

PATTON – FULLER COMMUNITY HOSPITAL



Annual Report
2009

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Company History

Since its inception in 1975, Patton – Fuller Community Hospital has been dedicated to providing cutting-edge medical care to the people of Kelsey and the surrounding communities. PFCH is a for-profit hospital and is owned by physicians active at the facility. Quality patient care is the key to a hospital’s success and as shareholders in PFCH, our physicians are motivated to provide the best patient care possible.

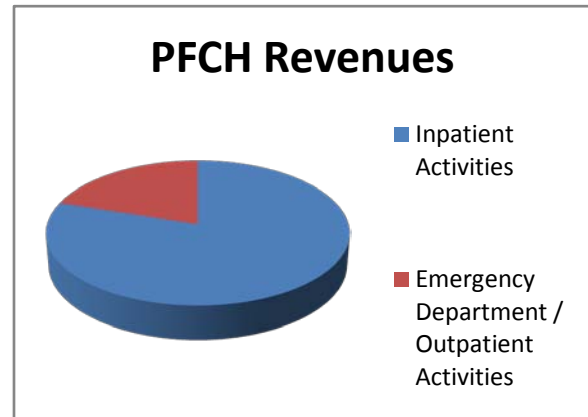
Our commitment to quality patient care has allowed us to grow to where we are today. As a 600-bed, full-service hospital, Patton – Fuller Community Hospital is the premier healthcare facility in the Northwest Valley.

Owned by the physicians active at the hospital, the organization is governed by a 14 member board of directors, comprised of 12 physician-owners, with the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) as non-voting members. The physician members serve 3-year terms and choose four new members every December during the annual shareholder meeting. The shareholder meeting is also when profits are distributed to the physician owners.

CFO Report

Patton - Fuller Community Hospital derives 80% of its revenue from inpatient activity, (including surgery charges, medical-surgical nursing, and Intensive Care Unit (ICU) charges).

The remaining 20% of its revenue is derived from the Emergency Department and other outpatient services.



The facility experiences the typical “seasonal” fluctuations in census, with the winter months producing the heavier workload and the summer months being less busy. Staffing is adjusted for census and workload, and other expenses also fluctuate. Utilities and other costs - contracted maintenance, some professional fees, and computer and other usage fees - do not fluctuate.

In 2009, PFCH experienced some significant events which are reflected in the financial statements.

In 2008, the PFCH community mourned the passing of Abigail Baderman, a long-time benefactor of the hospital. In December 2009, pursuant to the probate of her will, the hospital received a bequest from her estate, recognized as an unrestricted donation. (\$1,000,000 is shown on the Interim Statement of Income in December.).

Declines in the stock market and real estate markets resulted in a sharp drop in the return on investment income. This caused PFCH to reassess the value of its investments and, on their auditors’ advice, to write down those assets. This was reflected

in the Interim Statement of Income in November and is a “one-time” loss.

An annual inventory in December revealed that supply expenses were underestimated by \$1,000,000. That cost was added to December’s statement.

Following the favorable settlement of some managed care contract disputes, net patient revenue increased by 9% over the previous year, with an average 6% increase in expenses. However, the new arrangement allowed slower payment by the managed care companies, and Patient Accounts Receivable have risen sharply.

The Board responded favorably to heavy discounts offered by equipment vendors and invested in new equipment, using cash and releasing restricted assets, and borrowing as necessary.

In response to the overall economic recession, the Board held an emergency meeting in November and paid out annual profits early. The bonuses for the CEO and CFO were also paid, based on the hospital’s improved financial performance.

Because of the rise in Accounts Receivable, the Board created a business management committee to examine and report on efficiencies in the business office, including the error in inventory expense and the increase in inventory overall.

Long-term debt was obtained with an adjustable interest rate, on the CFO’s advice.

We start 2010 in an environment of uncertainty fueled by an uneven economy, continued high unemployment and the contentious debate on healthcare reform. However, we are confident that Patton – Fuller Community Hospital will weather the

storm. As in the past, our commitment to quality healthcare will allow us to prosper in the days ahead.

Zachary Hardie, Chief Financial Officer

Zachary Hardie

Message from the CEO

Patton - Fuller Community Hospital has had a successful year. The previous year’s loss has been turned into a gain, a change of over \$16 million. Net patient revenues have grown by over 9%, yet most expenses have been kept to an increase of just 3%. While the nation-wide economic downturn has affected the hospital, there were opportunities in that downturn. Major equipment vendors offered deep discounts and the board of directors released restricted cash reserves to purchase much-needed new equipment. Borrowing was also authorized on a limited basis for equipment. Extra supplies were also purchased at a deep discount, reducing expenses in the future. The physician owners have received the benefits of aggressive management of their hospital.

An analysis of the unaudited financial statements shows that all financial ratios have improved, and the hospital is poised to continue its profitable trend.

Davis Geach, Chief Executive Officer

Davis Geach

Report of Independent Auditors

To the Board of Directors of Patton - Fuller Community Hospital:

We have audited the accompanying balance sheet of Patton - Fuller Community Hospital (a stock corporation) as of December 31, 2009 and 2008, and the related statements of income, changes in net assets, and cash flow.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the hospital's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for expressing an opinion on the effectiveness of the hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the aforementioned financial statements present fairly, in all material respects, the financial position of Patton - Fuller Community Hospital at December 31, 2009 and 2008, and of their operations and their cash flows in conformity with accounting principles generally accepted in the United States.

