

BEAUFORT MEMORIAL HOSPITAL  
AND OTHER COMBINED ENTITY

Combined Financial Statements

September 30, 2008 and 2007

( with Independent  
Auditors' Report thereon )

**BEAUFORT MEMORIAL HOSPITAL  
AND OTHER COMBINED ENTITY**

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## Independent Auditors' Report

To the Board of Trustees  
Beaufort Memorial Hospital and Other Combined Entity

We have audited the accompanying combined financial statements of Beaufort Memorial Hospital and Other Combined Entity, a public agency, (the "Hospital") as of September 30, 2008 and 2007, which comprise the Hospital's basic financial statements, as presented on pages 11 through 17. These combined financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal 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 combined financial statements and includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Beaufort Memorial Hospital and Other Combined Entity as of September 30, 2008 and 2007, and the results of their 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.

Management's Discussion and Analysis on pages 3 through 10 is not a required part of the basic combined financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

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To the Board of Trustees  
Beaufort Memorial Hospital and Other Combined Entity  
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Our audits were conducted for the purpose of forming an opinion on the combined financial statements taken as a whole. The supplementary combining information on pages 36 and 37 is presented only for purposes of additional analysis of the combined financial statements rather than to present the financial position and results of operations of the individual organizations, and is not a required part of the basic combined financial statements. Accordingly, we do not express an opinion on the financial position and results of operations of the individual organizations. However, the supplementary combining information has been subjected to the auditing procedures applied in the audit of the combined financial statements and, in our opinion, is fairly stated in all material respects in relation to the combined financial statements taken as a whole.

*Dixon Hughes PLLC*

January 16, 2009

## **BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**

### **Annual Financial Report**

The annual financial report of Beaufort Memorial Hospital (“BMH”) and Other Combined Entity (the “Hospital”) provides an overview of the Hospital’s financial activities for the fiscal years ended September 30, 2008 and 2007. The combined financial statements include the independent auditors’ opinion, the required combined financial statements, and accompanying explanatory notes. The required combined financial statements include a combined balance sheet, a combined statement of revenues, expenses, and changes in net assets, and a combined statement of cash flows. Management’s discussion and analysis should be read in conjunction with the combined financial statements and notes.

Beaufort Memorial Hospital Endowment Foundation (the Foundation) is a legally separate, tax-exempt component unit of the Hospital. The Foundation is a South Carolina corporation whose purpose is to support and encourage, through financial and fundraising assistance, the healthcare services and interests of the Hospital. Complete financial statements for the Foundation can be obtained from the Beaufort Memorial Hospital Endowment Foundation.

### **Management’s Discussion and Analysis**

#### ***Mission and Organizational Structure***

Beaufort Memorial Hospital is a not-for-profit, freestanding rural referral center, with a sole community hospital (Medicare) designation, located in Beaufort, South Carolina. The Hospital has 197 licensed beds, of which, 169 are medical/surgical acute, 14 are rehabilitation and 14 are mental health beds. The mission of the Hospital is to deliver superior healthcare services to our patients and to improve the health of our community. This mission embraces the charitable focus of the organization, which is to provide healthcare services regardless of the patient’s ability to pay. The hospital continues to be active in the community through its wellness and healthy community efforts. The Hospital’s vision is to exceed expectations for quality and compassionate care.

In addition to the financial statements and operations of Beaufort Memorial Hospital, the “Other Combined Entity” includes the information and accounts of Broad River Healthcare, Inc. (“Broad River”), which is a blended component unit of BMH. Broad River is a private, not-for-profit South Carolina corporation organized to assist BMH in meeting its mission and operational goals. The Hospital’s related entity company, Broad River, has a non-controlling interest in an outpatient surgery center, manages a mobile PET, and has a 100% interest in Beaufort Medical Imaging, LLC, which was created in 2007.

***Financial Highlights***

Net assets increased to \$129.8 million in 2008 from \$120.3 million in 2007, a \$9.5 million or 7.9% increase. The Hospital has had sound financial operations over the past four years, with consistently increasing net assets, primarily due to growing operating income. Although market share has remained stable, inpatient activity has declined while outpatient volumes have increased only 3.0% over 2007. Reimbursement issues have actually reduced net patient revenues to a point of only producing a 1.3% increase over the 2007 level. Operating expenses, while well controlled, increased 6.6% over the prior year. Thus the 2008 operating income decreased \$5.9 million from the 2007 operating income of \$11.6 million. Nonoperating revenues, net of expenses, slightly decreased from \$3.2 million in 2007 to \$3.1 million in 2008, a 2.8% decline.

***Required Combined Financial Statements***

The required financial statements are presented on an “enterprise” basis. Entities accounted for on an enterprise basis are primarily financed by charges for services to their users rather than tax receipts.

The combined balance sheet is a statement of the investments in resources (assets) and obligations to creditors (liabilities) on the last day of the fiscal year. The net asset balance is the value of the Hospital’s assets less its liabilities (net assets). The combined balance sheet classifies assets and liabilities as current and non-current, and can be used to evaluate the Hospital’s liquidity and ability to meet its future financial obligations.

The combined statement of revenues, expenses, and changes in net assets reports the revenue the Hospital generated from providing services to patients and the expenses required providing these services. Enterprise basis financial statements are prepared on an “accrual” basis, in which revenue is recorded for charges not yet received in cash and for obligations to creditors not yet paid in cash. Enterprise accounting requires that a portion of the cost of capital assets be recorded as depreciation expense. The statement also reports the changes in net assets attributable to nonoperating activities and from other transactions.

The combined statement of cash flows reports cash inflows and outflows from operations, financing activities, and investing activities, and their effect on the change in cash from the combined balance sheet.

### ***Analysis of Overall Financial Position and Results of Operations***

A summary of the Hospital's condensed combined balance sheets at September 30 is presented below:

| <i>(In thousands of dollars)</i>                   | <b><u>2008</u></b>       | <b><u>2007</u></b>       | <b><u>2006</u></b>       |
|--|--------------------------|--------------------------|--------------------------|
| Current assets                                     | \$ 95,283                | \$ 81,846                | \$ 71,959                |
| Capital assets, net                                | 72,629                   | 68,801                   | 68,172                   |
| Other non-current assets                           | <u>3,465</u>             | <u>13,578</u>            | <u>5,277</u>             |
| <b>Total assets</b>                                | <b><u>171,377</u></b>    | <b><u>164,225</u></b>    | <b><u>145,408</u></b>    |
| Current liabilities                                | 25,884                   | 26,990                   | 22,640                   |
| Long-term debt                                     | <u>15,722</u>            | 16,956                   | 18,119                   |
| <b>Total liabilities</b>                           | <b><u>\$ 41,606</u></b>  | <b><u>\$ 43,946</u></b>  | <b><u>\$ 40,759</u></b>  |
| <b>Net Assets</b>                                  |                          |                          |                          |
| Invested in capital assets,<br>net of related debt | \$ 43,885                | \$ 39,961                | \$ 41,893                |
| Restricted for debt service                        | 2,314                    | 2,376                    | 2,376                    |
| Expendable for specific<br>operating activities    | 481                      | 545                      | 601                      |
| Unrestricted                                       | <u>83,091</u>            | <u>77,397</u>            | <u>59,779</u>            |
| <b>Total net assets</b>                            | <b><u>\$ 129,771</u></b> | <b><u>\$ 120,279</u></b> | <b><u>\$ 104,649</u></b> |

Current assets, which consist primarily of cash, investments and accounts receivable, totaled \$95.3 million in 2008 and \$81.8 million in 2007. The Hospital's total current assets cover current liabilities 3.7 times in 2008, up from 2007's ratio of 3.0 times coverage. This is an improvement of the Hospital's liquidity. Current assets increased \$13.4 million or 16.4% in 2008 compared to 2007 primarily due to increases in cash and short-term investments as a result of continued improvements in patient receivable management. The Hospital's focus on improving its cash position through improved revenue cycle management can be seen in its consistent increases in current assets over the three year period ending 2008. Cash and short-term investments have increased from \$49.1 million in 2006 to \$61.8 million in 2007, to \$73.0 million in 2008, a three year increase of 78.7%. The Hospital's days cash on hand has increased from 157 days in 2006 to 203 days in 2008, a 29.3% improvement over this period. Current liabilities decreased slightly in 2008 due to reduction in our accounts payable. Long-term debt was reduced due to the annual bond principal payment made in November. Overall, total liabilities decreased \$2.3 million or 5.3% in 2008. Although the line of credit was used to purchase land during the fiscal year and increased slightly less than \$1.0 million, accounts payable and estimated third-party settlements decreased by \$2.2 million.

Net assets represent the residual interest in the Hospital's assets after liabilities are deducted. Total net assets in 2008 increased \$9.5 million or 7.9% over 2007, 2007 increased 14.9% over 2006, and 2006 increased 17.7% over 2005. Although not as great an increase in 2008 as the prior two years, Beaufort Memorial Hospital continues to show

sound growth in our net assets. Investments in capital assets (net) increased from \$39.9 million in 2007 to \$43.9 million in 2008, an increase of 9.8%. In addition to building improvements, expansions, and equipment purchases, the Hospital also purchased land across the street from the main campus to facilitate future growth. The Hospital continues to maintain its plant. The average age of plant for the Hospital is 7.8 years in 2008, up slightly from 7.2 years in 2007 and 2006. The capital budget for 2009 is approximately \$4.4 million, down from the 2008 capital budget.

