

**Newaygo County General Hospital Association
(Gerber Memorial Health Services)**

**Financial Report
June 30, 2009**

Newaygo County General Hospital Association (Gerber Memorial Health Services)

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Independent Auditor's Report

To the Board of Directors
Newaygo County General Hospital Association
(Gerber Memorial Health Services)

We have audited the accompanying balance sheet of Newaygo County General Hospital Association (Gerber Memorial Health Services) as of June 30, 2009 and 2008 and the related statements of operations, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Newaygo County General Hospital Association (Gerber Memorial Health Services) at June 30, 2009 and 2008 and the results of its operations, changes in net assets, and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

October 1, 2009

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Balance Sheet

	<u>June 30, 2009</u>	<u>June 30, 2008</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 6,544,867	\$ 4,282,697
Accounts receivable (Note 2)	2,642,615	2,903,241
Estimated third-party payor settlements (Note 3)	580,000	509,855
Inventory	1,072,033	1,067,773
Other current assets	2,835,462	1,899,423
	<hr/>	<hr/>
Total current assets	13,674,977	10,662,989
Property and Equipment - Net (Note 6)	33,056,448	35,386,532
Investments (Note 4)	9,000,523	11,319,669
	<hr/>	<hr/>
Total assets	<u>\$ 55,731,948</u>	<u>\$ 57,369,190</u>
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt (Note 7)	\$ 911,006	\$ 876,006
Notes payable (Note 9)	1,500,000	-
Accounts payable	2,127,092	1,491,704
Estimated third-party payor settlements (Note 3)	350,000	-
Accrued liabilities and other	3,995,436	3,836,504
	<hr/>	<hr/>
Total current liabilities	8,883,534	6,204,214
Long-term Debt - Net of current portion (Note 7)	20,639,469	21,518,373
Fair Value of Interest Rate Swap Agreement (Note 7)	1,637,393	552,147
	<hr/>	<hr/>
Total liabilities	31,160,396	28,274,734
Net Assets		
Unrestricted	23,452,583	27,975,487
Temporarily restricted (Note 10)	1,093,836	1,093,836
Permanently restricted (Note 10)	25,133	25,133
	<hr/>	<hr/>
Total net assets	24,571,552	29,094,456
	<hr/>	<hr/>
Total liabilities and net assets	<u>\$ 55,731,948</u>	<u>\$ 57,369,190</u>

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Statement of Operations

	Year Ended	
	June 30, 2009	June 30, 2008
Unrestricted Revenue, Gains, and Other Support		
Net patient service revenue	\$ 61,128,204	\$ 59,037,610
Other	1,278,500	1,162,499
Total unrestricted revenue, gains, and other support	62,406,704	60,200,109
Expenses		
Salaries and wages	25,795,142	23,548,457
Employee benefits and payroll taxes	7,044,788	7,120,587
Medical supplies and drugs	8,646,481	8,854,553
Professional services and consultant fees	3,531,164	3,444,823
Purchased services	3,088,084	2,643,883
Depreciation and amortization	3,763,307	3,566,883
Provision for bad debts	3,652,727	4,910,226
Interest expense	1,477,083	843,019
Other	6,885,438	6,367,585
Total expenses (Note 13)	63,884,214	61,300,016
Operating Loss from Continuing Operations	(1,477,510)	(1,099,907)
Results from Discontinued Operations (Note 1)	(1,051,282)	(317,451)
Operating Loss	(2,528,792)	(1,417,358)
Other Income (Loss)		
Investment income	188,536	508,760
Contributions	856,314	750,849
Realized (loss) gain on sale of investments	(73,953)	167,257
Other income	46,675	(23,224)
Change in unrealized investment loss	(1,926,438)	(1,315,097)
Change in fair value of interest swap agreements	(1,085,246)	(761,108)
Total other loss	(1,994,112)	(672,563)
Excess of Expenses Over Revenues and Decrease in Unrestricted Net Assets	\$ (4,522,904)	\$ (2,089,921)

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Statement of Changes in Net Assets

