Deposits	\$ 27,805,376	\$ 40,084,043
Investments	24,320,478	4,260,579
	<u>\$ 52,125,854</u>	<u>\$ 44,344,622</u>

Included in the combined financial statements as follows:

	<u>2011</u>	<u>2010</u>
Cash and cash equivalents	\$ 15,219,864	\$ 34,846,832
Certificates of deposit	3,624,301	4,987,211
Investments	514,529	-
Assets limited as to use	32,767,160	4,510,579
	<u>\$ 52,125,854</u>	<u>\$ 44,344,622</u>

The Hospital holds deposits only in banks participating in the State of Tennessee Collateral Pool, in banks that provide collateral for all deposits or banks that are members of the Federal Deposit Insurance Corporation (FDIC). Certificates of deposit in excess of the FDIC insurance limit must be issued by a bank that is a member of the Certificate of Deposit Account Registry Service.

Additionally, the Hospital's deposits in financial institutions are required by State statute to be secured and collateralized by the institutions. Collateral requirements are not applicable for financial institutions that participate in the State of Tennessee's collateral pool. Collateral securities required to be pledged by the participating banks to protect their public fund accounts are pledged to the State Treasurer on behalf of the collateral pool. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

At June 30, 2011, the Hospital's bank balances for deposits totaled \$31,526,979, a majority of which was insured by the FDIC or by the bank's participation in the State of Tennessee's collateral pool. Deposits totaling \$1,069,216 are collateralized by securities held by the financial institution and pledged as collateral for the Hospital's deposits.

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE D--CASH, CASH EQUIVALENTS, CERTIFICATES OF DEPOSIT, INVESTMENTS AND ASSETS LIMITED AS TO USE - Continued

The estimated fair values and maturities for investments, all of which were held in the Hospital's name by a custodial bank that is an agent of the Hospital, are as follows:

<u>June 30, 2011</u> <i>Investment Type</i>	<i>Carrying Amount</i>	<u>Investment Maturities in Years</u>		<i>N/A</i>
		<i>Less than 1</i>	<i>1-5</i>	
Mutual funds - fixed income	\$ 3,455,070	\$ 3,455,070	\$ -	\$ -
Mutual funds - equity	281,998	-	-	281,998
Government agency bonds	18,572,390	-	18,572,390	-
Corporate bonds	2,011,020	-	2,011,020	-
	<u>\$ 24,320,478</u>	<u>\$ 3,455,070</u>	<u>\$ 20,583,410</u>	<u>\$ 281,998</u>

<u>June 30, 2010</u> <i>Investment Type</i>	<i>Carrying Amount</i>	<u>Investment Maturities in Years</u>		<i>N/A</i>
		<i>Less than 1</i>	<i>1-5</i>	
Mutual funds - fixed income	\$ 1,510,731	\$ 1,510,731	\$ -	\$ -
Government agency bonds	2,511,100	-	2,511,100	-
Corporate bonds	238,748	-	238,748	-
	<u>\$ 4,260,579</u>	<u>\$ 1,510,731</u>	<u>\$ 2,749,848</u>	<u>\$ -</u>

Interest Rate Risk: As a means to limiting its exposure to fair value losses by rising interest rates, the Hospital's investment policy limits investment in U.S. treasury securities, government agency bonds or notes, corporate bonds, and municipal bonds to those with maturities of less than five years.

Credit Risk: The Hospital's investment policy restricts investments in corporate bonds and municipal bonds to those with a credit rating of at least AA. Mutual fund's underlying investments must meet the same credit ratings as other investments. At June 30, 2011, the Hospital's investment in corporate bonds and mutual funds were rated AAA by Standard and Poor's.

Concentration of Credit Risk: The Hospital's investment policy limits investments in corporate bonds to 50% of total investments with no security issuer exceeding 5% of total investments and municipal bonds to 25% of total investments with no security issuer exceeding 5% of total investments. There is no limit on investments in U.S. treasury securities, government agency bonds or notes. Mutual funds containing corporate bonds should not exceed 50% of total investments and a single mutual fund should not exceed 25% of total investments.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Hospital will be able to recover the value of its investment or collateral. All investments are in the Hospital's name at a custodial bank.