The Hospital's current and long-term debt includes Hospital Revenue and Refinancing Bonds, Series 1997 with an outstanding balance of \$17.1 million as of September 30, 2008. Additionally, two short-term lines of credit have \$11.0 million outstanding in 2008 compared to \$10.1 million in 2007. The draws on the lines in 2008 are related to the purchase of 4.0 acres of commercial/medical property across the street from the main campus. Additionally, the Hospital is making monthly principal payments on the outstanding lines. The Hospital's debt service coverage has decreased due to its operating income reduction in 2008. However, the coverage ratio remains at a financially healthy 3.74 times.

The Combined Statements of Revenues, Expenses, and Changes in Net Assets present the Hospital's resulting financial activity for the year. A summary of the Hospital's condensed combined statements of revenues, expenses, and changes in net assets at September 30 is presented below:

| <i>(In thousands of dollars)</i>                              | <u>2008</u>       | <u>2007</u>       | <u>2006</u>       |
|---|-------------------|-------------------|-------------------|
| Operating revenues  | \$ 129,999        | \$ 128,226        | \$ 115,763        |
| Operating expenses  | <u>124,292</u>    | <u>116,593</u>    | <u>106,816</u>    |
| Operating income  | 5,707             | 11,633            | 8,947             |
| Nonoperating revenues<br>(net of expenses)                    | <u>3,151</u>      | <u>3,241</u>      | <u>3,025</u>      |
| Excess revenues over expenses<br>before capital contributions | 8,858             | 14,874            | 11,972            |
| Capital contributions   | <u>634</u>        | <u>756</u>        | <u>3,740</u>      |
| Increase in net assets  | 9,492             | 15,630            | 15,712            |
| <b>Net assets:</b>  |                   |                   |                   |
| Beginning of year   | <u>120,279</u>    | <u>104,649</u>    | <u>88,937</u>     |
| End of year   | \$ <u>129,771</u> | \$ <u>120,279</u> | \$ <u>104,649</u> |

Patient service revenues accounts for 98.3% of the Hospital's operating revenues. Operating revenues for 2008 increased 1.4% over 2007, compared to 2007's increase of 10.8% over the prior 2006. During 2008, contractual adjustments increased slightly (6.9%), and the Medicaid disproportionate share was reduced by \$2.5 million; the greatest influence on the Hospital's small operating revenue increase was the decline in inpatient activity. The Hospital's average daily census in 2008 dropped 3.2% from the prior year. Bad debts actually declined slightly in 2008 compared to 2007 and charity care as a percentage of revenues remained 3.6% in 2008 as it was in 2007. Overall, revenue deductions increased from 62.6% in 2006 to 64.0% in 2007, and finally to 65.0% in 2008.

Total operating expenses increased 6.6%, 9.2% and 4.8% in 2008, 2007 and 2006, respectfully. Labor costs (salaries, benefits and contract labor) accounted for 56.3% of operating expenses during 2008, compared to 56.0% in 2007 and 56.7% in 2006. The addition of a spine surgeon during the later part of 2008 had a material impact on the Hospital's supply expenses. Although the Hospital continues to have an active and successful supply chain management program, continued drug cost increases and surgical hardware influenced the 6.9% increase in supply costs during 2008. Overall, supply costs as a percentage of net patient revenues increased to 18.5% in 2008, up from 17.5% in 2007, but down from 19.3% in 2006. Nonoperating revenues, net of expenses decreased 2.77% during 2008. Part of this decrease was attributed to a decline in investment income. The Hospital maintains all investments in fully secured instruments, primarily in FDIC insured banks. Certificate of deposits are collateralized and therefore the stock market will have no impact on the Hospital's cash position other than reduction in interest earnings.

Excess revenues over expenses, before capital contributions and transfers, decreased 40.4% in 2008 as opposed to an increase of 24.2% in 2007 and an increase of 16.8% in 2006. The Hospital's operating margin for 2008 was 4.0% compared to 8.0% in 2007.

The Combined Statement of Cash Flows provides additional information about the Hospital's financial results by reporting the major sources and uses of cash. A summary of the Hospital's condensed combined statements of cash flows at September 30 is presented below:

| <i>(In thousands of dollars)</i>         | <u>2008</u>      | <u>2007</u>      | <u>2006</u>      |
|--|------------------|------------------|------------------|
| <b>Cash Flows</b>                        |                  |                  |                  |
| Operating activities                     | \$ 10,137        | \$ 23,486        | \$ 14,760        |
| Capital and related financing activities | (14,227)         | (7,428)          | (11,418)         |
| Investing activities                     | 3,761            | (13,223)         | 9,393            |
| Noncapital financing activities          | <u>1,269</u>     | <u>1,132</u>     | <u>1,153</u>     |
| Net increase(decrease) in cash           | 940              | 3,967            | 13,888           |
| <b>Cash and Cash Equivalents</b>         |                  |                  |                  |
| Beginning of year                        | <u>27,697</u>    | <u>23,730</u>    | <u>9,842</u>     |
| End of year                              | \$ <u>28,637</u> | \$ <u>27,697</u> | \$ <u>23,730</u> |

In 2008, the Hospital had cash generated by operating activities of \$10.1 million, a decrease of \$13.3 million from 2007 or 56.8%. This decrease was mainly due to a decline in receipts from patients totaling \$3.9 million. The majority of this decline came in the form of Medicaid disproportionate share funding that declined from \$3.6 million in 2007 to \$1.1 million in 2008. In addition, from 2007 to 2008, wages and benefits (payments to employees) increased 4.6% and payments to suppliers increased 15.6%, with a combined total increase of \$8.4 million.

### ***Budgets***

Unlike for other government facilities, budgets for entities accounted for on the enterprise basis are not legally binding documents. The budget for an enterprise fund is a guide for management and the Board in evaluating the success of the institution in meeting its financial goals.

### ***Future Opportunities and Challenges***

Beaufort Memorial Hospital continues to focus on strategic market capture, particularly in the southern portion of Beaufort County. This includes Hilton Head Island and Bluffton, two of the fastest growing communities in the State. The Hospital has worked with a national consulting firm to assist us in identifying the best locations, as well as the best services for the communities. The Hospital's multi-specialty clinic located in Bluffton continues to grow with a second floor in its current building expanded to facilitate additional physicians and ancillary services, to include bone density, ultrasound and mammography. The Hospital purchased a primary care clinic, with two physicians, located west of the Sun City retirement community. The free-standing cancer center continues to grow and the relationship with Duke Medical University has assisted this program's development. A new outpatient Woundcare Clinic was built in the Medical Office Plaza located on the campus of the Hospital. This clinic is providing many patients with needed services unavailable in the immediate area and volumes are increasing. This program includes two bariatric chambers for oxygen treatments. The pediatric physical therapy program, HealthLink, is relocating to the same medical plaza. The Hospital and community have a third spine surgeon and orthopedic activity remains strong with growth related to this additional spine surgeon. Our community is a growing retirement area and this specialty remains a focus for the Hospital. The Hospital is in discussions with a number of physicians and groups with the possibility of employment. The State of South Carolina is a certificate of need state and the Hospital follows the rules and regulations associated with this protocol. New and additional heart services for our retirement community are an area of considerable need. It is hoped that the Hospital will expand our heart catherizations program in the near future. During 2008, Beaufort Memorial Hospital filled a number of senior management positions that were vacant in 2007. The President and Chief Executive Officer was hired in November 2007. The Vice President of Human Resources and the Vice President and Chief Information Officer both arrived in 2008.

Both Moody's and Fitch have changed the 2009 outlook for not-for-profit hospitals from stable to negative. As mentioned in this discussion, our Hospital has felt the financial impact of this changing industry. Third-party programs are reducing their reimbursement as demanded by State and Federal budget issues and economic trends. Medicaid managed care programs are now taking over South Carolina's compensation for medical services. Additionally, as the only not-for-profit hospital in Beaufort County, we see continued increases in charity care adjustments, bad debts and account adjustments for uninsured patients. The Hospital has reduced its capital equipment budget by approximately \$1.0 million in 2009, and has placed major construction projects on hold until the industry has settled to the point that we are confident of the ability to financially cover these projects. The Hospital is focusing on revenue generation and cost control. Many new regulations

have restricted the ability of physician groups to take advantage of independently owned ancillary programs, such as imaging centers. The Hospital is carefully reviewing any situation that could allow local groups to terminate these centers and services, while ultimately increasing the Hospital volumes and revenues. Staffing levels throughout the industry have required the Hospital to use contract labor. Beaufort Memorial Hospital's contract labor costs in 2008 totaled \$3.9 million, compared to \$2.3 million in 2007. This labor cost is a focus for reduction in 2009 through increased hiring programs.