	Year Ended	
	<u>June 30, 2009</u>	<u>June 30, 2008</u>
Decrease in Unrestricted Net Assets	\$ (4,522,904)	\$ (2,089,921)
Net Assets - Beginning of year	<u>29,094,456</u>	<u>31,184,377</u>
Net Assets - End of year	<u>\$ 24,571,552</u>	<u>\$ 29,094,456</u>

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Statement of Cash Flows

	Year Ended	
	June 30, 2009	June 30, 2008
Cash Flows from Operating Activities		
Decrease in net assets	\$ (4,522,904)	\$ (2,089,921)
Adjustments to reconcile decrease in net assets to net cash from operating activities:		
Depreciation and amortization	3,763,307	3,566,883
Net change in unrealized net gains and losses on investments	1,926,438	1,315,097
Loss (gain) on sale of investments	73,953	(167,257)
Loss on disposal of equipment	44,740	24,984
Provision for bad debts	3,652,727	4,910,226
Change in fair value of interest rate swap agreements	1,085,246	761,108
Changes in assets and liabilities which (used) provided cash:		
Accounts receivable	(3,392,101)	(2,737,364)
Inventory	(4,260)	101,871
Other current assets	(936,039)	(183,078)
Accounts payable	635,388	(1,047,115)
Accrued liabilities	158,932	446,526
Estimated third-party payor settlements payable	279,855	(1,252,221)
Net cash provided by operating activities	2,765,282	3,649,739
Cash Flows from Investing Activities		
Purchase of property and equipment	(1,477,963)	(7,959,879)
Purchase of investments	(1,091,990)	(3,949,336)
Proceeds from sale and maturities of investments	1,410,745	11,150,778
Net cash used in investing activities	(1,159,208)	(758,437)
Cash Flows from Financing Activities		
Principal payment on long-term debt	(843,904)	(856,006)
Net change in notes payable	1,500,000	-
Net cash provided by (used in) financing activities	656,096	(856,006)
Net Increase in Cash and Cash Equivalents	2,262,170	2,035,296
Cash and Cash Equivalents - Beginning of year	4,282,697	2,247,401
Cash and Cash Equivalents - End of year	\$ 6,544,867	\$ 4,282,697
Supplemental Cash Flow Information - Cash paid for interest	\$ 1,477,083	\$ 843,019

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 1 - Nature of Business and Significant Accounting Policies

Newaygo County General Hospital Association (Gerber Memorial Health Services) (the "Hospital") is a nonstock corporation organized under the laws of the State of Michigan, which operates a short-term, acute-care facility offering inpatient and outpatient healthcare services primarily to residents of Newaygo County and surrounding areas. During 2009, the Hospital ceased providing psychiatric services. The results from operations of psychiatric services are shown as discontinued operations on the statement of operations. The Hospital is managed under the direction of the association's board of directors, elected as provided in its bylaws. A significant portion of the Hospital's net patient service revenue is received under contractual arrangements with Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs and various health maintenance organizations.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents - Cash and cash equivalents include cash and investments in highly liquid investments purchased with an original maturity of three months or less, excluding those amounts included in assets limited as to use.

Accounts Receivable - Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges. An allowance for uncollectible accounts is established on an aggregate basis by using historical write-off rate factors applied to unpaid accounts based on aging. Loss rate factors are based on historical loss experience and adjusted for economic conditions and other trends affecting the Hospital's ability to collect outstanding amounts. Uncollectible amounts are written off against the allowance for doubtful accounts in the period they are determined to be uncollectible. An allowance for contractual adjustments and interim payment advances is based on expected payment rates from payors based on current reimbursement methodologies. This amount also includes amounts received as interim payments against unpaid claims by certain payors.

Inventories - Inventories, which consist of dietary, operating room, storeroom, and pharmaceutical products, are stated at cost, determined on a first-in, first-out basis or market. Maintenance and operating supplies are expensed as incurred.

Property and Equipment - Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

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

Investments - Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheet. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in income from operations unless the income or loss is restricted by donor or law.

