HENRY COUNTY MEDICAL CENTER
(a component unit of Henry County)

Financial Statements and Supplemental Schedules

June 30, 2012 and 2011

(With Independent Auditors' Report Thereon)

LATTIMORE BLACK MORGAN & CAIN, PC
CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

HENRY COUNTY MEDICAL CENTER
(a component unit of Henry County)

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INDEPENDENT AUDITORS' REPORT

**The Board of Trustees
Henry County Medical Center
Paris, Tennessee:**

We have audited the accompanying statements of net assets of Henry County Medical Center (Medical Center), a component unit of Henry County, Tennessee, as of June 30, 2012 and 2011, and the related statements of revenue, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Medical Center's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 and opinion on the effectiveness of the Medical Center's internal control 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 financial statements. An audit also includes assessing the accounting principles used and the 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 previously present fairly, in all material respects, the financial position of Henry County Medical Center as of June 30, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 17, 2012 on our consideration of the Medical Center'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 control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our 2012 audit.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplemental schedules are fairly stated in all material respects in relation to the basic financial statements as a whole.

Accounting principles generally accepted in the United States of America require that management's discussion and analysis and budgetary comparison information on pages 3-14 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Lattimore Black Morgan & Cain, PC

Brentwood, Tennessee
September 17, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

As management of Henry County Medical Center (HCMC), we offer readers of the financial statements this narrative overview and analysis of the financial performance during the years ended June 30, 2012, 2011, and 2010. The budget for year ended 2012 is also included for comparative review. Please read this analysis in conjunction with the financial statements.

STATISTICAL HIGHLIGHTS

Table 1 below is a comparative analysis of statistics. While we continue to see growth and stability in observations, surgeries, emergency visits, and outpatient visits, we also see a continued decline in hospital admissions, Healthcare Center (HCHC) average daily census, and Agency (EMS) runs. Statistics for the budget are based on the prior year with growth factors for physician recruiting and marketing initiatives.

Table 1

Statistics

					FYE 2012 vs.		
	FYE	FYE	FYE	FYE		FYE	FYE
Hospital	2012	Budget	2011	2010	Budget	2011	2010
Admissions	3,717	3,892	3,828	4,180	-4%	-3%	-11%
Average Daily Census	45	46	46	51	-2%	-2%	-12%
Observations	2,005	1,732	1,698	1,906	16%	18%	5%
Surgeries	6,159	5,397	5,073	5,266	14%	21%	17%
Emergency Visits	18,493	17,995	17,988	17,657	3%	3%	5%
Outpatient Visits	54,674	53,000	54,526	53,361	3%	0%	2%
Healthcare Center - ADC	127	131	130	142	-3%	-2%	-11%
EMS Agency – Runs	5,499	5,739	5,648	5,588	-4%	-3%	-2%
Total Patients in a Bed (Admits + Observations)	5,722	5,624	5,526	6,086	2%	4%	-6%

A review of the above statistics shows that admissions, average daily censuses for both the hospital and HCHC, and EMS runs experienced declines during the previous years, and were also under budget. This is a result of current economic conditions, unemployment, and changes in insurance policy, thereby driving more patients to treatments in the outpatient setting delivered through hospital outpatient services, physician in-office treatments, home health, and other at home treatments. The insurance policy driving short stay inpatients into outpatient observation stays is an example of such treatment change. Our outpatient observations show year over year growth of 18% and 5% respectively, with a 16% increase compared to the FYE 2012 Budget. These are patients in the hospital for one to three days, classified as outpatient, and not included in our average daily census. The Total Patients in a Bed statistic shows a growth rate of 4% over prior year and 2% over budget. Second to the impacts from above, our psychiatric service line was under budget by 4% while we recruited a psychiatrist. Our psychiatric service line ran an average daily census of 8 versus the prior year and budgeted census of 10. The FYE 2010 census was 9.

Surgeries show a significant increase year over year and in budget. During the fiscal year, HCMC purchased a local surgery center. The purchase has allowed HCMC to recapture market share, gain economies of scale, to position ourselves in collaboration versus competition, and begin preparing for health reform.

Observations, emergency visits and outpatient visits, trend above prior years and the budget. Changes in technology and insurance policy continue to drive growth in outpatient procedures and testing. Thirdly, patients continue to experience loss of insurance and therefore push off medical needs and ultimately land in the emergency room. As stated above, patients are seeking medical attention in more of an outpatient setting.

The aging of the population in the service area of HCMC promotes gradual growth for the hospital. Recruiting efforts are on-going and key to growth. Two physicians were brought to the area. Their practices have started and are moving forward with attracting patient visits. Marketing initiatives are also key to growth. Our hospital is accredited by Joint Commission, our home health is listed in the top twenty-five percent of agencies in the nation for quality of care, quality improvement, and financial performance, and our healthcare center is a four star facility. Marketing literature and media includes the above and highlights many services offered in our service area.

FINANCIAL HIGHLIGHTS

Table 2

Consolidated Financial Highlights (000s)

	FYE 2012	FYE Budget	FYE 2011	FYE 2010	FYE 2012 vs. FYE Budget	FYE 2012 vs. FYE 2011	FYE 2012 vs. FYE 2010
Operating Revenues	71,662	69,977	67,498	66,980	2%	6%	7%
Operating Expenses	71,433	69,272	67,535	66,161	3%	6%	8%
Non-operating Income	58	225	270	249	-74%	-79%	-77%
Net Income (loss)	287	930	233	1,068	-69%	23%	-73%

1) Consolidated Operating Revenues show increases over budget and prior years. An increase of 2% compared to the Budget, an increase of 6% compared to FYE 2011 and an increase of 7% compared to FYE 2010 are stated above. The increase in operating revenues is due to the purchase of a surgery center, growth in outpatient services, payment for Meaningful Use Phase I of the Electronic Health Record, efficiencies gained thorough documentation improvement projects, and payment from the Center for Medicare and Medicaid Services for correction in budget neutrality calculations on past cost report. Netted against the increase in operating revenues is an increase in insurance adjustments from insurance policy changes, and an increase in bad debts from patients' inability to pay for services.

2) Consolidated Operating Expenses also show increases over budget and prior years. The increase is 3%, 6%, and 8%, respectively. The primary increase in operating expenses is attributed to increases in salaries and wages, employee benefits, and supplies. A detail review of expenses is included with Table 4.

3) Non-operating income decreased compared to budget and prior years due to usage of funds and lower interest rates.

4) Consolidated Net Income has been a positive net income for all fiscal year ends. However, consolidated Net Income was 69% less than budget, 23% more than FYE 2011, and 73% less than FYE 2010. The hospital's net income was $1,120,000 in FYE 2012, $522,000 in FYE 2011, which is an increase of 115%. The healthcare center's income was a loss of $466,000 in FYE 2012 versus a FYE 2011 net income of $149,000 which is a 413% decrease. The EMS Agency's net loss was ($368,000) in FYE 2012 versus a net loss of ($437,000) in FYE 2011, which is a 16% decrease in the loss.

USING THIS REPORT

The financial statements consist of three statements

- A Statement of Net Assets, a Statement of Revenue, Expenses and Changes in Net Assets, and a Statement of Cash Flows.

STATEMENTS OF NET ASSETS AND STATEMENTS OF REVENUE, EXPENSES, AND CHANGES IN NET ASSETS

Our analysis of the financial statements will follow and we will answer with this analysis "Is Henry County Medical Center in a better financial position or a worse financial position as a result of this year's activities?" The Statement of Net Assets and Statement of Revenues, Expenses, and Changes in Net Assets, will provide information that will answer this question.