***Contacting the Hospital's Financial Management***

If you have questions about this report or need additional financial information, contact the Hospital's Senior Vice President and Chief Financial Officer at Beaufort Memorial Hospital, 955 Ribaut Road, Beaufort, South Carolina 29902.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**

Combined Balance Sheets

September 30, 2008 and 2007

| <u>Assets</u>   | <u>2008</u>           | <u>2007</u>           |
|---|-----------------------|-----------------------|
| Current assets:   |                       |                       |
| Cash and cash equivalents   | \$ 28,636,964         | \$ 27,696,418         |
| Short-term investments  | 44,378,800            | 34,074,997            |
| Patient accounts receivable, net of allowance for uncollectible accounts of \$8,619,795 in 2008 and \$8,225,984 in 2007 | 16,616,163            | 15,112,684            |
| Other accounts receivable   | 1,612,687             | 1,167,189             |
| Physician receivable, current portion   | 130,270               | 141,277               |
| Inventories of drugs and supplies   | 2,700,770             | 2,547,398             |
| Prepaid expenses  | <u>1,207,981</u>      | <u>1,106,096</u>      |
| Total current assets  | 95,283,635            | 81,846,059            |
| Assets limited as to use  | 2,314,094             | 2,376,072             |
| Investments   | -                     | 10,030,832            |
| Long-term equity investments  | 970,536               | 888,940               |
| Capital assets, net   | 72,629,245            | 68,801,024            |
| Physician receivable, less current portion  | 84,816                | 166,187               |
| Deferred financing costs, net   | <u>95,396</u>         | <u>116,230</u>        |
| Total assets  | \$ <u>171,377,722</u> | \$ <u>164,225,344</u> |
| <b><u>Liabilities and Net Assets</u></b>  |                       |                       |
| Current liabilities:  |                       |                       |
| Current portion of long-term debt   | \$ 1,415,000          | \$ 1,345,000          |
| Bank credit lines   | 11,017,542            | 10,080,767            |
| Accounts payable  | 4,337,283             | 5,816,196             |
| Accrued liabilities   | 7,803,364             | 7,712,503             |
| Estimated third-party payor settlements   | <u>1,311,429</u>      | <u>2,035,647</u>      |
| Total current liabilities   | 25,884,618            | 26,990,113            |
| Long-term debt, less current portion  | <u>15,721,840</u>     | <u>16,956,492</u>     |
| Total liabilities   | <u>41,606,458</u>     | <u>43,946,605</u>     |
| Net assets:   |                       |                       |
| Invested in capital assets, net of related debt   | 43,884,773            | 39,960,649            |
| Restricted:   |                       |                       |
| For debt service  | 2,314,094             | 2,376,072             |
| Expendable for specific operating activities  | 481,152               | 545,107               |
| Unrestricted  | <u>83,091,245</u>     | <u>77,396,911</u>     |
| Total net assets  | <u>129,771,264</u>    | <u>120,278,739</u>    |
| Total liabilities and net assets  | \$ <u>171,377,722</u> | \$ <u>164,225,344</u> |

The accompanying notes are an integral part of these combined financial statements.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**  
**Component Unit - Beaufort Memorial Hospital Endowment Foundation**

Statements of Position

September 30, 2008 and 2007

| <u>Assets</u>                         | <u>2008</u>         | <u>2007</u>          |
|---------------------------------------|---------------------|----------------------|
| Cash and cash equivalents             | \$ 621,162          | \$ 1,343,276         |
| Certificates of deposit               | 2,050,000           | 512,966              |
| Pledges receivable, net               | 210,053             | 237,873              |
| Investments                           | 6,014,619           | 7,928,246            |
| Other assets                          | <u>25,988</u>       | <u>25,957</u>        |
| Total assets                          | <u>\$ 8,921,822</u> | <u>\$ 10,048,318</u> |
| <u>Liabilities and Net Assets</u>     |                     |                      |
| Liabilities:                          |                     |                      |
| Payable to Beaufort Memorial Hospital | \$ 660,080          | \$ 1,124,264         |
| Obligation under gift annuity         | <u>8,911</u>        | <u>10,772</u>        |
| Total liabilities                     | 668,991             | 1,135,036            |
| Net assets:                           |                     |                      |
| Unrestricted                          | 1,721,061           | 932,086              |
| Board designated for endowment        | <u>6,072,777</u>    | <u>7,435,230</u>     |
| Total unrestricted                    | 7,793,838           | 8,367,316            |
| Temporarily restricted net assets     | <u>458,993</u>      | <u>545,966</u>       |
| Total net assets                      | <u>8,252,831</u>    | <u>8,913,282</u>     |
| Total liabilities and net assets      | <u>\$ 8,921,822</u> | <u>\$ 10,048,318</u> |

The accompanying notes are an integral part of these combined financial statements.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**

Combined Statements of Revenues, Expenses, and Changes in Net Assets

For the Years Ended September 30, 2008 and 2007

|  | <u>2008</u>                  | <u>2007</u>                  |
|--|------------------------------|------------------------------|
| Operating revenues:  |                              |                              |
| Net patient service revenue, net of provision for<br>bad debts of \$15,424,973 in 2008 and \$15,875,498<br>in 2007 | \$ 127,811,525               | \$ 126,196,063               |
| Other operating revenue  | <u>2,187,866</u>             | <u>2,030,472</u>             |
| Total operating revenues   | <u>129,999,391</u>           | <u>128,226,535</u>           |
| Operating expenses:  |                              |                              |
| Salaries and wages   | 52,101,204                   | 49,916,874                   |
| Employee benefits  | 13,937,448                   | 13,173,568                   |
| Contract labor   | 3,932,154                    | 2,259,649                    |
| Supplies   | 23,661,313                   | 22,143,584                   |
| Purchased services   | 8,761,725                    | 7,672,160                    |
| Physician fees   | 2,724,206                    | 3,469,142                    |
| Depreciation and amortization  | 8,653,998                    | 8,177,100                    |
| Other  | <u>10,520,014</u>            | <u>9,781,263</u>             |
| Total operating expenses   | <u>124,292,062</u>           | <u>116,593,340</u>           |
| Operating income   | <u>5,707,329</u>             | <u>11,633,195</u>            |
| Nonoperating revenues (expenses):  |                              |                              |
| Investment income  | 3,068,568                    | 3,125,843                    |
| Interest expense   | (1,359,280)                  | (1,450,359)                  |
| Loss on disposal of capital assets   | (812,487)                    | (75,925)                     |
| Share of income of investees, net  | 985,245                      | 509,900                      |
| County apportionment   | 643,382                      | 583,550                      |
| Noncapital gifts and bequests  | <u>626,011</u>               | <u>548,202</u>               |
| Total nonoperating revenues  | <u>3,151,439</u>             | <u>3,241,211</u>             |
| Excess of revenues over expenses before capital grants and contributions   | 8,858,768                    | 14,874,406                   |
| Capital grants and contributions   | <u>633,757</u>               | <u>755,859</u>               |
| Increase in net assets   | 9,492,525                    | 15,630,265                   |
| Net assets, beginning of year  | <u>120,278,739</u>           | <u>104,648,474</u>           |
| Net assets, end of year  | \$ <u><u>129,771,264</u></u> | \$ <u><u>120,278,739</u></u> |

The accompanying notes are an integral part of these combined financial statements.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**  
**Component Unit - Beaufort Memorial Hospital Endowment Foundation**

Statements of Activities and Changes in Net Assets

For the Years Ended September 30, 2008 and 2007

|                                      | <u>Year Ended September 30, 2008</u> |                     |                               | <u>Year Ended September 30, 2007</u> |                     |                               |
|--------------------------------------|--------------------------------------|---------------------|-------------------------------|--------------------------------------|---------------------|-------------------------------|
|                                      | <u>Total</u>                         | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Total</u>                         | <u>Unrestricted</u> | <u>Temporarily Restricted</u> |
| Support, revenue, and other          |                                      |                     |                               |                                      |                     |                               |
| Interest, dividends, and other       | \$ 367,577                           | \$ 367,577          | \$ -                          | \$ 338,902                           | \$ 338,902          | \$ -                          |
| Gains (losses) on investments        | (1,367,381)                          | (1,367,381)         | -                             | 915,560                              | 915,560             | -                             |
| Donations, gifts and bequests        | 998,125                              | 699,996             | 298,129                       | 893,488                              | 681,135             | 212,353                       |
| Fundraising income                   | 91,728                               | 91,728              | -                             | 111,206                              | 111,206             | -                             |
| Satisfaction of program restrictions | -                                    | 385,102             | (385,102)                     | -                                    | 230,179             | (230,179)                     |
|                                      | <u>90,049</u>                        | <u>177,022</u>      | <u>(86,973)</u>               | <u>2,259,156</u>                     | <u>2,276,982</u>    | <u>(17,826)</u>               |
| Total support and revenue            |                                      |                     |                               |                                      |                     |                               |
| Expenses                             |                                      |                     |                               |                                      |                     |                               |
| Fundraising events                   | 55,606                               | 55,606              | -                             | 49,163                               | 49,163              | -                             |
| General and administrative           | 46,490                               | 46,490              | -                             | 54,199                               | 54,199              | -                             |
| Grants to Beaufort Memorial Hospital | 648,404                              | 648,404             | -                             | 960,698                              | 960,698             | -                             |
| Total expenses                       | <u>750,500</u>                       | <u>750,500</u>      | <u>-</u>                      | <u>1,064,060</u>                     | <u>1,064,060</u>    | <u>-</u>                      |
|                                      |                                      |                     |                               |                                      |                     |                               |
| Increase (decrease) in net assets    | (660,451)                            | (573,478)           | (86,973)                      | 1,195,096                            | 1,212,922           | (17,826)                      |
| Net assets, beginning of year        | <u>8,913,282</u>                     | <u>8,367,316</u>    | <u>545,966</u>                | <u>7,718,186</u>                     | <u>7,154,394</u>    | <u>563,792</u>                |
| Net assets, end of year              | <u>\$ 8,252,831</u>                  | <u>\$ 7,793,838</u> | <u>\$ 458,993</u>             | <u>\$ 8,913,282</u>                  | <u>\$ 8,367,316</u> | <u>\$ 545,966</u>             |