In previous years, investments held by the Hospital were classified as available-for-sale securities with unrealized gains and losses that were considered temporary excluded from excess of expenses over revenue. During 2009, the Hospital determined that substantially all of its investment portfolio was more appropriately classified as trading, with unrealized gains and losses included in excess of expenses over revenue. Therefore, certain amounts in the accompanying financial statements have been reclassified to reflect this change in classification. These reclassifications did not impact the increase in net assets previously reported; however, the excess of expenses over revenue for 2008 decreased by \$1,315,097 as a result of the reclassification.

The Hospital invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the balance sheet.

Interest Rate Swap - The Hospital entered into an interest rate swap transaction to reduce economic risks associated with variability in cash outflows for interest required under provisions of variable rate bonds. Interest rate swaps are recognized as assets or liabilities at fair value. The change in the fair value of the interest rate swaps is included in other income (expense) in the statement of operations.

Temporarily and Permanently Restricted Net Assets - Temporarily restricted net assets are those whose use by the Hospital has been limited by donors to a specific time period or purpose. Donor-restricted assets whose restrictions are met within the same year as received are reported as unrestricted assets in the accompanying financial statements. Permanently restricted net assets have been restricted by donors to be maintained by the Hospital in perpetuity.

Contributions - The Hospital reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of changes in net assets as net assets released from restrictions.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

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

The Hospital reports gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Hospital reports the expiration of donor restrictions when the assets are placed in service.

Excess of Expenses Over Revenue - The statement of operations includes excess of expenses over revenue. Changes in unrestricted net assets, which are excluded from excess of expenses over revenue, consistent with industry practice, include net assets released from restrictions for the acquisition of long-lived assets, changes in certain qualifying interest rate swap agreements, and changes in unrealized gains and losses on investments.

Net Patient Service Revenue - The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactively calculated adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Management believes that it is in compliance with all applicable laws and regulations. Final determination of compliance of such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusions from the Medicare and Medicaid programs.

Professional and Other Liability Insurance - The Hospital accrues an estimate of the ultimate expense, including litigation and settlement expense, net of applicable reinsurance coverage, for incidents of potential improper professional service and other liability claims occurring during the year as well as for those claims that have not been reported at year end.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

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

Charity Care - The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The amount of charity care was \$1,959,219 and \$1,231,844 for the years ended June 30, 2009 and 2008, respectively.

Tax Status - The Hospital is a nonprofit, tax-exempt organization and, accordingly, no tax provision is reflected in the financial statements.

Fair Value of Financial Instruments - The fair value of financial instruments, including cash, accounts receivable, accounts payable, and debt, approximates the carrying values. Investments are recorded at fair value under generally accepted accounting principles. The fair value of debt approximates carrying value because of the variable-rate nature of the instrument. The interest rate swap is recorded at fair value on the Hospital's balance sheet.

Reclassification - Certain 2008 amounts have been reclassified to conform to the 2009 presentation.

Subsequent Events - The financial statements and related disclosures include evaluation of events up through and including October 1, 2009, which is the date the financial statements were issued.

Note 2 - Accounts Receivable

The details of accounts receivable are set forth below:

	2009	2008
Patient accounts receivable	\$ 14,980,721	\$ 15,513,537
Less allowance for uncollectible accounts	(2,459,576)	(1,889,654)
Less allowance for contractual adjustments	(9,878,530)	(10,720,642)
Net patient accounts receivable	<u>\$ 2,642,615</u>	<u>\$ 2,903,241</u>

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 2 - Accounts Receivable (Continued)

The Hospital grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The composition of receivables from patients and third-party payors was as follows:

	Percentage	
	2009	2008
Medicare	11	12
Blue Cross/Blue Shield of Michigan	7	9
Medicaid	20	21
Commercial insurance and HMOs	32	36
Self-pay	30	22
Total	100	100

Note 3 - Estimated Third-party Payor Settlements

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A significant portion of the Hospital's net patient service revenue is received from the Medicare, Medicaid, and Blue Cross Blue/Shield of Michigan programs. A summary of the basis of reimbursement with these third-party payors is as follows:

- **Medicare** - Inpatient, acute-care, and psychiatric services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Outpatient and home-care services related to Medicare beneficiaries are reimbursed based on a prospectively determined amount per episode of care.
- **Medicaid** - Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Capital costs relating to Medicaid patients are paid on a cost-reimbursement method. Outpatient and physician services are reimbursed on an established fee-for-service methodology.
- **Blue Cross/Blue Shield of Michigan** - Inpatient, acute-care services are reimbursed at prospectively determined rates per discharge. Outpatient services are reimbursed on a fee-for-service and percentage of charge basis.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 3 - Estimated Third-party Payor Settlements (Continued)

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 per discharge, discounts from established charges, and prospectively determined daily rates.

The Medicare program has initiated a Recovery Audit Contractor (RAC) initiative, whereby claims subsequent to October 1, 2007 will be reviewed by contractors for validity, accuracy, and proper documentation. A demonstration project completed in several other states resulted in the identification of potential significant overpayments. The RAC program is scheduled for Michigan hospitals in 2009. The Hospital is unable to determine if it will be audited and, if so, the extent of liability for overpayments, if any. If selected for audit, the potential exists for significant overpayment of claims liability for the Hospital at a future date.

Note 4 - Investments

The detail of investments at June 30 is as follows:

	2009	2008
Investments:		
General investments	\$ 7,271,311	\$ 9,128,800
Assets limited as to use:		
Investments held under bond indenture	610,243	1,071,900
Temporarily restricted assets	1,093,836	1,093,836
Permanently restricted assets	25,133	25,133
Total investments	<u>\$ 9,000,523</u>	<u>\$ 11,319,669</u>

Investments stated at fair value at June 30 include the following:

	2009	2008
Short-term investments	\$ 149,336	\$ 130,761
Corporate bonds	978,975	1,472,005
Corporate stock	4,544,106	5,585,174
Mutual funds	3,328,106	4,131,729
Total investments	<u>\$ 9,000,523</u>	<u>\$ 11,319,669</u>

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 4 - Investments (Continued)

Investment income and gains and losses are comprised of the following for the years ended June 30:

	<u>2009</u>	<u>2008</u>
Dividends and interest	\$ 188,536	\$ 508,760
Realized gains on sale of investments	(73,953)	167,257
Net change in unrealized gains and losses on investments	<u>(1,926,438)</u>	<u>(1,315,097)</u>
Total	<u>\$ (1,811,855)</u>	<u>\$ (639,080)</u>

Note 5 - Fair Value

As of July 1, 2008, the Hospital adopted Statement of Financial Accounting Standards No. 157 (SFAS 157), *Fair Value Measurements*. SFAS 157 clarifies the definition of fair value, establishes a framework for measuring fair value, and expands the disclosures for fair value measurements. The standard applies under other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. The provisions of SFAS 157 are effective prospectively for periods beginning July 1, 2008 for financial assets and liabilities and for periods beginning July 1, 2009 for nonfinancial assets and liabilities as a result of the deferral of the effective date of SFAS 157 provided by FSP FAS 157-2. The implementation of the provisions of SFAS 157 for financial assets and liabilities as of July 1, 2008 did not have a material impact on the Hospital's financial statements.

The following table presents information about the Hospital's assets and liabilities measured at fair value on a recurring basis at June 30, 2009, and the valuation techniques used by the Hospital to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Hospital has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 5 - Fair Value (Continued)

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in the entirety are categorized based on the lowest level input that is significant to the valuation. The Hospital's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

Disclosures concerning assets and liabilities measured at fair value on a recurring basis are as follows:

Fair Value Measurements at June 30, 2009

	Balance at June 30, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets - Investments	\$ 9,000,523	\$ 8,021,548	\$ 978,975	\$ -
Liabilities - Interest rate swaps	\$ 1,637,393	\$ -	\$ 1,637,393	\$ -

Note 6 - Property and Equipment

The cost of property and equipment and depreciable lives are summarized as follows:

	2009	2008	Depreciable Life - Years
Land	\$ 1,796,000	\$ 1,796,000	-
Land improvements	619,945	593,895	5-15
Buildings	40,628,701	38,288,275	5-40
Equipment	23,487,607	22,637,776	3-15
Construction in progress	-	1,816,911	-
Total cost	66,532,253	65,132,857	
Accumulated depreciation	(33,475,805)	(29,746,325)	
Net property and equipment	\$ 33,056,448	\$ 35,386,532	

Construction in progress during 2008 consisted of costs incurred in connection with renovations to the east wing of the Hospital's facility. This construction was completed during 2009.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 7 - Long-term Debt

Long-term debt at June 30, 2009 and 2008 is as follows:

	<u>2009</u>	<u>2008</u>
Series 2007 Revenue Bonds, collateralized by equipment and first mortgage on real estate. The revenue bonds require yearly principal payments on December 1 in amounts ranging from \$400,000 to \$775,000. The bonds bear interest at a variable rate (3.25 percent and 1.59 percent at June 30, 2009 and 2008, respectively), plus a 1.5 percent letter-of-credit commitment fee on outstanding balances	\$ 10,040,000	\$ 10,425,000
Series 2002 Revenue Bonds, collateralized by equipment and first mortgage on real estate. The revenue bonds require yearly principal payments on December 1, commencing in 2016, in amounts ranging from \$150,000 to \$705,000. The bonds bear interest at a variable rate (3.25 percent and 1.61 percent at June 30, 2009 and 2008, respectively), plus a 1.5 percent letter-of-credit commitment fee on outstanding balances	7,040,000	7,040,000
Series 1999 Revenue Bonds, collateralized by equipment and first mortgage on real estate. The revenue bonds require yearly principal payments on December 1 in amounts ranging from \$330,000 to \$435,000. The bonds have a variable rate of interest (3.25 percent and 1.61 percent at June 30, 2009 and 2008, respectively), plus a 1.25 percent letter-of-credit commitment fee on outstanding balances	2,585,000	2,895,000
Note payable to Michigan State Hospital Finance Authority (MSHFA), due in monthly installments of \$15,084 plus interest at a variable rate of 3.85 percent as of June 30, 2009 and 2008, plus a 1.25 percent letter-of-credit commitment fee on outstanding balances	<u>1,885,475</u>	<u>2,034,379</u>
Total	21,550,475	22,394,379
Less current portion	<u>(911,006)</u>	<u>(876,006)</u>
Long-term portion	<u>\$ 20,639,469</u>	<u>\$ 21,518,373</u>

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 7 - Long-term Debt (Continued)

The variable rate revenue bonds are remarketed on a weekly basis. Should the remarketing agent be unable to remarket the bonds based on its best efforts, these bonds would be "put" back to the bond trustee, who would draw down on the letter of credit to pay down the bonds. The reimbursement agreement between the letter-of-credit bank and the Hospital calls for the Hospital to reimburse the letter-of-credit bank for any remarketing draws within 367 days of the draw.

In connection with the revenue bonds, the Hospital has entered into an interest rate swap agreement with a swap provider to reduce the impact of changes in the interest rate on the variable rate bonds payable. At June 30, 2008, the notional principal amount of the Hospital's portion of the outstanding interest rate swap agreement was \$15,495,000. The swap agreement essentially changed the Hospital's interest rate exposure on the notional amount to a fixed 3.52 percent while receiving a variable rate payment equal to the sum of 67 percent of one-month LIBOR. During 2009, the Hospital entered into an agreement with the swap provider to terminate the existing swap and enter into a new swap at a notional amount of \$20,360,000. At June 30, 2009, the notional amount of the outstanding interest rate swap agreement was \$19,655,000. The interest rate exposure is a fixed rate at 4.18 percent while receiving a variable rate payment equal to the SIFMA index. The interest differential to be paid or received under the swap agreement is accrued and recognized as an adjustment to interest expense. The fair value of the interest rate swap is included on the Hospital's balance sheet. The interest rate swap agreement matures in December 2023.