The two statements reflect the net assets and the changes in such. Net assets are defined as the differences between assets and liabilities and are used as a measure of the financial health of our facilities. Over time, increases and decreases in the net assets is one of the indicators as to whether we are improving or deteriorating. Financial profits create directly proportional increases in net assets where financial losses cause equal decrease in net assets.

THE STATEMENT OF CASH FLOWS

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

HCMC'S NET ASSETS

The net assets are the difference between assets and liabilities reported in the Statement of Net Assets on page 15 and Table 3 below. The net assets increased by $287,000 or by 1% in FYE 2012 versus an increase of 0.4% or $233,000 in FYE 2011. This increase indicates a greater growth in assets than liabilities in the facilities. Table 3 below reflects the balance of assets, liabilities, and net assets as of FYE 2012, 2011 and FYE 2010. It is important to note that strengthening of net asset balances and financial health is directly driven by the financial profits from operations as well as the investments of and in assets.

Table 3

Consolidated Statements of Net Assets (000s)

	FYE 2012	FYE 2011	FYE 2010
Assets:			
Current Assets	$18,234	$14,333	$14,692
Net Property & Equipment	42,496	42,153	37,129
Long Term Investments	7,228	7,769	7,604
Assets Limited to Use	10,279	13,759	14,219
Goodwill and Other Intangible Assets	5,141	0	0
Other Assets	1,312	1,071	955
Total Assets	$84,690	$79,085	$74,599
Liabilities:			
Current Liabilities	$ 7,311	$ 7,238	$ 7,666
Long-Term Debt	23,543	17,890	13,418
Other Long-Term Liabilities	0	408	199
Total Liabilities	$30,854	$25,536	$21,283
Net Assets:			
Investment in Capital Assets Net of Debt	$17,497	$22,802	$22,658
Unrestricted Net Assets	36,339	30,747	30,658
Total Net Assets	$53,836	$53,549	$53,316

The increase in net assets in FYE 2012 can be seen above as increases in current assets, net property and equipment, goodwill and other intangible assets, and other assets. These increases account for most of the growth in operations for FYE 2012. The majority of these increases are related to the purchase of the surgery center and posting a receivable for the Meaningful Use Stage 2 of the Electronic Health Record. The purchase of the surgery center increased accounts receivables in current assets, increased goodwill and other intangible assets, and increased long term debt for borrowing funds for the purchase. Net property plant and equipment increases were a result of hospital investment in infrastructure and equipment. Meaningful Use Stage 2 standards for the Electronic Health Record were met in April 2012. Payment was received in July 2012.

OPERATING INCOME

The Statement of Revenue, Expenses, and Changes in Net Assets on page 16 and Table 4 below reflect the operating results for FYE 2012 and FYE 2011 and FYE 2010.

TABLE 4
Statements of Revenue and Expenses (000s)

	FYE 2012	FYE 2011	FYE 2010
Operating revenues			
Net patient service revenue	$68,484	$66,312	$65,557
Other revenue	3,178	1,186	1,423
Total operating revenue	$71,662	$67,498	$66,980
Operating expenses:			
Salaries and benefits	$39,666	$38,235	$37,806
Medical Supplies and Drugs	15,180	13,912	14,041
Depreciation and amortization	4,962	4,748	4,694
Other operating expense	11,625	10,640	9,620
Total Operating Expenses	$71,433	$67,535	$66,161
Operating Income (Loss)	$ 229	$ (37)	$ 819
Non Operating Income-Investments	58	270	249
Excess of Revenue over Expenses	$ 287	$ 233	$ 1,068

As noted above, we realized an increase of $54,000 or 23% in excess revenues over expenses for FYE 2012 over FYE 2011. This is a $781,000 or 73% decrease compared to FYE 2010. Operating revenue increased 6% and total operating expenses increased 6% compared to FYE 2011. The variances for FYE 2012 are explained in the following paragraphs.

Net Patient Service revenues increased only $2,172,000 or 3% during FYE 2012. The increase in net patient service revenue is attributed to the purchase of a surgery center, increase in patient service volumes from outpatient activity at the hospital, service line improvements of efficiencies with documentation, and changes in estimates for cost report settlements. This increase was balanced with declines in admissions, insurance reimbursement changes, and write-off increases related to charity and bad debts. Bad Debt expenses (recorded as a reduction to net patient service revenue) increased $341,000 during FYE 2012 or 5% over prior year. Bad Debt expense as a percent of gross patient service revenue is 3.6% in FYE 2012 compared to 3.9% in FYE 2011 and 3.7% in FYE 2010. The stagnation of the economy has impacted collections of co-pays, deductibles, and services. The overall increase to net patient service revenues was a healthy 3%.

Other revenue increased by $1,992,000 or 168% in FYE 2012. The hospital met Meaningful Use Stage 1 standards for the Electronic Health Record. Incentive payments are made as multiple stages are met.

Salary and benefits costs increased $1,431,000 or 4% in FYE 2012. Salary increases of $505,000 were the net increase over prior year. This is the net increase of 2% in salaries coupled with a slight decrease in full time equivalent employees. The 2% salary increase was given to remain competitive with employment initiatives. The remaining increase of $926,000 is related to claims experiences with our health insurance and workers compensation programs. Costs for health insurance claims increased 12%, while workers compensation claims increased 149%.

Medical supply and drug expense increased $1,268,000 or 9% in FYE 2012. Medical supplies and drug expense as a percentage to total operating revenues is 21% for all three fiscal years. Medical supply and drug expense is related to increases in usage of supplies as well as increases in cost of supplies. HCMC purchased a surgery center during the year which increased supply costs by $309,000. Management continues to review cost control measures and implementation of cost saving programs through our group purchasing organization.

Depreciation and amortization costs increased $214,000 or 5% during FYE 2012 as a result of continuing investment in the facility and equipment. Investment in capital was $5,166,000 for FYE 2012, $9,790,000 for FYE 2011, and $2,358,000 for FYE 2010. FYE 2012 includes replacement of many equipment items plus the purchase of a daVinci Robot for $1,210,000. FYE 2011 includes a central energy plant expansion of $7,430,000.

Other operating expenses increased $985,000 or 9% during FYE 2012. Various expense items increased over the year. Other professional fees increased $399,000 or 14% due to costs associated with consulting and legal fees for the purchase of the surgery center, fees associated with a new hyperbaric oxygen treatment service line, and increased staffing costs for the hospitalist program. Leases and rentals increased $266,000 or 23% due to the building lease for the surgery center and an extended and upgraded MRI equipment lease which increased capacity to two machines. Physician fees increased $232,000 or 45% from increases in on-call payments for emergency call pay for physicians. Repairs and maintenance increased $167,000 or 8% due to increased maintenance contracts for computerization. Other general expenses which include marketing, dues, travel, and education decreased $99,000 or by 6% due to efforts to reduce expenses.

In summary, Henry County Medical Center provided a consolidated net income of $287,000 while managing volatility in volumes and controlling expenses.

Non-operating income or investment income decreased $212,000 or 79% during FYE 2012. Usage of cash and investments, coupled with a downturn in rates, led to a decrease in investment income.

We continue to be fortunate to have assets to invest in physician recruiting and growing programs through marketing initiatives for our service area. We continue to work to improve services and productivity, to contain costs and to promote growth and efficiencies.

Due to ongoing pressure in our economy and reimbursement rates, and due to increased costs associated with pharmacy, implantable devices, and increased capital investment for technology and expansion, we expect to be challenged. We feel that it is imperative to continue to invest in growth and marketing and that we closely manage our controllable costs in order to improve our level of profitability.

Our plan in future years is to build profit from our assets and operations so that we can meet the requirements that stem from the growing healthcare needs of the patient population that we serve.