The accompanying notes are an integral part of these combined financial statements.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**

Combined Statements of Cash Flows

For the Years Ended September 30, 2008 and 2007

|   | <u>2008</u>          | <u>2007</u>          |
|---|----------------------|----------------------|
| Cash flows from operating activities:                     |                      |                      |
| Receipts from and on behalf of patients                   | \$ 125,583,828       | \$ 129,446,687       |
| Other receipts and payments, net                          | (8,685,268)          | (7,586,217)          |
| Payments to employees                                     | (65,947,791)         | (63,058,472)         |
| Payments to suppliers                                     | <u>(40,813,568)</u>  | <u>(35,316,019)</u>  |
| Net cash provided by operating activities                 | <u>10,137,201</u>    | <u>23,485,979</u>    |
| Cash flows from capital and related financing activities: |                      |                      |
| Principal paid on long-term debt                          | (1,345,000)          | (1,275,000)          |
| Payments on lines of credit and capital leases            | (2,340,680)          | (68,370)             |
| Borrowing on lines of credit and capital leases           | 3,277,455            | 3,125,625            |
| Interest paid on long-term debt                           | (907,762)            | (1,049,783)          |
| Interest paid on lines of credit                          | (451,518)            | (421,683)            |
| Purchases of capital assets                               | (13,327,599)         | (8,704,212)          |
| Proceeds from sale of capital assets                      | 234,075              | 209,830              |
| Capital grants and contributions                          | <u>633,757</u>       | <u>755,859</u>       |
| Net cash used in capital and related financing activities | <u>(14,227,272)</u>  | <u>(7,427,734)</u>   |
| Cash flows from investing activities:                     |                      |                      |
| Increase (decrease) in investments, net of earnings       | 2,857,575            | (14,054,722)         |
| Distribution from investees                               | <u>903,649</u>       | <u>831,592</u>       |
| Net cash provided by (used in) investing activities       | <u>3,761,224</u>     | <u>(13,223,130)</u>  |
| Cash flows from noncapital financing activities:          |                      |                      |
| Noncapital gifts and bequests                             | 626,011              | 548,202              |
| County apportionment                                      | <u>643,382</u>       | <u>583,550</u>       |
| Net cash provided by noncapital financing activities      | <u>1,269,393</u>     | <u>1,131,752</u>     |
| Net increase in cash and cash equivalents                 | 940,546              | 3,966,867            |
| Cash and cash equivalents, beginning of year              | <u>27,696,418</u>    | <u>23,729,551</u>    |
| Cash and cash equivalents, end of year                    | <u>\$ 28,636,964</u> | <u>\$ 27,696,418</u> |

(continued)

## BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY

### Combined Statements of Cash Flows, Continued

For the Years Ended September 30, 2008 and 2007

|   | <u>2008</u>          | <u>2007</u>          |
|---|----------------------|----------------------|
| Reconciliation of operating income to net cash provided by operating activities:        |                      |                      |
| Operating income  | \$ 5,707,329         | \$ 11,633,195        |
| Adjustments to reconcile operating income to net cash provided by operating activities: |                      |                      |
| Depreciation and amortization   | 8,653,998            | 8,177,100            |
| Provision for bad debts   | 15,424,973           | 15,875,498           |
| Changes in assets and liabilities:  |                      |                      |
| Patient accounts receivable, net  | (16,928,452)         | (13,983,046)         |
| Other receivables and note receivable   | (353,120)            | 273,865              |
| Prepaid expenses and inventories of drugs and supplies                                  | (255,257)            | 448,336              |
| Accounts payable  | (1,478,913)          | (286,277)            |
| Accrued liabilities and estimated third party settlements                               | <u>(633,357)</u>     | <u>1,347,308</u>     |
| Net cash provided by operating activities   | <u>\$ 10,137,201</u> | <u>\$ 23,485,979</u> |
| <br><b><u>Schedule of non-cash investing and financing activities</u></b>               |                      |                      |
| Purchases of capital assets through accounts payable                                    | <u>\$ -</u>          | <u>182,686</u>       |

The accompanying notes are an integral part of these combined financial statements.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**  
**Component Unit - Beaufort Memorial Hospital Endowment Foundation**

Statements of Cash Flows

For the Years Ended September 30, 2008 and 2007

|   | <u>2008</u>       | <u>2007</u>         |
|---|-------------------|---------------------|
| Cash flows from operating activities:                                 |                   |                     |
| Increase (decrease) in net assets                                     | \$ (660,451)      | \$ 1,195,096        |
| Adjustments to reconcile to net cash provided by operating activities |                   |                     |
| Unrealized and realized (gains) losses on investments                 | 1,367,381         | (915,560)           |
| Other assets  | (31)              | (14,776)            |
| Pledges receivable, net   | 27,820            | 69,854              |
| Liabilities   | <u>(466,045)</u>  | <u>(323,746)</u>    |
| Net cash provided by operating activities                             | <u>268,674</u>    | <u>10,868</u>       |
| Cash flows from investing activities:                                 |                   |                     |
| Increase in certificates of deposit                                   | (1,537,034)       | (12,966)            |
| Decrease in investments, net of earnings                              | <u>546,246</u>    | <u>203,955</u>      |
| Net cash (used in) provided by investing activities                   | <u>(990,788)</u>  | <u>190,989</u>      |
| Net (decrease) increase in cash and cash equivalents                  | (722,114)         | 201,857             |
| Cash and cash equivalents, beginning of year                          | <u>1,343,276</u>  | <u>1,141,419</u>    |
| Cash and cash equivalents, end of year                                | <u>\$ 621,162</u> | <u>\$ 1,343,276</u> |

The accompanying notes are an integral part of these combined financial statements.

# BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY

## Notes to Combined Financial Statements

September 30, 2008 and 2007

### 1. Description of Reporting Entity and Summary of Significant Accounting Policies

**Reporting Entity** - The combined financial statements of Beaufort Memorial Hospital (“BMH”) and Other Combined Entity (the “Hospital”) include the accounts of Broad River Healthcare, Inc. (“Broad River”) and Beaufort Medical Imaging, LLC (“BMI”), which are blended component units of BMH. The Hospital’s related entity company Broad River has a non-controlling interest in limited liability companies (“LLC’s”). The Hospital’s combined financial statements are prepared using the accrual basis of accounting. All significant intercompany accounts have been eliminated.

Beaufort Memorial Hospital Endowment Foundation (the “Foundation”) is a legally separate, tax-exempt component unit of the Hospital. The Foundation is a South Carolina corporation, the purpose of which is to support and encourage, through financial and fundraising assistance, the health care services and interests of the Hospital. The Foundation is governed by a self-perpetuating board of trustees. Although the Hospital does not control the timing or amount of receipts from the Foundation, significantly all of the resources, or income thereon, that the Foundation holds and invests are restricted to the activities of the Hospital by the donors. Because these restricted resources held by the Foundation can only be used by, or for the benefit of the Hospital, the Foundation is considered a component unit of the Hospital and is discretely presented in the Hospital’s combined financial statements.

Complete financial statements for the Foundation can be obtained from Beaufort Memorial Hospital Endowment Foundation at 1005 Ribaut Road, Suite 21, Beaufort, South Carolina 29902.

Beaufort Memorial Hospital and Other Combined Entity are collectively referred to as the “Organizations” throughout the notes to the combined financial statements.

**Organization** - The Hospital is a not-for-profit healthcare facility which owns and operates a 197-bed acute care community hospital, a 14-bed rehabilitation facility and 14 mental health beds located in Beaufort, South Carolina. The Hospital is governed by a nine member Board of Trustees (the “Board”), whose members are appointed by the County Council of Beaufort County. The Board also appoints the board of directors for Broad River, which is a supporting organization for BMH. The Hospital, is a public agency as defined in Title 44, Chapter 7, of the Code of Laws of South Carolina, 1976, as amended, and is not included in the financial statements of Beaufort County.