Albert, Brooks, Borze & Stoops, LLC
Certified Public Accountants

Kay Albert

Kay Albert, CPA

Patton - Fuller Community Hospital
Balance Sheet as of December 31, 2009 and 2008
(In thousands)
(Audited)

	2009	2008
Assets		
Current Assets		
Cash and Cash Equivalents	\$22,995	\$41,851
Assets of limited use	27,594	41,851
Patient Accounts Receivable ¹ (net of allowance for bad debts 2009: \$11,757 / 2008: \$7,533)	58,787	37,666
Other receivables (3rd-party payer settlements)	-	87
Inventories	18,396	8,370
Prepaid Expenses	95	201
Total Current Assets	\$127,867	\$130,026
Other Assets		
Funded Depreciation	\$137,970	\$167,404
Held under bond indenture	73,584	75,332
Property, Plant and Equipment, net	248,346	175,774
Total Assets	587,767	548,535
 Liabilities and Equity		
Current Liabilities		
Current portion of long-term debt	\$14,599	\$4,185
Accounts payable, accrued expenses	9,198	4,185
Bond interest payable	10	10
Total Current Liabilities	\$23,807	\$ 8,380
Other Liabilities		
Long-term debt	\$452,945	\$209,255
Less: current portion of long-term debt	14,599	4,185
Net long-term debt	\$438,346	\$205,069
Total Liabilities	\$462,153	\$213,450

Equity

Common stock, \$ 0.01 par value 10,000,000 shares authorized 5,000,000 shares outstanding	\$50	\$50
Additional Paid-in Capital	0	0
Retained Earnings	<u>125,564</u>	<u>335,035</u>
Total Liabilities and Equity	<u>\$587,767</u>	<u>\$548,535</u>

¹ Includes adjustment due to audit

Note: Maximum Annual Debt Service

Bond interest payable	\$10	\$10
Current portion of long-term debt	<u>14,599</u>	<u>4,185</u>
Maximum annual debt service	\$14,609	\$4,195

Patton - Fuller Community Hospital
Statement of Revenue and Expense
2009 and 2008
(In thousands)
(Audited)

	<u>2009</u>	<u>2008</u>
Revenues		
Net Patient Revenue	\$459,900	\$418,509
Other Revenue	3,082	2,805
Total Revenues	<u>\$462,982</u>	<u>\$421,314</u>
Expenses		
Salaries and benefits	\$220,752	\$214,129
Supplies	74,584	71,346
Physician and professional fees	110,376	107,065
Utilities	1,200	1,164
Other	1,840	1,784
Depreciation & Amorization ("non-cash" expenses)	36,036	24,955
Interest	3,708	3,597
Provision for doubtful accounts ¹	14,797	13,383
Total Expenses	<u>\$463,293</u>	<u>\$437,424</u>
Operating Income	(\$311)	(\$16,110)
Non-operating income (loss)		
Investment income	(62)	264
Net Income	<u>(\$373)</u>	<u>(\$15,846)</u>

¹ Includes adjustment due to audit

Patton - Fuller Community Hospital, Inc.
Notes to Financial Statements
December 31, 2009 and 2008

1. Description of Business

Patton – Fuller Community Hospital is a stock corporation that owns the hospital and its related functions.

2. Significant Accounting Policies

Fair Values

Fair values carry the value of financial instruments, classified as current assets and current liabilities approximate fair value. The fair values of investments were adjusted during the year due to the extraordinary drop in market vales, with a resulting loss of investment income.

Cash and Cash Equivalents

Cash and cash equivalents consist primarily of cash and highly liquid marketable securities with an original maturity of 3 months or less when purchased by the hospital.

Investments

Hospital has substantially designated its investment portfolio as trading. Investment income, including gains and losses on investments, is included on the income statement.

Assets Limited as to Use

Assets limited as to use include assets that have been designated by the board of directors for payments under lease and loan agreements and for property and equipment replacement and expansion.

Net Patient Accounts Receivable

Net patient accounts receivable and net patient services revenues have been adjusted to the estimated amounts expected to be received. These are subject to further adjustments upon review by third-party payers. Management estimated bad debt expense and the allowance for doubtful accounts based on the historical collection experience, but new agreements with managed care payers required a substantial adjustment (\$1,000,000) to the expense and allowance accounts during this audit.

Costs of Borrowing

Debt issuance costs are deferred and amortized over the terms of the bonds using the straight-line method, which approximates the effective interest method. Interest incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Contributions

Unrestricted contributions received are recorded as other income.

Performance Indicator

The performance indicator is the excess of revenues over expenses, which includes all changes in unrestricted net assets through February 1, 2010.

Net Patient Revenue

Hospital has new agreements with third-party payers that provide for payments at amounts different from its established rates. Net patient revenue is reported at estimated net realizable amounts for rendered services. Contractual adjustments result from these agreements, with various organizations providing services for amounts that differ from billed charges, including services under Medicare, Medicaid, and certain managed care programs. These are recorded as deductions in net patient revenue. Hospital recognizes that revenue from managed care organizations is significant to the operations, and management believes that there are significant credit risks associated with these payers. Accordingly, an adjustment has been made to the provision for doubtful accounts and patient accounts receivable.

Adjustable Rate Debt

Hospital has new debt, which features an adjustable interest rate. The uncertainty of future interest rates is a contingency liability and will result in an adjustment to interest expense in the coming year.