HCMC CASH FLOW

The Statement of Cash Flows on page 17 provides information regarding the sources and uses of cash during FYE 2012 and FYE 2011. Henry County Medical Center saw an increase in cash flow in FYE 2012 of $130,000. This is the result of our investments in physician recruiting, our staff, and our property improvements, plus the generation of cash flow from operating activities.

The net cash provided by operations was $651,000 in FYE 2012 versus $2,062,000 in FYE 2011 and $6,763,000 in FYE 2010. Net cash provided (used) by capital and financing activities were $407,000 in FYE 2012 versus ($4,964,000) in FYE 2011 and ($3,391,000) in FYE 2010. Net cash provided or (used) by investing activities were ($928,000) in FYE 2012 versus $536,000 in FYE 2011 and ($2,942,000) in FYE 2010. For FYE 2012, HCMC used the majority of the cash in the manner as stated in Table 5 below, which yielded a net increase in cash of $130,000. The table below shows highlights of uses of cash over FYE 2012, FYE 2011, and FYE 2010.

Table 5

Consolidated Statement of Cash Flows Highlights (000s)

	FYE 2012	FYE 2011	FYE 2010
Proceeds from Debt	$7,000	$6,000	$ -
Principal Payment on debt	$1,456	$1,121	$ 976
Property and Equipment Purchases	$5,166	$9,790	$2,358
Investment Activities	($ 928)	$ 536	($2,942)
Increase (Decrease) in Cash and Cash Equivalents	$ 130	($2,366)	$ 430

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets:

At the end of FYE 2012, Henry County Medical Center had invested $42,496,000 in capital assets net of depreciation. This represents a 1% increase over the FYE 2011 amount of $42,153,000 and a 14% increase over the FYE 2010 amount of $37,129,000. Increases are due to funding plant expansion, government required computerization and various equipment. The summary of Capital Assets can be found in note 5 on pages 26-27.

Debt:

At the end of FYE 2012, Henry County Medical Center has $24,999,000 in long-term debt, including the current portion. This is an increase over the FYE 2011 long-term debt balance of $19,351,000. This increase is the net result of an additional $7,000,000 loan for the purchase of a surgery center and a daVinci Robot, and net of payments of debt of $1,456,000. The FYE 2010 balance of long term debt was $14,471,000. The summary of long-term debt is in note 7 of the financial statements on pages 27-29.

OTHER ECONOMIC FACTORS

FYE 2012, FYE 2011, and FYE 2010 continue with results from unstable economic conditions. The local area is impacted by the changes in insurance policy, the rising cost of recruiting physicians, and the rising cost of materials like drugs, implants, fuel and energy. The changes in insurance policy impacts patients spending abilities and the differing of health care needs.

We as a community healthcare provider strive to help recruit industry and attract retirement ventures to the area by continuing to offer quality healthcare at an affordable price.

CONTRACTING HCMC'S FINANCIAL MANAGEMENT

This financial report is designed to provide our patients, suppliers, and creditors with a general overview of HCMC finances and to show good stewardship of the resources we possess. If you have any questions regarding this report contact Henry County Medical Center's Chief Financial Officer, at Henry County Medical Center, 301 Tyson Avenue, P.O. Box 1030, Paris, TN 38242.

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HENRY COUNTY MEDICAL CENTER
(a component unit of Henry County)

Statements of Net Assets

June 30, 2012 and 2011

Assets

	2012	2011
Current assets:		
Cash and cash equivalents	$ 948,280	$ 817,943
Assets limited as to use and that are required for current liabilities	1,456,181	1,460,610
Patient accounts receivable, less allowance for uncollectible accounts of $9,823,000 and $8,402,000 in 2012 and 2011, respectively	10,727,902	9,305,437
Other receivable	1,543,634	-
Inventories	2,111,494	1,772,575
Prepaid expenses and other current assets	775,416	373,331
Estimated third-party payor settlements	671,438	602,883
Total current assets	18,234,345	14,332,779
Property and equipment, net	42,495,732	42,152,932
Long-term investments	7,227,537	7,768,993
Assets limited as to use, excluding assets required for current liabilities	10,279,199	13,758,636
Goodwill and other intangible assets	5,141,270	-
Other assets	1,312,003	1,071,889
	$ 84,690,086	$ 79,085,229

Liabilities and Net Assets

	2012	2011
Current liabilities:		
Current portion of long-term debt	$ 1,456,181	$ 1,460,610
Accounts payable	2,000,418	1,946,639
Accrued expenses	3,854,981	3,830,669
Total current liabilities	7,311,580	7,237,918
Long-term debt, excluding current portion	23,542,638	17,889,918
Other long-term liabilities	-	408,555
Total liabilities	30,854,218	25,536,391
Net assets:		
Unrestricted:		
Invested in capital assets, net of related debt	17,496,913	22,802,404
Unrestricted net assets	36,338,955	30,746,434
Total unrestricted net assets	53,835,868	53,548,838
	$ 84,690,086	$ 79,085,229

See accompanying notes to the financial statements.

HENRY COUNTY MEDICAL CENTER
(a component unit of Henry County)

Statements of Revenue, Expenses and Changes in Net Assets

Years ended June 30, 2012 and 2011

	2012	2011
Operating revenue:		
Patient service revenue, net of provision for bad debts of $7,152,486 and $6,811,963 in 2012 and 2011, respectively	$ 68,483,644	$ 66,311,572
Other revenue	3,178,328	1,186,565
Total operating revenue	71,661,972	67,498,137
Expenses:		
Salaries and wages	29,847,792	29,342,675
Employee benefits	9,818,474	8,891,876
Supplies	15,179,740	13,912,356
Professional fees	3,252,733	2,850,704
Physician fees	747,511	515,424
Utilities and telephone	1,565,135	1,505,207
Repairs and maintenance	2,235,662	2,074,027
Leases and rentals	1,438,452	1,172,873
Insurance	468,845	430,515
Interest expense	35,817	87,985
Depreciation and amortization	4,962,162	4,747,589
Other expenses	1,542,350	1,617,040
Services tax	338,200	387,148
Total expenses	71,432,873	67,535,419
Operating income (loss)	229,099	(37,282)
Nonoperating income - investment income	57,931	270,432
Excess of revenue over expenses	287,030	233,150
Net assets at beginning of year	53,548,838	53,315,688
Net assets at end of year	$ 53,835,868	$ 53,548,838

See accompanying notes to the financial statements.

HENRY COUNTY MEDICAL CENTER
(a component unit of Henry County)