**Basis of Presentation** - The Hospital utilizes enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the Hospital has elected to apply the provisions of all relevant pronouncements of the FASB, including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

The Foundation is a private nonprofit organization that reports under Financial Accounting Standards Board (“FASB”) standards, including FASB Statement No. 117, *Financial Reporting for Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from Governmental Accounting Standards Board (“GASB”) revenue recognition criteria and presentation standards. No modifications have been made to the Foundation’s financial information in the Hospital’s financial reporting entity for these differences.

**Use of Estimates** - The preparation of combined 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 combined financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include allowances for uncollectible accounts, contractual allowances, estimated useful lives of capital assets, settlements with third party payors, and risk retention areas such as estimates for incurred but not reported employee medical claims.

**Cash and Cash Equivalents** - Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less.

The Organizations maintain bank accounts at various financial institutions covered by the FDIC. At times throughout the year, the Organizations may maintain bank account balances in excess of the FDIC insured limit. It is management’s opinion that these financial institutions are financially sound and that the Organizations are not exposed to any significant credit risk related to cash.

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

**Investments** – The Hospital’s investments consist primarily of interest earning investment contracts and certificates of deposit. Non-participating investment contracts and certificates of deposit are carried at cost. All other investments are carried at fair value except investments in debt securities with maturities less than one year at the time of purchase. These investments are carried at amortized cost, which approximates fair value. Investment income including realized and unrealized gains and losses are reported as nonoperating revenues (expenses).

The Foundation’s investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the Statement of Position. Investment income or loss (including realized and unrealized gains and losses on investments, interest and dividends) is included in the Statement of Activities and Changes in Net Assets. Securities or other investments donated are recorded at their market value at the date of the gift.

**Long-Term Equity Investments** - The Hospital records its interest in investments where the Hospital has a twenty to fifty percent interest in a corporation under the equity method of accounting. Under the equity method, original investments are recorded at cost and adjusted for the Hospital's share of undistributed earnings or losses and distributions.

**Assets Limited as to Use** - Assets limited as to use include assets held by bond trustees under bond indenture agreements. Amounts required to meet current liabilities of the Hospital are classified as current assets on the combined balance sheets.

**Capital Assets** - Capital assets are recorded at cost or, in the case of donated property, at fair market value at the time of donation. Assets are depreciated using the straight-line method based on the estimated useful lives of the assets, which range from three to forty years. Additions and improvements are capitalized and depreciated over the estimated remaining lives of the related assets.

|                                     |                |
|-------------------------------------|----------------|
| Land improvements                   | 15 to 20 years |
| Buildings and building improvements | 20 to 40 years |
| Equipment, computers and furniture  | 3 to 7 years   |

**Deferred Financing Costs** - Deferred financing costs are amortized over the period the related obligation is outstanding. Accumulated amortization for deferred financing costs was \$304,918 and \$284,084 for September 30, 2008 and 2007, respectively. Losses on early extinguishment of debt are deferred and amortized over the remaining life of the old debt or the new debt, whichever is shorter.

**Physician Receivable** - The Hospital enters into loans to physicians as a method of recruiting certain physician specialties that are considered underserved in the community. If the physician complies with the provisions of the contract, the loan is forgiven by the Hospital over the term

of the loan. The Hospital amortizes the amount of the loan forgiven over the remaining life of the contracts. The remaining contract lives range from one to three years at September 30, 2008. Physician loans outstanding totaled \$215,086 and \$307,464 at September 30, 2008 and 2007, respectively.

**Net Assets** - Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and deferred financing costs reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted net assets include amounts deposited with trustees as required by revenue bond indentures, and amounts expendable for specific operating purposes. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

Net assets of the Foundation are classified in two components. Temporarily restricted net assets are those whose use has been limited by donors to a specific time period or purpose. Temporarily restricted net assets are transferred to unrestricted net assets when donor restrictions as to time and purpose have been met and are shown as net assets released from restrictions in the accompanying Statements of Activities and Changes in Net Assets.

**Net Patient Service Revenue** - 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. Third-party contractual revenue adjustments are accrued on an estimated basis in the period the related services are rendered. Such amounts are subject to audit by the governmental agencies. Adjustments, if any, are included in contractual revenue adjustments in the year of determination. In compliance with GASB 34, net patient revenue has been reduced by the amount of bad debt expense incurred by the Hospital.

The Hospital's policy does not require collateral or other security for patient accounts receivable. The Hospital routinely accepts assignment of, or is otherwise entitled to receive, patient benefits payable under health insurance programs, plans or policies such as those related to Medicare, Medicaid, Blue Cross, health maintenance organizations and commercial insurance carriers.

**Charity Care** - The Hospital 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 Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as net patient revenue. Partial payments to which the Hospital is entitled from public assistance on behalf of patients that meet the Hospital's charity care criteria are reported as patient service revenue.

**Recognition of Revenue by Component Unit Foundation** - Contributions are recognized as revenue when they are received or unconditionally pledged and are measured at their fair value and are reported as an increase in net assets.

The Foundation 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 or if they are stipulated as support for future periods. When a donor restriction expires, that is, when a stipulated purpose restriction is accomplished or time restriction ends, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Donor-restricted gifts which are received and either spent or deemed spent within the same year are reported as unrestricted revenues. Expenses are reported as decreases in unrestricted net assets.

**Operating Revenues and Expenses** - The statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Hospital's principal activity. Nonexchange revenues, including grants and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

**Grants and Contributions** - From time to time, the Hospital receives grants and contributions from individuals and private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses.

Under Financial Accounting Standards Board Statement No. 116, *Accounting for Contributions Received and Contributions Made*, (SFAS No. 116) the Foundation records contribution expense and a payable to the Hospital when the Foundation's board approves the future payment of funds to the hospital for specified purposes. The Foundation considers these restricted contributions to the Hospital because the funds must be spent for the purposes specified by the Foundation. In accordance with Governmental Accounting Standards Board Statement No. 33, *Accounting and Reporting for Non-exchange Transactions*, (GASB No. 33) the Hospital records contribution revenue when the funds are spent for the specified purpose, that is, when the reimbursable costs have been incurred. As a result of the different accounting treatment required under SFAS No. 116 and GASB No. 33, the Foundation has payable of approximately \$660,000 and \$1,124,000 as of September 30, 2008 and 2007, respectively, for which a corresponding receivable has not been recorded by the Hospital.

**Compensated Absences** – The Hospital’s employees earn paid days off (“PDO”) at varying rates depending on years of service. Accumulated PDO time may be carried over each year up to a maximum of 480 hours. The employee may elect to use PDOs or cash in PDO hours at that time.

If an employee has given and worked proper notice, upon termination, the employee will receive pay at the regular hourly rate for all unused PDO, providing the employee has completed three months of service.

All full-time employees must use a minimum of 40 PDO hours each calendar year and part time employees must use a minimum of 20 PDO hours. Failure to use these mandatory PDO hours will result in the forfeiture of these hours.

The estimated amount of the PDO payable is reported as a current accrued liability in both the 2008 and 2007 years.

**Restricted Resources** - When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources.

**Income Taxes** - Beaufort Memorial Hospital, Broad River Healthcare, Inc., Beaufort Medical Imaging, Inc., and Beaufort Memorial Hospital Endowment Foundation are exempt from Federal income tax as organizations described in Section 501(c)(3) of the Internal Revenue Code.

**Risk Management** - The Hospital is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice claims and judgments; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. The Hospital is self-insured for amounts up to a specified level for health and medical coverages for its employees. The estimated liability is the total estimated amount to be paid for all known claims or incidents and a reserve for incurred but not reported claims. The Hospital purchases professional and general liability insurance to cover medical malpractice claims. Claims under such coverage are covered based on the date of occurrence.

**Reclassifications** - Certain reclassifications were made in the 2007 combined financial statements to conform to the 2008 presentation.

2. **Accounts Receivable and Payable**

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the Hospital at September 30, 2008 and 2007 consisted of the following amounts:

|   | <b><u>2008</u></b>   | <b><u>2007</u></b>   |
|---|----------------------|----------------------|
| <b><u>Patient Accounts Receivable</u></b>           |                      |                      |
| Receivable from patients                            | \$ 14,262,806        | \$ 11,998,343        |
| Receivable from third-party payors and other        | 5,506,681            | 8,035,901            |
| Receivable from Medicare                            | 3,862,376            | 2,289,003            |
| Receivable from Medicaid                            | <u>1,604,095</u>     | <u>1,015,421</u>     |
| Total patient accounts receivable                   | 25,235,958           | 23,338,668           |
| Less: allowance for uncollectible accounts          | <u>(8,619,795)</u>   | <u>(8,225,984)</u>   |
| Net patient accounts receivable                     | <u>\$ 16,616,163</u> | <u>\$ 15,112,684</u> |
| <b><u>Accounts Payable and Accrued Expenses</u></b> |                      |                      |
| Payable to suppliers                                | \$ 4,435,944         | \$ 5,816,196         |
| Payable to employees (including payroll taxes)      | 7,405,818            | 7,355,247            |
| Accrued interest payable                            | <u>298,885</u>       | <u>357,256</u>       |
| Total accounts payable and accrued expenses         | <u>\$ 12,140,647</u> | <u>\$ 13,528,699</u> |

3. **Foundation Pledges Receivable**

Foundation pledges receivable consist of the following at September 30:

|                                     | <b><u>2008</u></b> | <b><u>2007</u></b> |
|-------------------------------------|--------------------|--------------------|
| Receivable in less than one year    | \$ 193,118         | \$ 156,710         |
| Receivable in one to five years     | 220,000            | 284,227            |
| Receivable after five years         | 400,000            | 400,000            |
| Discounts to present value          | (69,396)           | (76,645)           |
| Allowance for uncollectible pledges | <u>(533,669)</u>   | <u>(526,419)</u>   |
| Net pledges receivable              | <u>\$ 210,053</u>  | <u>\$ 237,873</u>  |

Pledges have been discounted at a 3.44% and 3.72% annual rate of interest for at September 30, 2008 and 2007, respectively.