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE E--PROPERTY, PLANT AND EQUIPMENT

A summary of changes in property, plant and equipment and related accumulated depreciation for the years ended June 30, 2011 and 2010 is as follows:

	<i>Balance July 1, 2010</i>	<i>Additions/ Transfers</i>	<i>Retirements</i>	<i>Balance June 30, 2011</i>
<u>Capital assets being depreciated</u>				
Land improvements	\$ 5,424,616	\$ 131,568	\$ -	\$ 5,556,184
Buildings	166,452,249	1,423,641	(17,312)	167,858,578
Equipment	134,045,305	10,060,135	(3,540,865)	140,564,575
Total capital assets being depreciated	305,922,170	11,615,344	(3,558,177)	313,979,337
Less accumulated depreciation for:				
Land improvements	3,539,538	176,071	-	3,715,609
Buildings	79,331,452	7,166,239	-	86,497,691
Equipment	108,053,533	9,864,265	(3,034,112)	114,883,686
Total accumulated depreciation	190,924,523	17,206,575	(3,034,112)	205,096,986
Total capital assets being depreciated, net	114,997,647	(5,591,231)	(524,065)	108,882,351
<u>Capital assets not being depreciated</u>				
Land	5,098,378	1,167,502	-	6,265,880
Construction in progress	1,103,375	1,797,091	-	2,900,466
Total capital assets not being depreciated	6,201,753	2,964,593	-	9,166,346
Total capital assets, net	\$ 121,199,400	\$ (2,626,638)	\$ (524,065)	\$ 118,048,697
	<i>Balance July 1, 2009</i>	<i>Additions/ Transfers</i>	<i>Retirements</i>	<i>Balance June 30, 2010</i>
<u>Capital assets being depreciated</u>				
Land improvements	\$ 5,421,136	\$ 3,480	\$ -	\$ 5,424,616
Buildings	163,923,772	2,528,477	-	166,452,249
Equipment	130,844,689	4,949,339	(1,748,723)	134,045,305
Total capital assets being depreciated	300,189,597	7,481,296	(1,748,723)	305,922,170
Less accumulated depreciation for:				
Land improvements	3,360,964	178,574	-	3,539,538
Buildings	72,154,230	7,177,222	-	79,331,452
Equipment	100,281,020	9,132,507	(1,359,994)	108,053,533
Total accumulated depreciation	175,796,214	16,488,303	(1,359,994)	190,924,523
Total capital assets being depreciated, net	124,393,383	(9,007,007)	(388,729)	114,997,647
<u>Capital assets not being depreciated</u>				
Land	5,098,378	-	-	5,098,378
Construction in progress	1,247,264	(143,889)	-	1,103,375
Total capital assets not being depreciated	6,345,642	(143,889)	-	6,201,753
Total capital assets, net	\$ 130,739,025	\$ (9,150,896)	\$ (388,729)	\$ 121,199,400

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE E--PROPERTY, PLANT AND EQUIPMENT - Continued

During 2011 and 2010, the Hospital capitalized interest expense on construction projects totaling approximately \$78,000 and \$28,000, respectively. Construction in progress at June 30, 2011 consists primarily of facility renovations and total estimated costs required to complete construction in progress amounted to approximately \$5,500,000.