The Hospital adopted Financial Accounting Standards Board Interpretation on Statement No. 133, *Cash Flow Hedges: Hedging Interest Cash Flows on Variable-rate Assets and Liabilities That Are Not Based on Benchmark Interest Rates*. This interpretation requires changes in fair value of interest rate swaps to be recorded through the performance indicator unless certain conditions are met and then the changes in the fair value of interest rate swaps are recorded through net assets.

In connection with its debt obligations, the Hospital has agreed to certain covenants, including minimum debt service and cash flow coverage ratios. During 2009, the Hospital failed to meet certain financial covenants and has obtained a waiver from the letter-of-credit bank.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 7 - Long-term Debt (Continued)

The following represents scheduled future principal payments on long-term debt:

2010	\$ 911,006
2011	946,006
2012	2,323,463
2013	840,000
2014	875,000
Thereafter	<u>15,655,000</u>
Total	<u>\$ 21,550,475</u>

Note 8 - Operating Leases

The Hospital leases building space and certain equipment under agreements that expire at various dates through 2013. Some of the leases contain provisions for renewal and purchase options and require the Hospital to pay related expenses.

The following schedule shows future lease payments under noncancelable operating leases for the next five years:

2010	\$ 762,227
2011	306,251
2012	110,105
2013	53,329
2014	<u>22,221</u>
Total	<u>\$ 1,254,133</u>

Rental expense charged to operations was approximately \$850,000 and \$900,000 for the years ended June 30, 2009 and 2008, respectively.

Note 9 - Notes Payable

The Hospital has a line of credit with a local bank for \$1,500,000 at a 30-day LIBOR interest rate plus 3.5 percent (an effective rate of 3.82 percent). The amount outstanding as of June 30, 2009 was \$1,500,000. The line of credit expires May 15, 2010.

Newaygo County General Hospital Association (Gerber Memorial Health Services)

Notes to Financial Statements June 30, 2009 and 2008

Note 10 - Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at June 30, 2009 and 2008:

	<u>2009</u>	<u>2008</u>
Indigent care	\$ 1,093,566	\$ 1,093,566
Various other programs	<u>270</u>	<u>270</u>
Total temporarily restricted net assets	<u>\$ 1,093,836</u>	<u>\$ 1,093,836</u>

Permanently restricted net assets are restricted for an endowment set aside for the obstetrical department.

Note 11 - Retirement Plan

The Hospital maintains a defined contribution retirement plan covering substantially all employees. For the years ended June 30, 2009 and 2008, the amount of pension expense was \$1,297,569 and \$1,275,604, respectively.

Note 12 - Professional Liability

The Hospital is insured against potential professional liability claims under a claims-made policy, whereby only the claims reported to the insurance carrier during the policy period are covered regardless of when the incident giving rise to the claim occurred. Under the terms of the policy, the Hospital bears the risk of the ultimate cost of any individual and aggregate claims exceeding the policy limits for claims asserted during the policy year.

Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during the claims-made term, but reported subsequently, will be uninsured.

Note 13 - Functional Expenses

The Hospital is a general acute-care facility that provides inpatient and outpatient healthcare services to patients in Newaygo County and the surrounding area. Expenses related to providing these services for the years ended June 30, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
Healthcare services	\$ 50,861,710	\$ 49,553,291
General and administrative	<u>13,022,504</u>	<u>11,746,725</u>
Total	<u>\$ 63,884,214</u>	<u>\$ 61,300,016</u>

Newaygo County General Hospital Association (Gerber Memorial Health Services)

**Notes to Financial Statements
June 30, 2009 and 2008**

Note 14 - Subsequent Event

During June 2009, the Hospital entered into a letter of intent with Spectrum Health, a Michigan nonprofit corporation, setting forth understanding in principle with respect to a potential acquisition or merger with the Hospital by Spectrum Health. Discussions related to any acquisition or merger are currently in preliminary phases and any such proposed merger will need to obtain approval under the Hart-Scott-Radino Antitrust Act by the federal government. The letter of intent expires December 31, 2009.