4. **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. A summary of the reimbursement arrangements with major third-party payors follows:

**Medicare** - Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient services are reimbursed under a prospective payment system called the Ambulatory Payment Classification System (“APCs”). Inpatient non-acute services and defined capital and medical education costs related to Medicare beneficiaries are paid based a cost reimbursement methodology. The Hospital is reimbursed for cost-reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Hospital’s Medicare cost reports have been audited by the Medicare fiscal intermediary through 2006.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 created the Recovery Audit Contractors (RAC) program to detect and correct improper payments in the Medicare program. This began as a 3-year demonstration program in New York, Massachusetts, Florida, South Carolina, and California that ended in March 2008. This program is now being phased into all 50 states through 2009. During the year, the Hospital paid approximately \$390,000 as a result of RAC audits. As of September 30, 2008, the Hospital is not aware of any amounts due to the Medicare program as a result of the RAC audits, and no amounts are recorded on the Hospital’s combined financial statements.

**Medicaid** - Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Outpatient services are reimbursed at prospectively determined rates per procedures. The Hospital’s Medicaid cost reports have been audited by the Medicaid fiscal intermediary through 2008.

Revenue from Medicare and Medicaid programs accounted for approximately 36% and 6%, respectively, of the Hospital's net patient revenue for the year ended September 30, 2008, and 32% and 10%, respectively, of the Hospital's net patient service revenue, for the year ended September 30, 2007. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term as a result of third party reviews. The 2008 net patient service revenue decreased by approximately \$877,000 due to a change in the allowances previously estimated for tentative cost report settlements. The 2007 net patient service revenue decreased by approximately \$1,008,000 due to a change in the allowances previously estimated for tentative cost report settlements.

**Other** - The Hospital has also entered into payment agreements with certain commercial insurance carriers and provider organizations. The basis for payment to the Hospital under these agreements includes established Hospital charges, prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Net patient service revenue is comprised of the following at September 30:

|  | <u>2008</u>           | <u>2007</u>           |
|--|-----------------------|-----------------------|
| Gross patient charges at established rates | \$ 365,243,871        | \$ 347,334,066        |
| Medicaid disproportionate share            | 1,097,282             | 3,580,778             |
| Contractual adjustments                    | (209,757,247)         | (196,265,596)         |
| Provision for bad debts                    | (15,424,973)          | (15,875,498)          |
| Charity care                               | <u>(13,347,408)</u>   | <u>(12,577,687)</u>   |
| Net patient service revenue                | <u>\$ 127,811,525</u> | <u>\$ 126,196,063</u> |

5. **Cash and Cash Equivalents, Investments, and Assets Limited as to Use**

As required by state statutes, all of the Hospital's cash and cash equivalents and investments, which consist principally of certificates of deposit, overnight repurchase agreements and interest earning investment contracts, are covered by federal depository insurance, invested in U.S. Government obligations, or collateralized by U.S. governmental obligations held in the Hospital's name by a custodial bank.

The bond trustee invests in a non-participating interest earning investment contract in which the Hospital receives a guaranteed interest rate of return. As such, this investment is reported at cost at September 30, 2008 and 2007.

At September 30, the Hospital had bank balances including overnight investments as follows:

|  | <u>2008</u>          | <u>2007</u>          |
|--|----------------------|----------------------|
| Insured (FDIC) or collateralized by securities held by the pledging financial institution's trust department or agent in the Hospital's name | <u>\$ 34,766,300</u> | <u>\$ 29,854,330</u> |
| Carrying amount  | <u>\$ 28,636,964</u> | <u>\$ 27,696,418</u> |

Investments at September 30 consist of the following:

|   | <u>2008</u>          | <u>2007</u>          |
|---|----------------------|----------------------|
| Certificates of deposit maturing within one year  | \$ 44,378,800        | \$ 34,074,997        |
| Certificates of deposit maturing within two years | <u>-</u>             | <u>10,030,832</u>    |
|   | 44,378,800           | 44,105,829           |
| Guaranteed investment contract, held by trustee   | <u>2,314,094</u>     | <u>2,376,072</u>     |
|   | <u>\$ 46,692,894</u> | <u>\$ 46,481,901</u> |

Custodial credit risk for investments is the risk that, in the event of failure of the counterparty, the Hospital will not be able to recover the value of the investments or

collateral securities that are in the possession of an outside party. Investments with third party banks and investment held by a trustee are not registered in the name of the Hospital. Investments held with third party banks are invested primarily in certificates of deposit. Investments held by a trustee are invested in a guaranteed investment contract. Investments with third party banks and investments held by a trustee are fully collateralized and insured as of September 30, 2008 and 2007 with securities maintained by an outside party.

Concentration of credit risk is the risk of loss attributed to the magnitude of the Hospital's investments in a single issuer. The Hospital has the following investments in excess of five percent of total investments at September 30:

| Investment type                | <u>2008</u>   | <u>2007</u>   |
|--------------------------------|---------------|---------------|
| Certificate of deposit         | \$ 10,657,073 | \$ 10,084,423 |
| Certificate of deposit         | 8,933,599     | 16,398,821    |
| Certificate of deposit         | -             | 7,913,770     |
| Certificate of deposit         | 19,704,645    | 4,394,834     |
| Certificate of deposit         | 2,608,565     | 2,608,564     |
| Guaranteed investment contract | 2,314,094     | 2,376,072     |

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Hospital minimizes their interest rate risk by investing in certificates of deposit with maturities of less than two years and a guaranteed investment contract.

The carrying values of cash and cash equivalents and investments are included in the combined balance sheets as follows:

|                           | <u>2008</u>          | <u>2007</u>          |
|---------------------------|----------------------|----------------------|
| Cash and cash equivalents | \$ 28,636,964        | \$ 27,696,418        |
| Investments               | <u>46,692,894</u>    | <u>46,481,901</u>    |
|                           | <u>\$ 75,329,858</u> | <u>\$ 74,178,319</u> |

Included in the following combined balance sheet captions:

|                           | <u>2008</u>          | <u>2007</u>          |
|---------------------------|----------------------|----------------------|
| Cash and cash equivalents | \$ 28,636,964        | \$ 27,696,418        |
| Short-term investment     | 44,378,800           | 34,074,997           |
| Investments               | -                    | 10,030,832           |
| Assets limited as to use  | <u>2,314,094</u>     | <u>2,376,072</u>     |
|                           | <u>\$ 75,329,858</u> | <u>\$ 74,178,319</u> |

6. **Foundation Investments**

The fair market values of investments of the Foundation at September 30 are as follows:

|                           | <b><u>2008</u></b>  | <b><u>2007</u></b>  |
|---------------------------|---------------------|---------------------|
| Cash and cash equivalents | \$ 2,234,435        | \$ 1,344,298        |
| Mutual funds              | 4,382,130           | 5,403,738           |
| Equity                    | <u>1,448,054</u>    | <u>1,693,176</u>    |
|                           | <u>\$ 8,064,619</u> | <u>\$ 8,441,212</u> |

Investment income is comprised of the following at September 30:

|                           | <b><u>2008</u></b>  | <b><u>2007</u></b>  |
|---------------------------|---------------------|---------------------|
| Investment income:        |                     |                     |
| Interest and dividends    | \$ 367,577          | \$ 338,902          |
| Unrealized gains (losses) | (1,412,156)         | 883,681             |
| Realized gains (losses)   | <u>44,775</u>       | <u>31,879</u>       |
| Realized (losses) gains   | <u>\$ (999,804)</u> | <u>\$ 1,254,462</u> |