NOTE F--LONG-TERM DEBT

Long-term debt consists of the following as of June 30:

	<u>2011</u>	<u>2010</u>
Bonds Payable:		
Series 2006B, Maury County General Obligation Bond: issued on behalf of the Hospital, with interest rates from 4.00% to 4.25%, maturing over a 7-year period, with the final payment due June 1, 2014.	\$ 3,775,000	\$ 4,935,000
Series 2006, Maury County General Obligation Bonds issued on behalf of the Hospital, with interest rates from 4.125% to 5.00%, maturing over a 15-year period, with the final payment due June 1, 2021.	14,100,000	15,520,000
Series 2005, Maury County General Obligation Bonds issued on behalf of the Hospital, with interest rates from 3.375% to 4.00%, maturing over a 15-year period, with the final payment due June 1, 2020.	2,845,000	3,110,000
Series 2004B, Maury County General Obligation Refunding Bonds issued on behalf of the Hospital, with an interest rate of 5.00%, maturing over a 10- year period, with the final payment due April 1, 2014.	3,225,000	4,225,000
Total bonds payable	23,945,000	27,790,000
Unamortized loss on refunding	(106,203)	(146,030)
Unamortized premiums	785,871	992,728
Total bonds payable, net of unamortized loss and premiums	24,624,668	28,636,698

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE F--LONG-TERM DEBT - Continued

	<u>2011</u>	<u>2010</u>
Other Long-term Debt:		
Notes payable with interest rates ranging from 6.1% to 6.29% maturing through January, 2014 and secured by equipment and property with a net book value of \$40,392 at June 30, 2011	45,573	214,649
Line of credit with interest rate of 5.25% due in 2012, maximum available of \$775,000	710,243	735,243
Capital lease obligations - see Note H	331,151	867,241
Total other long-term debt	<u>1,086,967</u>	<u>1,817,133</u>
	25,711,635	30,453,831
Less: current portion	<u>4,905,385</u>	<u>4,627,180</u>
	<u>\$ 20,806,250</u>	<u>\$ 25,826,651</u>

The Hospital's bonds payable are general obligation bonds of Maury County, Tennessee. The bonds were issued for the purpose of acquiring property and equipment or for the retirement of previously outstanding bonds and notes and are secured by unlimited ad valorem taxes on all taxable property within the County.

The Series 2006 Bonds maturing on or after June 1, 2017 are subject to redemption prior to maturity at the option of the County on June 1, 2016 or thereafter, at a redemption price of par plus accrued interest. The Series 2004B Refunding Bonds maturing on or after April 1, 2013 are subject to redemption prior to maturity at the option of the County on April 1, 2012 at 102% of par or on April 1, 2013 at 101% of par.

The Hospital's scheduled principal maturities on all long-term debt as of June 30, 2011 (including the capital lease obligations and excluding unamortized premiums and loss on refunding) follows:

<u>Year Ending June 30</u>	<u>Principal</u>	<u>Interest</u>
2012	\$ 4,905,385	\$ 1,107,699
2013	4,119,897	891,315
2014	4,166,685	712,800
2015	1,725,000	521,528
2016	1,735,000	438,328
2017-2021	<u>8,380,000</u>	<u>1,040,979</u>
	<u>\$ 25,031,967</u>	<u>\$ 4,712,649</u>

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE F--LONG-TERM DEBT - Continued

A schedule of changes in long-term debt for the years ended June 30, 2011 and 2010 is as follows:

	<i>Balance</i> <i>July 1, 2010</i>	<i>Additions/</i> <i>Amortization</i>	<i>Payments/</i> <i>Maturities</i>	<i>Balance</i> <i>June 30, 2011</i>	<i>Amounts Due</i> <i>Within</i> <i>One Year</i>
Bonds payable	\$ 27,790,000	\$ -	\$ (3,845,000)	\$ 23,945,000	\$ 3,910,000
Unamortized loss on refunding	(146,030)	39,827	-	(106,203)	-
Unamortized premiums	992,728	(206,857)	-	785,871	-
Other long-term debt	1,817,133	266,400	(996,566)	1,086,967	995,385
	<u>\$ 30,453,831</u>	<u>\$ 99,370</u>	<u>\$ (4,841,566)</u>	<u>\$ 25,711,635</u>	<u>\$ 4,905,385</u>