Statements of Cash Flows

Years ended June 30, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Receipts from and on behalf of patients	$ 65,556,350	$ 64,509,903
Payments to suppliers and employees	(66,061,290)	(61,553,045)
Other receipts and payments, net	1,156,174	(894,931)
Net cash provided by operating activities	651,234	2,061,927
Cash flows from capital and related financing activities:		
Proceeds from long-term debt	7,000,000	6,000,000
Principal paid on long-term debt	(1,455,513)	(1,120,722)
Interest paid on long-term debt	(35,817)	(87,985)
Proceeds from disposal of property and equipment	63,695	34,406
Purchases of property and equipment	(5,165,615)	(9,790,168)
Net cash provided (used) by capital and related financing activities	406,750	(4,964,469)
Cash flows from investing activities:		
Distributions from joint venture	675,000	437,500
Proceeds from (purchases) of investments	514,752	(153,689)
(Increase) decrease in assets limited as to use	3,483,866	(18,105)
Investment income	57,931	270,432
Purchase of Kentucky Lake Surgery Center, LLC (see Note 1(b)), net of cash acquired	(5,659,196)	-
Net cash provided (used) by investing activities	(927,647)	536,138
Increase (decrease) in cash and cash equivalents	130,337	(2,366,404)
Cash and cash equivalents at beginning of year	817,943	3,184,347
Cash and cash equivalents at end of year	$ 948,280	$ 817,943
Reconciliation of operating income (loss) to net cash provided by operating activities:		
Operating income (loss)	$ 229,099	$ (37,282)
Adjustments to reconcile changes in net assets to cash provided by operating activities:		
Depreciation and amortization	4,962,162	4,747,589
Provision for bad debts	7,152,486	6,811,963
(Gain) loss on disposal of property and equipment	168,492	(15,763)
Equity in earnings of joint venture	(648,296)	(448,693)
Interest paid on debt	35,817	87,985
(Increase) decrease in operating assets, net of the effects of acquisition (see Note 1(b)):		
Patient accounts receivable and other receivables	(10,011,225)	(7,800,822)
Estimated third-party payor settlements	(68,555)	(812,810)
Inventories	(198,604)	75,856
Prepaid expenses and other current assets	(399,564)	(13,163)
Other assets	(240,114)	(116,381)
Increase (decrease) in operating liabilities, net of the effects of acquisition (see Note 1(b)):		
Accounts payable	53,779	133,509
Accrued expenses	24,312	(759,308)
Other long-term liabilities	(408,555)	209,247
Net cash provided by operating activities	$ 651,234	$ 2,061,927
Supplemental schedule of noncash investing, capital and financing activities:		
Capital lease obligation for equipment	$ 103,804	$ -

See accompanying notes to the financial statements.

(1) Nature of operations

(a) Organization

Henry County Medical Center (Medical Center) is a political subdivision of Henry County, Tennessee (County). The Medical Center provides comprehensive health care services through the operation of an acute care hospital (Hospital), nursing home (Healthcare Center), home health agency (HHA), and emergency medical services agency (EMS). It is governed by a Board of Trustees under the authority of the County Commission of Henry County, Tennessee and the Henry County Hospital District. The Board of County Commissioners appoints the Board of Trustees of the Medical Center which may not issue debt without the County's approval. Under accounting principles generally accepted in the United States of America, the Medical Center constitutes a component unit of the County for financial reporting purposes.

(b) Acquisition

On December 30, 2011, the Medical Center acquired certain assets of Kentucky Lake Surgery Center, LLC (Center) for $5,800,000. The purchase price was funded through the issuance of debt (see Note 7). The Medical Center incurred various transaction expenses approximating $72,000 which are included in operating expenses on the accompanying statement of revenue, expenses and changes in net assets. This transaction has been accounted for as an acquisition and, accordingly, the acquisition price was allocated to the assets acquired based upon the fair value of the assets at the date of acquisition. No liabilities were assumed in the transaction. The acquisition resulted in excess costs over the fair value of the assets acquired, which is recorded as goodwill and other intangible assets in the accompanying statement of net assets. The intangible assets included a certificate of need (CON) and non-compete agreements. The non-compete will be amortized over 7 years which is the term of the agreements. The acquisition was allocated as follows:

Cash	$ 140,804
Patient receivables	$ 107,360
Inventories	$ 140,315
Prepaid expenses	$ 2,521
Property and equipment	$ 230,743
Goodwill and other intangible assets	$ 5,178,257

(2) Summary of significant accounting policies

(a) Basis of presentation

The Medical Center utilizes the proprietary fund method of accounting whereby revenues and expenses are recognized on the accrual basis. 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) and predecessor standard setting organizations, including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

(b) Inventories

Inventories are stated at the lower of cost, determined on the first-in, first-out (FIFO) basis, or market (net realizable value).

(c) Assets limited as to use

Assets limited as to use include cash and cash equivalents designated by the Board of Trustees for future capital improvements and debt repayment, over which the Board retains control and may at its discretion use for other purposes. Investments are reported at fair value.

(d) Cash, cash equivalents and investments

For the purpose of the statement of cash flows, cash and cash equivalents are defined as cash on hand or in banks and investments with original maturities at date of purchase of less than three months, excluding assets limited as to use.

Cash and cash equivalents include cash on hand and certificates of deposit, with original maturities of less than three months, with financial institutions. Investments consist of certificates of deposit with original maturities of greater than three months and certain mutual funds. Those investments with original maturities greater than three months but less than one year are classified as short-term investments, while the remaining amount is classified as long-term. Amounts included in the balance sheet caption "Assets limited as to use" consist of cash and cash equivalents. All of the Medical Center's cash and cash equivalents and certificates of deposit are insured or collateralized by securities held by the financial institutions' trust department in the Medical Center's name.

At June 30, 2012 and 2011, the total carrying value of the Medical Center's cash, cash equivalents and investments was $19,279,168 and $23,147,449, respectively, and the bank balance was $20,205,915 and $23,822,452, respectively. The entire financial institution balance as of June 30, 2012, was covered by federal depository insurance or by collateral held by the trustee in the Medical Center's name.

A fifty percent interest in a joint venture that provides cancer care services in the Henry County area is included in long-term investments on the accompanying balance sheet. This investment is accounted for under the equity method. The investment balance included in long-term investments is $632,029 and $658,733 at June 30, 2012 and 2011, respectively.

(e) Fair value measurements

Fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, fair value accounting standards establish a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity including quoted market prices in active markets for identical assets (Level 1), or significant other observable inputs (Level 2) and the reporting entity's own assumptions about market participant assumptions (Level 3). While a majority of the Medical Center's assets whose use is limited and investments are cash equivalents, the Medical Center has approximately $11,500,000 and $12,300,000 as of June 30, 2012 and 2011, respectively, in certificates of deposit that would be classified as Level 2 under the hierarchy above. The Medical Center does not have any fair value measurements using significant unobservable inputs (Level 3) as of June 30, 2012 or 2011.

(f) Property and equipment

Property and equipment acquisitions are recorded at cost. The Medical Center capitalizes purchases that cost a minimum of $500 and have a useful life greater than three years. Assets are depreciated on a straight-line basis over their estimated useful lives as follows: land improvements 5-20 years; buildings and improvements 5-40 years; fixed equipment 10-20 years; and major movable equipment 5-20 years.

(g) Goodwill and other intangible assets

Goodwill represents the excess of cost over the fair value of net assets acquired in business combinations recorded as purchases (see Note 1(b)). The Medical Center evaluates goodwill and other intangible assets for impairment on an annual basis or more frequently if impairment indicators arise. In the event goodwill and other intangible assets are considered to be impaired, a charge to earnings would be recorded during the period in which management makes such impairment assessment.

Other intangible assets consist of a certificate of need and non-compete agreements. The non-competes are amortized over their respective useful life on a straight-line basis.

(h) 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. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Patient service revenue is net of contractual adjustments and policy discounts of approximately $120,500,000 and $103,500,000 for the years ended June 30, 2012 and 2011, respectively. Approximately 61% and 54% of net patient service revenue was from Medicare for the years ended June 30, 2012 and 2011, respectively. Approximately 13% and 14% of net patient service revenue was from Medicaid/TennCare for the years ended June 30, 2012 and 2011, respectively.

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. These costs are estimated based on the ratio of total costs to gross charges and amounted to $1,022,829 and $1,268,128 for the years ended June 30, 2012 and 2011, respectively.

(i) Costs of borrowing

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

(j) Pension plan

Medical Center employees are covered under The Tennessee Consolidated Retirement System, a defined benefit plan. The Medical Center's costs are charged to expense and funded annually.