7. **Capital Assets**

Capital asset additions, retirements and balances for the years ended September 30 are as follows:

|                                | <b><u>September 30,<br/>2007</u></b> | <b><u>Additions</u></b> | <b><u>Retirements</u></b> | <b><u>September 30,<br/>2008</u></b> |
|--------------------------------|--------------------------------------|-------------------------|---------------------------|--------------------------------------|
| Land                           | \$ 13,323,897                        | \$ 3,913,644            | \$ -                      | \$ 17,237,541                        |
| Land improvements              | 1,344,081                            | 12,455                  | -                         | 1,356,536                            |
| Buildings                      | 58,794,315                           | 4,533,800               | 823,358                   | 62,504,757                           |
| Equipment                      | 52,365,221                           | 4,867,700               | -                         | 57,232,921                           |
| Construction in progress       | <u>280,155</u>                       | <u>-</u>                | <u>280,155</u>            | <u>-</u>                             |
| Total at historical cost       | <u>126,107,669</u>                   | <u>13,327,599</u>       | <u>1,103,513</u>          | <u>138,331,755</u>                   |
| Less accumulated depreciation: |                                      |                         |                           |                                      |
| Land improvements              | 777,963                              | 68,398                  | -                         | 846,361                              |
| Buildings                      | 24,079,216                           | 3,242,984               | 56,951                    | 27,265,249                           |
| Equipment                      | <u>32,449,466</u>                    | <u>5,141,434</u>        | <u>-</u>                  | <u>37,590,900</u>                    |
| Total accumulated depreciation | <u>57,306,645</u>                    | <u>8,452,816</u>        | <u>56,951</u>             | <u>65,702,510</u>                    |
| Capital assets, net            | <u>\$ 68,801,024</u>                 | <u>\$ 4,874,783</u>     | <u>\$ 1,046,562</u>       | <u>\$ 72,629,245</u>                 |

|                                | <b>September 30,<br/>2006</b> | <b>Additions</b>  | <b>Retirements</b> | <b>September 30,<br/>2007</b> |
|--------------------------------|-------------------------------|-------------------|--------------------|-------------------------------|
| Land                           | \$ 13,323,897                 | \$ -              | \$ -               | \$ 13,323,897                 |
| Land improvements              | 1,333,689                     | 10,392            | -                  | 1,344,081                     |
| Buildings                      | 57,407,055                    | 1,486,864         | 99,604             | 58,794,315                    |
| Equipment                      | 45,828,611                    | 7,109,487         | 572,877            | 52,365,221                    |
| Construction in progress       | -                             | 280,155           | -                  | 280,155                       |
| Total at historical cost       | <u>117,893,252</u>            | <u>8,886,898</u>  | <u>672,481</u>     | <u>126,107,669</u>            |
| Less accumulated depreciation: |                               |                   |                    |                               |
| Land improvements              | 711,558                       | 66,405            | -                  | 777,963                       |
| Buildings                      | 21,254,248                    | 2,824,968         | -                  | 24,079,216                    |
| Equipment                      | <u>27,755,533</u>             | <u>5,080,652</u>  | <u>386,719</u>     | <u>32,449,466</u>             |
| Total accumulated depreciation | <u>49,721,339</u>             | <u>7,972,025</u>  | <u>386,719</u>     | <u>57,306,645</u>             |
| Capital assets, net            | <u>\$ 68,171,913</u>          | <u>\$ 914,873</u> | <u>\$ 285,762</u>  | <u>\$ 68,801,024</u>          |

**8. Long-Term Equity Investments**

The Hospital's ownership percentage and investments at September 30, 2008 and 2007 for entities recorded under the equity method are as follows:

|  | <b>Ownership<br/>Percentage</b> |             | <b>Investment</b> |                   | <b>Share of Income</b> |                   |
|--|---------------------------------|-------------|-------------------|-------------------|------------------------|-------------------|
|  | <b>2008</b>                     | <b>2007</b> | <b>2008</b>       | <b>2007</b>       | <b>2008</b>            | <b>2007</b>       |
| The Surgery Center<br>of Beaufort, LLC | 40.0%                           | 40.0%       | \$ 970,386        | \$ 888,790        | \$ 985,245             | \$ 509,900        |
| Other                                  | -                               | -           | <u>150</u>        | <u>150</u>        | <u>-</u>               | <u>-</u>          |
|  |                                 |             | <u>\$ 970,536</u> | <u>\$ 888,940</u> | <u>\$ 985,245</u>      | <u>\$ 509,900</u> |

Summarized un-audited financial information of The Surgery Center of Beaufort, LLC as of and for the year ended September 30, 2008 and 2007 is as follows:

|                              | <b>2008</b>         | <b>2007</b>         |
|------------------------------|---------------------|---------------------|
| Current assets               | \$ 1,662,346        | \$ 1,381,301        |
| Total assets                 | 3,777,874           | 3,740,770           |
| Current liabilities          | 287,723             | 281,491             |
| Total liabilities            | 1,400,749           | 1,518,794           |
| Equity                       | 2,377,125           | 2,221,976           |
| Total liabilities and equity | 3,777,874           | 3,740,770           |
| Revenue                      | 6,128,572           | 5,017,112           |
| Expenses                     | <u>3,665,460</u>    | <u>3,742,362</u>    |
| Net income                   | <u>\$ 2,463,112</u> | <u>\$ 1,274,750</u> |

In 2007, Beaufort Medical Imaging, LLC was created as a wholly owned subsidiary of Broad River Health Care, LLC. Broad River and Beaufort Memorial Hospital transferred \$3,825,000 of imaging equipment to BMI, LLC through an inter-company transaction. All intercompany transactions have been eliminated in the combined statements.

**9. Long-term Debt**

At September 30, long-term obligations included the following:

|   | <b>September 30,<br/><u>2007</u></b> | <b><u>Additions</u></b> | <b><u>Reductions</u></b> | <b>September 30,<br/><u>2008</u></b> | <b><u>Amounts due<br/>within one year</u></b> |
|---|--------------------------------------|-------------------------|--------------------------|--------------------------------------|---|
| Bonds and notes payable:                                    |                                      |                         |                          |                                      |   |
| Revenue bonds   | \$ 19,175,000                        | \$ -                    | \$ (1,345,000)           | \$ 17,830,000                        | \$ 1,415,000                                  |
| Less unamortized discount and deferred loss on re-financing | <u>873,508</u>                       | <u>-</u>                | <u>(180,348)</u>         | <u>693,160</u>                       | <u>-</u>                                      |
| Total long-term debt  | <u>\$ 18,301,492</u>                 | <u>\$ -</u>             | <u>\$ (1,164,652)</u>    | <u>\$ 17,136,840</u>                 | <u>\$ 1,415,000</u>                           |

|   | <b>September 30,<br/><u>2006</u></b> | <b><u>Additions</u></b> | <b><u>Reductions</u></b> | <b>September 30,<br/><u>2007</u></b> | <b><u>Amounts due<br/>within one year</u></b> |
|---|--------------------------------------|-------------------------|--------------------------|--------------------------------------|---|
| Bonds and notes payable:                                    |                                      |                         |                          |                                      |   |
| Revenue bonds   | \$ 20,450,000                        | \$ -                    | \$ (1,275,000)           | \$ 19,175,000                        | \$ 1,345,000                                  |
| Capital lease payments                                      | <u>68,370</u>                        | <u>-</u>                | <u>(68,370)</u>          | <u>-</u>                             | <u>-</u>                                      |
|   | 20,518,370                           | -                       | (1,343,370)              | 19,175,000                           | 1,345,000                                     |
| Less unamortized discount and deferred loss on re-financing | <u>1,056,105</u>                     | <u>-</u>                | <u>(182,597)</u>         | <u>873,508</u>                       | <u>-</u>                                      |
| Total long-term debt  | <u>\$ 19,462,265</u>                 | <u>\$ -</u>             | <u>\$ (1,160,773)</u>    | <u>\$ 18,301,492</u>                 | <u>\$ 1,345,000</u>                           |

On November 13, 1997, BMH issued \$28,740,000 of Series 1997 Bonds. Net proceeds of \$26,093,971 were used: i) to advance refund outstanding principal amounts for the Series 1977 Bonds and Series 1990 Bonds amounting to \$1,190,000 and \$19,580,000, respectively, ii) to provide \$5,670,086 for the cost of acquiring construction, improving, and equipping an expansion of the Hospital, and iii) to fund a debt service reserve account and to pay certain expenses associated with Series 1997 Bonds. The Series 1997 Bonds are secured by revenues of the Hospital. Interest is payable each May and November at rates ranging from 3.90% to 5.25%. BMH is the sole member of the obligated group.

The advance refunding resulted in an economic gain (the difference between the reacquisition price and the net carrying amount of the old and new debt service payments) of approximately \$1,300,000. The difference between the reacquisition price and the net carrying amount of the old debt, including unamortized financing costs was approximately \$2,200,000 and is reported as a reduction in the new debt and amortized to operations through the year 2012.

BMH has the option to prepay the Series 1997 Bonds maturing on or after December 1, 2008 at a redemption price of 102% declining to 100% on December 1, 2009.

Future principal payments under the Hospital's long-term debt agreements are:

| Year Ending September 30, | <u>Principal</u>     | <u>Interest</u>     |
|---------------------------|----------------------|---------------------|
| 2009                      | \$ 1,415,000         | \$ 891,500          |
| 2010                      | 1,490,000            | 820,750             |
| 2011                      | 1,560,000            | 746,250             |
| 2012                      | 1,640,000            | 668,250             |
| 2013                      | 1,725,000            | 586,250             |
| 2014 to 2018              | <u>10,000,000</u>    | <u>1,548,500</u>    |
|                           | <u>\$ 17,830,000</u> | <u>\$ 5,261,500</u> |

The financing arrangements contain several covenants, the most restrictive of which requires the Hospital to maintain certain debt service coverage ratios. At September 30, 2008 and 2007, the Hospital was compliant with such financial covenants.