	<i>Balance</i> <i>July 1, 2009</i>	<i>Additions/</i> <i>Amortization</i>	<i>Payments/</i> <i>Maturities</i>	<i>Balance</i> <i>June 30, 2010</i>	<i>Amounts Due</i> <i>Within</i> <i>One Year</i>
Bonds payable	\$ 33,120,000	\$ -	\$ (5,330,000)	\$ 27,790,000	\$ 3,845,000
Unamortized loss on refunding	(185,856)	39,826	-	(146,030)	-
Unamortized premiums	1,199,585	(206,857)	-	992,728	-
Other long-term debt	3,510,818	-	(1,693,685)	1,817,133	782,180
	<u>\$ 37,644,547</u>	<u>\$ (167,031)</u>	<u>\$ (7,023,685)</u>	<u>\$ 30,453,831</u>	<u>\$ 4,627,180</u>

NOTE G--EMPLOYEE BENEFIT PLANS

Defined Benefit Plan: Prior to May 1, 1997, all employees of the Hospital were eligible to participate in the Maury Regional Hospital Retirement Plan (the Plan), a single-employer public retirement system (PERS), accounted for as a separate entity from the Hospital. The purpose of the Plan is to provide retirement, death, and certain other benefits to employees as specified in the Plan.

The actuarial method generally employed to determine contributions to the Plan is the entry age normal actuarial cost method. Although it has not expressed any intention to do so, the Hospital has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions set forth in ERISA.

The Plan was amended effective May 1, 1997 to stop accrual of benefit service on April 30, 1997 for participants who made an irrevocable election to participate in the Maury Regional Healthcare System 403(b) Plan on May 1, 1997. As of May 1, 2011, 127 participants are earning future service accruals. Employees hired after May 1, 1997, are not eligible to participate in the Plan.

Defined Benefit Plan Funding Policy: Voluntary contributions may not be made by participants. The Hospital's contributions are based on an actuarially determined rate. The Hospital's annual

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE G--EMPLOYEE BENEFIT PLANS - Continued

pension cost for 2011 was \$752,987. The Hospital's net pension obligation to the Plan for 2011 and 2010 was zero. The annual required contribution for the current year was determined as part of the May 1, 2010, actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions used included the following:

- 8.00% investment rate of return
- projected salary increases ranging from 4.0% to 7.5% per year
- amortization method - level dollar amount

Three-Year Trend Information

<i>Fiscal Year</i>	<i>Annual Required Contribution</i>	<i>Percentage Contributed</i>	<i>Pension Obligation</i>
April 30, 2009	\$ -	100.00%	\$ -
April 30, 2010	785,010	100.00%	-
April 30, 2011	752,987	100.00%	-

A schedule of funding progress for the Plan follows:

<i>Actuarial Valuation Date</i>	<i>Actuarial Value of Assets (a)</i>	<i>Actuarial Accrued Liability (AAL) (b)</i>	<i>Unfunded AAL (UAAL) (b-a)</i>	<i>Funded Ratio (a/b)</i>	<i>Covered Payroll (c)</i>	<i>UAAL as a % of Covered Payroll (b-a)/c</i>
May 1, 2009*	38,788,798	42,379,105	\$ 3,590,307	91.5%	6,225,197	57.7%
May 1, 2010*	39,793,024	43,271,426	3,478,402	92.0%	5,423,206	64.1%
May 1, 2011*	40,609,452	43,936,214	3,326,762	92.4%	5,061,006	65.7%

*Entry age normal actuarial method utilized for determining the unfunded actuarial liability.

The unfunded actuarial accrued liability is being amortized as a level percentage of covered payroll over 30 years beginning in fiscal 2009.

Defined Contribution Plan: Effective May 1, 1997, the Hospital implemented a defined contribution plan which includes a 403(b) feature and an employer matching provision and covers substantially all hourly and salaried employees. Voluntary contributions may be made by the participants as a percentage of annual compensation not to exceed Internal Revenue Service limits. The Hospital's

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE G--EMPLOYEE BENEFIT PLANS - Continued

contribution consists of a base contribution of 3% of annual covered compensation and a matching contribution equal to 50% of the employees' first 5% of annual compensation contributed. The Hospital's total contributions for the years ended June 30, 2011 and 2010 amounted to approximately \$3,930,000 and \$3,480,000, respectively.