(k) Compensated absences

The Medical Center provides its full-time employees with paid days off for holiday, vacation, sick, and bereavement absences. The paid days off begin accruing after a three month probationary period and are based on the table which follows. Such days may be taken only after the employee has earned them. All earned days must be taken annually, except that an employee may carry forward up to the normal number of hours worked in a four-week period. Such liabilities have been accrued in the accompanying balance sheet.

Years of service	Days earned per year
0-5	20
5-10	25
10 or more	30

(l) Risk management

The Medical Center is exposed to various risks of loss from medical malpractice; torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; and natural disasters. Commercial insurance is purchased for claims arising from such matters. The Medical Center is self-insured for employee health and workers' compensation claims and judgments as discussed in Note 9.

(m) Net assets

All resources that are not restricted by donors are included in unrestricted net assets. Resources temporarily restricted by donors for specific purposes are reported as temporarily restricted net assets. When specific purposes are achieved, either through passage of a stipulated time or the purpose for restriction is accomplished, they are classified to unrestricted net assets and reported in the statement of revenues, expenses and changes in net assets. Resources temporarily restricted by donors for additions to land, building and equipment are initially reported as temporarily restricted net assets and are transferred to unrestricted net assets when expended. Donor-imposed restrictions which stipulate that the resources be maintained permanently are reported as permanently restricted net assets. Investment income for the permanently restricted net assets is classified as either temporarily restricted or unrestricted based on the intent of the donor. As of June 30, 2012 and 2011, there were no permanently or temporarily restricted net assets.

(n) Income taxes

The Medical Center is a not-for-profit corporation as described in Chapter 176 of the Private Acts and is exempt from federal income taxes pursuant to Section 115 of the Internal Revenue Code.

(o) Performance indicator

Excess of revenue over expenses (expenses over revenue) reflected in the accompanying statements of revenue, expenses and changes in net assets is a performance indicator.

(p) Long-lived assets

Management evaluates the recoverability of its investment in long-lived assets on an ongoing basis and recognizes any impairment in the year of determination. It is reasonably possible that relevant conditions could change in the near term and necessitate a change in management's estimate of the recoverability of these assets.

(q) 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.

(r) Reclassifications

Certain reclassifications have been made to the 2011 financial statements in order for them to conform to the 2012 presentation. These reclassifications have no effect on net assets or changes in net assets as previously reported.

(s) Events occurring after reporting date

The Medical Center has evaluated events and transactions that occurred between June 30, 2012 and September 17, 2012, which is the date the financial statements were available to be issued, for possible recognition or disclosure in the financial statements.

(3) Third-party reimbursement programs

The Medical Center receives revenue under various third-party reimbursement programs which include Medicare, TennCare, and other third-party payors. Contractual adjustments under third-party reimbursement programs represent the difference between the Medical Center's billings at its established rates and the amounts reimbursed by third-party payors. They also include any differences between estimated third-party reimbursement settlements for prior years and subsequent tentative or final settlements. The adjustments resulting from tentative or final settlements to estimated reimbursement amounts resulted in an increase to revenue of approximately $146,000 and $350,000 for the years ended June 30, 2012 and 2011, respectively.

(a) Medicare

The Medical Center is paid for substantially all services rendered to inpatient Medicare program beneficiaries under prospectively determined rates-per-discharge. Those rates vary according to a classification system that is based on clinical, diagnostic, and other factors. The Medical Center is paid for outpatient, emergency medical services and psychiatric services under a Medicare program known as the Ambulatory Payment Classification (APC) system. Under the APC system, outpatient services are classified into APC categories based on standard procedure codes (CPT-4 Codes) for the service provided and payment for the APC categories are determined using prospectively determined Federal payment rates adjusted for geographical area wage differences. The Medical Center receives cash payments at an interim rate with final settlement determined after the Medical Center's submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. The Medical Center's classification of patients under the Medicare Prospective Payment System and the appropriateness of the patients' admissions are subject to validation reviews by the Medicare peer review organization.

(b) Medicaid

The Medicaid program reimburses the healthcare center for the cost of services rendered to Medicaid beneficiaries at a prospective rate which is based on the lower of the reimbursable cost of services rendered or a reimbursement cap set by Medicaid. The reimbursement cap is expressed as a per diem.

(c) TennCare

The State of Tennessee TennCare program is a managed care program which provides healthcare coverage to those previously eligible for Medicaid as well as the uninsured population. The Hospital contracts with various managed care organizations (MCO's) which offer both Health Maintenance Organization (HMO) and Preferred Provider Organization (PPO) healthcare products. Reimbursement to the Medical Center is received through per diems, Diagnosis-Related Group (DRG) payments and discounted fee for service.

(d) Commercial Payors

The Medical Center has 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 and discounts from established rates.

(e) Credit Concentration

The Medical Center grants credit to patients and generally does not require collateral or other security in extending credit; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans or policies. At June 30, 2012 and 2011, the Medical Center had net receivables from the Federal Government (Medicare) of approximately $4,200,000 and $3,500,000, respectively, and from Medicaid/TennCare of approximately $1,200,000 and $750,000, respectively.

(f) Meaningful use payments from Medicare and Medicaid

The American Recovery and Reinvestment Act of 2009 (ARRA) established incentive payments under the Medicare and Medicaid programs for hospitals that implemented "meaningfully use" certified electronic health record (EHR) technology. In order to receive incentive payments, a hospital which is able to meet the meaningful use criteria must attest that during the EHR reporting period, the hospital used certified EHR technology and specify the technology used, satisfied the required meaningful use objectives and associated measures for the applicable stage, and must specify the EHR reporting period and provide the result of each applicable measure for all patients admitted to the inpatient or emergency department of the hospital during the EHR reporting period for which a selected measure is applicable. A hospital may receive an incentive payment for up to four years, provided it successfully demonstrates meaningful use of certified EHR technology for the EHR reporting period. Hospitals that adopt a certified EHR system and are meaningful users can begin receiving incentive payments in any federal fiscal year from 2011 (October 1, 2010 - September 30, 2011) to 2015; however, the incentive payments will decrease for hospitals that first start receiving payments in federal fiscal year 2014 or 2015.

The Medical Center met the meaningful use criteria during 2012. As a result, the Medical Center recognized income of approximately $400,000 and $1,540,000 from Medicaid and Medicare, respectively, in 2012. The Medical Center received the $400,000 from Medicaid during 2012 and has a receivable of approximately $1,540,000 from Medicare related to the meaningful use incentive as of June 30, 2012. The Medicare funds were received during July 2012. The income is reported as other revenue on the accompanying statements of revenue, expenses and changes in net assets.

(4) Inventories

A summary of inventories as of June 30, 2012 and 2011 is as follows:

	2012	2011
Medical stores	$ 126,611	$ 122,979
Dietary	28,289	35,295
Departmental	1,956,594	1,614,301
	$ 2,111,494	$ 1,772,575

(5) Property and equipment

The major classifications and changes in property and equipment as of and for the years ended June 30, 2012 and 2011 are as follows:

	Balance at June 30, 2011	Additions/ Transfers	Placed in Service/ Retirements	Balance at June 30, 2012
Land	$ 655,041	$ 237,209	$ -	$ 892,250
Land improvements	1,232,786	11,410	-	1,244,196
Buildings and improvements	48,025,884	8,003,848	(3,948)	56,025,784
Machinery and equipment	30,126,822	3,125,538	(478,133)	32,774,227
	80,040,533	11,378,005	(482,081)	90,936,457
Less allowance for depreciation and amortization:				
Land improvements	(1,117,428)	(24,399)	-	(1,141,827)
Buildings and improvements	(22,088,453)	(1,662,918)	-	(23,751,371)
Machinery and equipment	(22,268,514)	(3,237,857)	249,894	(25,256,477)
	(45,474,395)	(4,925,174)	249,894	(50,149,675)
	34,566,138	6,452,831	(232,187)	40,786,782
Construction in progress	7,586,794	2,259,576	(8,137,420)	1,708,950
	$ 42,152,932	$ 8,712,407	$ (8,369,607)	$ 42,495,732