NOTE H--LEASES

Capital Leases: The Hospital leases medical equipment under various capital lease agreements with interest rates ranging from 4.70% to 15.7%. A summary of the leased equipment, which is included in property, plant and equipment, at June 30 is as follows:

	<u>2011</u>	<u>2010</u>
Equipment acquired under capital leases	\$ 2,169,151	\$ 3,145,576
Less accumulated amortization	(1,851,470)	(2,423,938)
	<u>\$ 317,681</u>	<u>\$ 721,638</u>

The following is a schedule of the future minimum lease payments required under capital leases as of June 30, 2011:

<u>Year Ending June 30,</u>	
2012	\$ 260,442
2013	74,000
Total minimum lease payments	334,442
Amount representing interest	(3,291)
Present value of minimum lease payments	<u>\$ 331,151</u>

Operating Leases: The Hospital also rents office space and equipment under various non-cancelable operating lease agreements with varying terms. Rent expense under operating lease agreements totaled approximately \$4,230,000 and \$3,890,000 for the years ended June 30, 2011 and 2010, respectively. Future minimum lease commitments for all significant non-cancelable operating leases are as follows:

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE H--LEASES - Continued

<u>Year Ending June 30,</u>	
2012	\$ 2,078,055
2013	1,521,022
2014	1,054,259
2015	764,479
2016	302,379
Thereafter	-
	<u>\$ 5,720,194</u>

Leases with Physicians: The Hospital leases office space in its medical office buildings to physicians under non-cancelable operating leases with varying terms. Rental income under these lease agreements totaled approximately \$1,090,000 and \$1,190,000 for the years ended June 30, 2011 and 2010, respectively. Future minimum lease commitments to the Hospital for all significant non-cancelable operating leases are as follows:

<u>Year Ending June 30,</u>	
2012	\$ 963,880
2012	260,601
2013	262,543
	<u>\$ 1,487,024</u>

NOTE I--LEASED HEALTHCARE FACILITIES

Effective July 1, 2005, the Hospital entered into the first of two 5-year renewal options provided under a lease arrangement with the Board of Trustees of Wayne County General Hospital for the operation of several Wayne County healthcare facilities, including the county hospital, nursing home, ambulance service and medical office buildings. The lease also extends to all equipment, improvements, fixtures and related personal property. The annual lease expense under the first renewal consisted of a base rent of \$175,000 and an annual capital improvement commitment of \$175,000. Effective July 1, 2010, the lease was amended to exclude the operations of the nursing home. The annual lease expense, as amended, is \$150,000 for the first year only and an annual capital improvement commitment of \$200,000. The amended lease provides for two five-year renewal options which occur automatically unless the Hospital provides notice of its intent to terminate the lease at least 180 days in advance.

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE J--COMMITMENTS AND CONTINGENCIES

General Liability Claims: The Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Hospital maintains commercial insurance coverage for each of those risks of loss. Management believes such coverage is sufficient to preclude any significant losses to the Hospital.

Malpractice Liability Claims: The Hospital is subject to claims and suits arising in the ordinary course of business from services provided to patients. Losses against the Hospital are limited by the Tennessee Governmental Tort Liability Act to \$350,000 for injury or death per person and \$700,000 per occurrence. However, claims against healthcare practitioners are not subject to these limits. The Hospital maintains professional liability insurance on a claims made basis with limits of \$1,000,000 per occurrence with a retention of \$250,000 per claim and a \$3,000,000 annual aggregate with a \$750,000 annual aggregate retention. The Hospital has estimated and recorded a liability for reported claims totaling approximately \$950,000 and \$1,290,000 at June 30, 2011 and 2010, respectively. In management's opinion, the Hospital is currently not a party to any proceeding, the ultimate resolution of which will have a material adverse effect on the Hospital's results of operations or financial condition. The Hospital has not estimated any liability for incurred but not reported claims.