	Balance at June 30, 2010	Additions/ Transfers	Placed in Service/ Retirements	Balance at June 30, 2011
Land	$ 655,041	$ -	$ -	$ 655,041
Land improvements	1,218,786	14,000	-	1,232,786
Buildings and improvements	47,938,113	87,771	-	48,025,884
Machinery and equipment	28,520,442	2,241,986	(635,606)	30,126,822
	78,332,382	2,343,757	(635,606)	80,040,533
Less allowance for depreciation and amortization:				
Land improvements	(1,082,016)	(35,412)	-	(1,117,428)
Buildings and improvements	(20,420,477)	(1,667,976)	-	(22,088,453)
Machinery and equipment	(19,841,276)	(3,044,201)	616,963	(22,268,514)
	(41,343,769)	(4,747,589)	616,963	(45,474,395)
	36,988,613	(2,403,832)	(18,643)	34,566,138
Construction in progress	140,382	7,799,139	(352,727)	7,586,794
	$ 37,128,995	$ 5,395,307	$ (371,370)	$ 42,152,932

The Medical Center is in the process of constructing various expansions and additions to the existing facilities. As of June 30, 2012, the total cost of these projects is expected to be approximately $5,550,000. Approximately $220,000 of interest costs were capitalized during the year ended June 30, 2012.

(6) Other intangible assets

Other intangible assets include non-compete agreements with 7 year lives. The non-compete agreements have a balance of $480,838 which is net of accumulated amortization of $36,988 as of June 30, 2012. Amortization expense totaled $36,988 in 2012. Future amortization expense of the net carrying amount of the non-compete agreement is $73,975 per year.

(7) Long-term debt

A schedule of changes in the Medical Center's long-term debt as of and for the years ended June 30, 2012 and 2011 is as follows:

	Balance at June 30, 2011	Additions	Reductions	Balance at June 30, 2012	Amounts Due Within One Year
Public Building Authority of the County of Montgomery, TN - Series 1997	$ 428,000	$ -	$ (428,000)	$ -	$ -
Public Building Authority of the County of Montgomery, TN - Series 2002	12,959,000	-	(548,000)	12,411,000	575,000
General Obligation Hospital Revenue and Tax Capital Outlay Note - Series 2011	5,932,278	-	(417,988)	5,514,290	431,281
Public Building Authority of the City of Clarksville, TN - Series 2012	-	7,000,000	-	7,000,000	398,000
Other debt	31,250	103,804	(61,525)	73,529	51,900
	$ 19,350,528	$ 7,103,804	$ (1,455,513)	$ 24,998,819	$ 1,456,181

	Balance at June 30, 2010	Additions	Reductions	Balance at June 30, 2011	Amounts Due Within One Year
Public Building Authority of the County of Montgomery, TN - Series 1997	$ 834,000	$ -	$ (406,000)	$ 428,000	$ 428,000
Public Building Authority of the County of Montgomery, TN - Series 2002	13,481,000	-	(522,000)	12,959,000	548,000
General Obligation Hospital Revenue and Tax Capital Outlay Note - Series 2011	-	6,000,000	(67,722)	5,932,278	453,360
Other debt	156,250	-	(125,000)	31,250	31,250
	$ 14,471,250	$ 6,000,000	$ (1,120,722)	$ 19,350,528	$ 1,460,610

During September 1997, the Medical Center entered into a loan agreement with the Public Building Authority of the County of Montgomery, Tennessee (Building Authority) whereby, the Building Authority loaned the Medical Center $4,500,000 for the construction, acquisition, and enlargement of its buildings, structures and facilities. As of June 30, 2011, the Medical Center had outstanding borrowings of $428,000 under this agreement. The remaining balance was paid during the fiscal year ending June 30, 2012.

During June 2002, the Medical Center entered into an additional loan agreement with the Public Building Authority of the County of Montgomery, Tennessee (Building Authority) whereby, the Building Authority agreed to loan the Medical Center up to $16,500,000 for the construction, acquisition, and enlargement of its buildings, structures, and facilities. As of June 30, 2012 and 2011, the Medical Center had outstanding borrowings of $12,411,000 and $12,959,000, respectively, under this agreement. The loan agreement bears interest at an adjustable rate (0.49% as of June 30, 2012), and is due in annual installments varying between $575,000 and $1,139,000 through May 25, 2027. The adjustable interest rate is adjusted daily as determined by the remarketing agent.

During April 2011, the Medical Center entered into a General Obligation Hospital Revenue and Tax Capital Outlay Note in the amount of $6,000,000 secured by the general obligation of Henry County for the construction and enlargement of its buildings, structures, and facilities. As of June 30, 2012 and 2011, the Medical Center had outstanding borrowings of $5,514,290 and $5,932,278 under this obligation. The note bears interest at a fixed rate of 3.27% per annum, and is due in monthly installments of $50,431 through April 1, 2023.

During January 2012, the Medical Center entered into a loan agreement with the Public Building Authority of the City of Clarksville, Tennessee (Building Authority) whereby, the Building Authority agreed to loan the Medical Center up to $7,000,000 to provide funding to finance certain public works projects, including the acquisition of the Kentucky Lake Surgery Center, LLC. As of June 30, 2012, the Medical center had outstanding borrowings of $7,000,000 under this obligation. The note bears interest at an adjustable rate (0.82% as of June 30, 2012), and is due in annual installments varying between $398,000 and $543,000 through June 1, 2027. The adjustable interest rate is adjusted weekly as determined by the remarketing agent.

Pursuant to the agreements for the Building Authority loans, if the principal of all bonds issued under such loans are accelerated, and the bonds are paid by the remarketing agent, the repayment schedule applicable to such loans shall be recalculated over a term of 60 months from the date of such acceleration. The interest rate on the loan amounts after such acceleration shall adjust to the prime rate as defined in the agreements.

A summary of future maturities and interest of long-term debt as of June 30, 2012 is as follows:

Year	Principal	Estimated Interest	Total Payments
2013	$ 1,456,181	$ 288,000	$ 1,744,181
2014	1,458,000	268,000	1,726,000
2015	1,512,000	246,000	1,758,000
2016	1,569,000	225,000	1,794,000
2017	1,627,000	202,000	1,829,000
2018 - 2022	9,101,000	640,000	9,741,000
2023 - 2027	8,275,638	128,000	8,403,638
	$ 24,998,819	$ 1,997,000	$ 26,995,819

(8) Employee benefit plans

Pension plan

Employees of the Medical Center are members of the Political Subdivision Pension Plan (PSPP), an agent multiple-employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement benefits as well as death and disability benefits. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members at the age of 55. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the system after July 1, 1979 become vested after five years of service and members joining prior to July 1, 1979 were vested after four years of service. Benefit provisions are established in state statute found in Title 8, Chapter 34-37 of the Tennessee Code Annotated (TCA). State statutes are amended by the Tennessee General Assembly. Political subdivisions such as the Medical Center participate in the TCRS as individual entities and are liable for all costs associated with the operation and administration of their plan. Benefit improvements are not applicable to a political subdivision unless approved by the chief governing body.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for the PSPP. That report may be obtained by writing to Tennessee Treasury Department, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, TN 37243-0230 or can be accessed at www.treasury.state.tn.us. Copies of footnotes in PDF format can be accessed at http://www.treasury.state.tn.us/tcrs/PS/.

The Medical Center is a political subdivision of the County. The Medical Center's funding policy and schedule of pension plan funding progress have not been included within the financial statements as these amounts are aggregated with the County. The Henry County Annual Financial Report should be read to obtain the aggregated information related to funding policy and schedule of pension plan funding progress. For the years ended June 30, 2012 and 2011, the Medical Center's annual pension costs were approximately $1,782,000 and $1,800,000, respectively.

Deferred compensation plans

Effective January 1, 2002, the Medical Center established a deferred compensation plan (the "Plan") under Section 457 of the Internal Revenue Code. Employees become eligible to participate in the Plan on their first day of employment. The Medical Center does not make any contributions to the Plan nor does it bear any of the administrative costs.

During 2010, the Medical Center implemented a physician call pay plan whereas the Medical Center would make contributions to the plan on behalf of the physicians. During 2011, the Medical Center made contributions to the plan of approximately $257,000. The plan had assets of approximately $400,000 and a liability of approximately $409,000 at June 30, 2011. The assets were included in other assets and the liability is included in other long-term liabilities in the accompanying statements of net assets. Effective July 1, 2011, the deferred element of the physician on-call plan was terminated and participants are paid quarterly. The deferred compensation was paid to the respective physicians during 2012. The Medical Center still holds the assets which are invested in mutual funds and amounted to approximately $470,000 at June 30, 2012. These assets are included in other assets in the accompanying statements of net assets.

(9) Commitments and contingencies

Lease commitments

The Medical Center leases various equipment under operating lease agreements. Rent expense was $1,438,452 and $1,172,873 in 2012 and 2011, respectively.

A summary of future minimum payments under these equipment leases as of June 30, 2012 is as follows:

Year		
2013	$	865,000
2014		777,000
2015		556,000
2016		297,000
2017		283,000
2018 and later years		1,303,000
	$	4,081,000

Insurance

The Medical Center maintains commercial insurance on a claims-made basis for medical malpractice liabilities. Insurance coverages are $300,000 individually and $900,000 in the aggregate annually, which is consistent with current litigation settlement limitations established by the State of Tennessee for governmental entities. Management intends to maintain such coverages in the future. The Medical Center is involved in litigation arising in the ordinary course of business; however, management is of the opinion that insurance coverages are adequate to cover any potential losses on asserted claims. Management is unaware of any incidents which would ultimately result in a loss in excess of the Medical Center's insurance coverages.

The Medical Center is self-insured for a portion of employee medical and other healthcare benefits and workers' compensation claims. The risk of loss retained by the Medical Center is limited to $130,000 and $350,000 per occurrence for employee health and workers' compensation, respectively. The Medical Center has purchased excess insurance to provide coverage for claims in excess of the self-insured retention. Contributions by the Medical Center for employee health are based on actuarial estimates, while contributions for workers' compensation are based on actual claims experience. Claims expense and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include a provision for estimated claims incurred but not reported. Reserves included within accrued expenses related to employee medical and other healthcare benefits amounted to $950,000 and $850,000 in 2012 and 2011, respectively. Reserves included within accrued expenses related to workers' compensation claims amounted to $384,867 and $334,867 in 2012 and 2011, respectively.

Healthcare Industry

The delivery of personal and health care services entails an inherent risk of liability. Participants in the health care services industry have become subject to an increasing number of lawsuits alleging negligence or related legal theories, many of which involve large claims and result in the incurrence of significant exposure and defense costs. The Company and its subsidiaries are insured with respect to medical malpractice risk on a claims-made basis. The Company also maintains insurance for general liability, director and officer liability and property. Certain policies are subject to deductibles. In addition to the insurance coverage provided, the Company indemnifies certain officers and directors for actions taken on behalf of the Company and its subsidiaries. Management is not aware of any claims against it or its subsidiaries which would have a material financial impact.

The health care 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 health care program participation requirements, reimbursement for patient services, and Medicare fraud and abuse. Recently, government activity has increased with respect to investigations and/or allegations concerning possible violations of fraud and abuse statutes and/or regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as repayments for patient services previously billed. Management believes that the Company is in compliance with fraud and abuse statutes, as well as other applicable government laws and regulations.

Management continues to implement policies, procedures, and compliance overview organizational structure to enforce and monitor compliance with the Health Insurance Portability and Accountability Act of 1996 and other government statues and regulations. The Medical Center's compliance with such laws and regulations is subject to future government review and interpretations, as well as regulatory actions which are unknown or unasserted at this time.

The Centers for Medicare and Medicaid Services ("CMS") have implemented a Recovery Audit Contractors ("RAC") program. The purpose of the program is to reduce improper Medicare payments through the detection and recovery of overpayments. CMS has engaged subcontractors to perform these audits and they are being compensated on a contingency basis based on the amount of overpayments that are recovered. While management believes that all Medicare billings are proper and adequate support is maintained, certain aspects of Medicare billing, coding and support are subject to interpretation and may be viewed differently by the RAC auditors. As the amount of any recovery is unknown, management has not recorded any reserves related to the RAC audit at this time.

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 ("collectively, the "Health Care Reform Legislation"). The Health Care Reform Legislation, among other matters, is designed to expand access to health care coverage to substantially all citizens through a combination of public program expansion and private industry health insurance. Provisions of the Health Care Reform Legislation become effective at various dates over the next several years and a number of additional steps are required to implement these requirements. Due to the complexity of the Health Care Reform Legislation, reconciliation and implementation of the legislation continues to be under consideration by lawmakers, and it is not certain as to what changes may be made in the future regarding health care policies. Changes to existing Medicaid coverage and payments are also expected to occur as a result of this legislation. While the full impact of Health Care Reform Legislation is not yet fully known, changes to policies regarding reimbursement, universal health insurance and managed competition may materially impact the Company's operations.

(10) Functional expenses

The following is a summary of management's functional classification of operating expenses:

	2012	2011
Healthcare services	$ 46,623,429	$ 44,262,436
General and administrative	24,809,444	23,272,983
	$ 71,432,873	$ 67,535,419

HENRY COUNTY MEDICAL CENTER
Hospital and HHA

Schedule of Net Assets Information

June 30, 2012 and 2011

Assets

	2012	2011
Current assets:		
Cash and cash equivalents	$ 225,161	$ 59,072
Assets limited as to use and that are required for current liabilities	1,456,181	1,460,610
Patient accounts receivable, net	8,886,936	7,617,682
Estimated third-party payor settlements	699,438	602,883
Other accounts receivable	1,543,634	-
Due from Healthcare Center	594,918	270,886
Due from EMS Agency	3,182,865	2,592,768
Inventories	2,057,659	1,714,799
Prepaid expenses and other current assets	736,921	356,895
Total current assets	19,383,713	14,675,595
Property and equipment, net	40,469,259	40,086,991
Long-term investments	7,227,537	7,768,993
Assets limited as to use, excluding assets required for current liabilities	10,279,199	13,758,636
Goodwill and other intangible assets	5,141,270	-
Other assets	1,312,003	1,071,889
	$ 83,812,981	$ 77,362,104

Liabilities and Net Assets

	2012	2011
Current liabilities:		
Current portion of long-term debt	$ 1,456,181	$ 1,460,610
Accounts payable	1,820,830	1,727,483
Accrued expenses	3,236,804	3,239,203
Total current liabilities	6,513,815	6,427,296
Long-term debt, excluding current portion	23,542,638	17,889,918
Other long-term liabilities	-	408,555
Total liabilities	30,056,453	24,725,769
Net assets:		
Unrestricted:		
Invested in capital assets, net of related debt	15,470,440	20,736,463
Unrestricted net assets	38,286,088	31,899,872
Total net assets	53,756,528	52,636,335
	$ 83,812,981	$ 77,362,104

See accompanying independent auditors' report.