Workers' Compensation Claims: The Hospital is covered for workers' compensation claims through an insurance policy with a deductible of \$500,000 per claim. Management has recorded an accrual for the estimated liability related to claims reported as of June 30, 2011 and 2010. The Hospital has not estimated any liability for incurred but not reported claims.

Healthcare Benefits: The Hospital maintains a partially self-insured healthcare plan to provide reimbursement for covered expenses incurred as a result of illness or injury to covered employees and dependents. Stop-loss insurance is purchased for annual claims per individual exceeding \$250,000 in both 2011 and 2010 with a life time maximum per individual totaling \$750,000. The Hospital has estimated and recorded a liability for healthcare claims incurred but not yet reported totaling approximately \$1,640,000 at both June 30, 2011 and 2010. Employees that retire after attaining age sixty and completing twenty years of service will receive continued coverage under the Hospital's health benefit program until they attain age sixty-five or become eligible for Medicare benefits. The estimated amount of retirement health benefits payable totaled approximately \$270,000 and \$300,000 at June 30, 2011 and 2010, respectively, and is reported as a noncurrent liability in the combined financial statements. Due to uncertainties in the estimate, it is at least reasonably possible that management's estimate could change in 2012.

Healthcare Industry: The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements,

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE J--COMMITMENTS AND CONTINGENCIES - Continued

reimbursement for patient services, Medicare fraud and abuse and under the provisions of the Health Insurance Portability and Accountability Act of 1996, patient records privacy and security. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers, such as the Medicare Recovery Audit Contractor Program. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. Management believes that any amounts payable related to audits through the Medicare Recovery Audit Contractor program, or similar initiatives, have been estimated and recorded as Other Long-term Liabilities in the combined financial statements and therefore, any additional impact on the combined financial statements will not be significant. However, due to the uncertainties involved, management's estimate could change in the near future.

Healthcare Reform: In March 2010, Congress adopted comprehensive health care insurance legislation, the Patient Care Protection and Affordable Care Act and the Health Care and Education Reconciliation Act. The legislation, among other matters, is designed to expand access to health care coverage to substantially all citizens by 2019 through a combination of public program expansion and private industry health insurance. Changes to existing TennCare coverage and payments are also expected to occur as a result of this legislation. Implementing regulations are generally required as a result of such legislation over a period of several years. Accordingly, the impact of any future regulations is not determinable.

NOTE K--FAIR VALUE OF FINANCIAL INSTRUMENTS

Management believes that carrying value approximates fair value for the majority of the Hospital's financial assets and liabilities. The estimated fair value of bonds payable, which are general obligation bonds of Maury County, is \$24,510,471 and \$28,355,473 at June 30, 2011 and 2010, respectively.

Generally accepted accounting principles establish a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

MAURY REGIONAL HOSPITAL

Notes to Combined Financial Statements - Continued

Years Ended June 30, 2011 and 2010

NOTE K--FAIR VALUE OF FINANCIAL INSTRUMENTS - Continued

- Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Hospital's investments are reported at fair value on a recurring basis based on Level 1 inputs at June 30, 2011.

Other Information



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

To the Board of Trustees of
Maury Regional Hospital:

We have audited the combined financial statements of Maury Regional Hospital (the Hospital) as of and for the years ended June 30, 2011 and 2010, and have issued our report thereon dated October 12, 2011. 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.

Internal Control Over Financial Reporting

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

A deficiency in internal control 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 and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hospital's combined financial statements are free of material misstatement we performed tests of its compliance with certain

provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of combined financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits 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 and the Board of Trustees in a separate letter dated October 12, 2011.

This report is intended solely for the information and use of the Board of Trustees, management and the Comptroller of the Treasury, Department of Audit of the State of Tennessee, and is not intended to be and should not be used by anyone other than these specified parties.

Peeling Yonky: Account PC

Knoxville, Tennessee
October 12, 2011