HENRY COUNTY MEDICAL CENTER
Hospital and HHA

Schedule of Revenue, Expenses, and Changes in Net Assets Information

Years ended June 30, 2012 and 2011

	2012	2011
Operating revenue:		
Patient service revenue, net of provision for bad debts of $6,644,330 and $6,385,367 in 2012 and 2011, respectively	$ 57,462,125	$ 54,609,032
Management fee revenue	96,000	96,000
Other revenue	3,158,165	1,152,495
Total operating revenue	60,716,290	55,857,527
Expenses:		
Salaries and wages	23,605,643	23,131,835
Employee benefits	7,771,072	6,744,199
Supplies	13,789,570	12,456,129
Professional fees	3,050,111	2,613,061
Physician fees	716,511	485,024
Utilities and telephone	1,318,261	1,249,321
Repairs and maintenance	2,065,078	1,914,276
Leases and rentals	1,384,000	1,122,213
Insurance	333,444	335,705
Interest expense	35,817	87,985
Depreciation and amortization	4,597,365	4,406,605
Other expenses	986,689	1,057,886
Total expenses	59,653,561	55,604,239
Operating income	1,062,729	253,288
Nonoperating income - investment income	57,464	268,311
Excess of revenue over expenses	1,120,193	521,599
Net assets at beginning of year	52,636,335	52,114,736
Net assets at end of year	$ 53,756,528	$ 52,636,335

See accompanying independent auditors' report.

HENRY COUNTY MEDICAL CENTER
Healthcare Center

Schedule of Net Assets Information

June 30, 2012 and 2011

Assets

	2012	2011
Current assets:		
Cash and cash equivalents	$ 672,252	$ 747,396
Patient accounts receivable, net	1,205,889	1,185,192
Inventories	35,286	40,048
Prepaid expenses and other current assets	9,709	10,739
Total current assets	1,923,136	1,983,375
Property and equipment, net	1,864,992	1,931,950
	$ 3,788,128	$ 3,915,325

Liabilities and Net Assets

	2012	2011
Current liabilities:		
Accounts payable	$ 156,083	$ 190,164
Accrued expenses	524,026	503,570
Estimated third-party payor settlements	28,000	-
Due to Medical Center	594,918	270,886
Total current liabilities	1,303,027	964,620
Net assets:		
Unrestricted:		
Invested in capital assets, net of related debt	1,864,992	1,931,950
Unrestricted net assets	620,109	1,018,755
Total net assets	2,485,101	2,950,705
	$ 3,788,128	$ 3,915,325

See accompanying independent auditors' report.

HENRY COUNTY MEDICAL CENTER
Healthcare Center

Schedule of Revenue, Expenses, and Changes in Net Assets Information

Years ended June 30, 2012 and 2011

	2012	2011
Operating revenue:		
Patient service revenue, net of provision for bad debts of $23,369 and $0 in 2012 and 2011, respectively	$ 9,191,458	$ 9,923,054
Other revenue	20,163	34,070
Total operating revenue	9,211,621	9,957,124
Expenses:		
Salaries and wages	5,004,088	4,989,820
Employee benefits	1,655,189	1,745,983
Supplies	1,232,384	1,307,979
Professional fees	133,607	154,695
Physician fees	25,000	24,400
Utilities and telephone	219,038	230,350
Repairs and maintenance	95,188	54,943
Leases and rentals	26,080	20,530
Insurance	100,549	59,487
Depreciation and amortization	300,182	288,610
Other expenses	548,128	546,246
Services tax	338,200	387,148
Total expenses	9,677,633	9,810,191
Operating income (loss)	(466,012)	146,933
Nonoperating income - investment income	408	1,818
Excess of revenue over expenses (expenses over revenue)	(465,604)	148,751
Net assets at beginning of year	2,950,705	2,801,954
Net assets at end of year	$ 2,485,101	$ 2,950,705

See accompanying independent auditors' report.

HENRY COUNTY MEDICAL CENTER
EMS Agency

Schedule of Net Deficit Information

June 30, 2012 and 2011

Assets

	2012	2011
Current assets:		
Cash and cash equivalents	$ 50,867	$ 11,475
Patient accounts receivable, net	635,077	502,563
Inventories	18,549	17,728
Prepaid expenses and other current assets	28,786	5,697
Total current assets	733,279	537,463
Property and equipment, net	161,481	133,991
	$ 894,760	$ 671,454

Liabilities and Net Deficit

	2012	2011
Current liabilities:		
Accounts payable	$ 23,505	$ 28,992
Accrued expenses	94,151	87,896
Due to Medical Center	3,182,865	2,592,768
Total current liabilities	3,300,521	2,709,656
Net Deficit:		
Unrestricted:		
Invested in capital assets, net of related debt	161,481	133,991
Unrestricted net deficit	(2,567,242)	(2,172,193)
Total net deficit	(2,405,761)	(2,038,202)
	$ 894,760	$ 671,454

See accompanying independent auditors' report.

HENRY COUNTY MEDICAL CENTER
EMS Agency

Schedule of Revenue, Expenses, and Changes in Net Deficit Information

Years ended June 30, 2012 and 2011

	2012	2011
Patient service revenue, net of provision for bad debts of $484,787 and $426,596 in 2012 and 2011, respectively	$ 1,830,061	$ 1,779,486
Expenses:		
Salaries and wages	1,238,061	1,221,020
Employee benefits	392,213	401,694
Supplies	157,786	148,248
Professional fees	69,015	82,948
Physician fees	6,000	6,000
Utilities and telephone	27,836	25,536
Repairs and maintenance	75,396	104,808
Leases and rentals	28,372	30,130
Insurance	34,852	35,323
Depreciation and amortization	64,615	52,374
Other expenses	7,533	12,908
Management fees	96,000	96,000
Total expenses	2,197,679	2,216,989
Operating loss	(367,618)	(437,503)
Nonoperating income - investment income	59	303
Excess of expenses over revenues	(367,559)	(437,200)
Net deficit at beginning of year	(2,038,202)	(1,601,002)
Net deficit at end of year	$ (2,405,761)	$ (2,038,202)

See accompanying independent auditors' report.

HENRY COUNTY MEDICAL CENTER
Psychiatric Department

Schedule of Revenue and Expenses Information

Years ended June 30, 2012 and 2011

	2012	2011
Patient service revenue(1)	$ 3,716,773	$ 4,121,320
Operating expenses(1):		
Salaries and wages	849,248	983,131
Employee benefits	65,329	72,144
Professional services	104,660	109,067
Rent	1,142	1,142
Office supplies	1,866	3,552
Medical supplies	5,095	5,548
Pantry	8,086	10,030
Small equipment	287	158
Miscellaneous	1,503	9,757
Total expenses	1,037,216	1,194,529
Excess of revenue over expenses(1)	$ 2,679,557	$ 2,926,791

(1) The above information is summarized from the departmental report. It does not include estimates for contractual adjustments or bad debt expense, nor does it include any allocation of the costs incurred by the general service departments.

See accompanying independent auditors' report.

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*

The Board of Trustees
Henry County Medical Center
Paris, Tennessee:

We have audited the financial statements of Henry County Medical Center (Medical Center), a component unit of Henry County, Tennessee, as of and for the year ended June 30, 2012, and have issued our report thereon dated September 17, 2012. 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

Management of the Medical Center is responsible for establishing and maintaining effective 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 audit 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.

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 Medical Center's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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 previously.

Compliance and Other Matters

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

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

Lattimore Black Morgan & Cain, PC

Brentwood, Tennessee
September 17, 2012