BMH has a line of credit in the amount of \$15,000,000 which bears interest at LIBOR plus 65 basis points 3.14% and 5.59% at September 30, 2008 and 2007, respectively. Borrowings against the line of credit totaled \$8,501,760 and \$6,955,142 for the years ended September 30, 2008 and 2007. The line of credit expires in October 2008.

Broad River has a line of credit in the amount of \$5,000,000 which bears interest at LIBOR plus 110 basis points 3.59% and 6.42% at September 30, 2008 and 2007, respectively. Borrowings against the line of credit totaled \$2,515,782 and \$3,125,625 for the years ended September 30, 2008 and 2007, respectively. The line of credit expires in January 2012.

10. **Professional Liability Insurance**

The Hospital purchases professional medical liability insurance with coverage up to \$300,000 per individual and an aggregate of \$600,000 on an occurrence basis. The coverage for physicians employed by the facility is \$1,200,000 per occurrence. Management believes that any pending claims or unasserted claims would be settled within the limits of coverage and is not aware of any potential claims not filed with the carrier as of September 30, 2008.

The laws of the state limit the amount that can be recovered from certain governmental medical facilities, including the Hospital, for damages for medical services rendered by the facility or the facility's employees to \$300,000 per individual and an aggregate of \$600,000 per occurrence and \$1,200,000 for physicians employed by the facility.

Insurance expense for professional medical liability coverage was approximately \$252,000 and \$230,000 in 2008 and 2007, respectively.

11. **Workers Compensation**

In 2006, the Hospital obtained commercial worker's compensation insurance subject to a deductible provision of \$100,000. The Hospital is responsible for all costs associated with each incident until the deductible limit is reached. The estimated accrual for identified claims and unreported but incurred claims was approximately \$95,000 and \$250,000 at September 30, 2008 and 2007, respectively.

12. **Retirement Plans**

The Hospital contributes to the South Carolina Retirement System ("SCRS"). SCRS is a cost-sharing multiple-employer defined benefit pension plan administered by South Carolina Retirement Systems, a Division of the State Budget and Control Board. The payroll for all Hospital employees was \$52,101,204 and \$49,916,897 respectively, for the years ended September 30, 2008 and 2007. The payroll for Hospital employees covered by the SCRS for the years ended September 30, 2008 and 2007 was \$33,128,287 and \$31,911,280, respectively or 64% of total Hospital payroll in both 2008 and 2007. The contribution from the Hospital for the years ended September 30, 2008 and 2007 was \$3,054,834 and \$2,698,549, respectively. The Hospital's 2008 and 2007 contributions represented less than 1% of total contributions to SCRS.

Under SCRS, employees who retire at or after age sixty-five (65) or have twenty eight (28) years of service are entitled to an annual retirement benefit, payable monthly for life equal

to 1.82% of their final compensation times years of credited service. Benefits are fully vested on reaching five (5) years of earned service. Vested employees may retire at or after age sixty (60) and receive reduced retirement benefits. SCRS also provides death and disability benefits. Benefits are established by state statute. A Comprehensive Annual Financial Report containing financial statements and required supplementary information of SCRS is issued and publicly available by writing the South Carolina Retirement System, P.O. Box 11960, Columbia, SC 29211-1960 or at [www.retirementsc.gov](http://www.retirementsc.gov).

The employee and employer contribution rates are actuarially determined for SCRS. Covered employees are required by state statute to contribute 6.5% of their total earnings. The Hospital is required to contribute 9.06% of earnable compensation. In addition, the Hospital is required by the same statute to contribute an additional .15% in both 2008 and 2007 for group life insurance coverage.

The accrued liability is a standardized disclosure measure of the actuarial present value of the projected benefits of each individual allocated on a level basis over the earnings or service of the individual between entry age and assumed exit age(s). The measure is intended to help users assess SCRS's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems. SCRS does not make separate measurements of assets and benefits payable for individual employers. The unfunded accrued liability at July 1, 2007, the most recent valuation date for retired and active members, determined through an actuarial valuation performed as of that date, was approximately \$10.2 billion. Ten-year historical trend information showing SCRS's progress in accumulating sufficient assets to pay benefits when due is presented in the June 30, 2008 Component Unit Comprehensive Annual Financial Report issued by the SCRS.

13. **Fair Value of Financial Instruments**

The carrying amount reported in the Organizations' combined balance sheet for cash and cash equivalents, short-term investments, assets limited as to use, accounts receivable, accounts payable, and accrued expenses approximates fair value. At September 30, 2008 and 2007, the approximate fair value based upon quoted market values of the Hospital's long-term debt was approximately \$18,085,000 and \$19,567,000, respectively.

14. **Commitments Under Noncancelable Operating Leases**

The Hospital leases certain equipment under operating leases, which expire over the next 9 years. Rent expense was approximately \$1,612,000 and \$1,077,000 for the years ended September 30, 2008 and 2007, respectively.

The Hospital has committed to lease approximately one-third of a medical office building for Hospital operations and has also agreed to lease any unused space remaining in the

building under a fifteen year master lease agreement commencing in October 2000. The Hospital has no annual contingent commitment based upon occupancy levels at September 30, 2008 and 2007.

At September 30, 2008, future minimum lease payments under the non-cancelable operating leases are as follows:

|            |                     |
|------------|---------------------|
| 2009       | \$ 1,487,577        |
| 2010       | 1,209,102           |
| 2011       | 1,175,780           |
| 2012       | 1,020,419           |
| 2013       | 962,578             |
| Thereafter | <u>2,107,885</u>    |
|            | <u>\$ 7,963,341</u> |

15. **Commitments and Contingencies**

In August 2008, the Hospital entered into a contract for approximately \$916,000 to renovate the Medical Services Building. As of September 30, 2008, the Hospital has paid approximately \$161,000. The renovation is expected to be completed in February of 2009.

The Hospital has also entered into contracts for approximately \$782,000 related to renovations at the Woundcare Facility and the HealthLink physical therapy program. As of September 30, 2008, the Hospital has paid approximately \$400,000. These renovations are expected to be completed during 2009.

Due to the short term nature of these projects, management has included the cost as of September 30, 2008 in buildings as reflected in Note 7.

16. **Litigation**

There is no litigation pending, or to the knowledge of management of the Hospital threatened, which if decided adversely to the Hospital would have a material adverse effect on the business operations, financial position or operations of the Hospital. Furthermore, there is no litigation pending, or to management's knowledge threatened, involving professional liability claims in which the amount sought by the plaintiff exceeds applicable professional liability or excess insurance policy coverage limits.

17. **Related Party Transactions**

The Hospital maintains one of its operating bank accounts at a bank in which a member of the Board of Trustees is part of the bank's management.

18. **Subsequent Event**

In October 2008, the Hospital extended their existing line of credit in the amount of \$15,000,000. The line of credit bears interest at LIBOR plus 65 basis points and expires in January 2009.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**

Combining Balance Sheet

September 30, 2008

| <u>Assets</u>  | <u>Beaufort</u>                          | <u>Broad River</u>  | <u>BMI</u>          | <u>Eliminations</u>   | <u>Combined</u>       |
|--|--|---------------------|---------------------|-----------------------|-----------------------|
| Current assets:  |  |                     |                     |                       |                       |
| Cash and cash equivalents  | \$ 28,194,957                            | \$ 442,007          | \$ -                | \$ -                  | \$ 28,636,964         |
| Short-term investments   | 44,378,800                               | -                   | -                   | -                     | 44,378,800            |
| Patient accounts receivable, net of allowance for<br>uncollectible accounts of \$8,619,795 | 16,616,163                               | -                   | -                   | -                     | 16,616,163            |
| Other accounts receivable  | 1,612,687                                | -                   | -                   | -                     | 1,612,687             |
| Physician receivable, current portion  | 130,270                                  | -                   | -                   | -                     | 130,270               |
| Inventories of drugs and supplies  | 2,700,770                                | -                   | -                   | -                     | 2,700,770             |
| Prepaid expenses   | 1,069,737                                | -                   | 138,244             | -                     | 1,207,981             |
| Total current assets   | <u>94,703,384</u>                        | <u>442,007</u>      | <u>138,244</u>      | <u>-</u>              | <u>95,283,635</u>     |
| Assets limited as to use   | 2,314,094                                | -                   | -                   | -                     | 2,314,094             |
| Investments  | -  | -                   | -                   | -                     | -                     |
| Long-term equity investments   | -  | 970,536             | -                   | -                     | 970,536               |
| Capital assets, net  | 69,427,977                               | 548                 | 3,200,720           | -                     | 72,629,245            |
| Physician receivable, less current portion   | 84,816                                   | -                   | -                   | -                     | 84,816                |
| Deferred financing costs, net  | 95,396                                   | -                   | -                   | -                     | 95,396                |
| Due from affiliate   | 2,366,414                                | 6,431,870           | -                   | (8,798,284)           | -                     |
| Total assets   | <u>\$ 168,992,081</u>                    | <u>\$ 7,844,961</u> | <u>\$ 3,338,964</u> | <u>\$ (8,798,284)</u> | <u>\$ 171,377,722</u> |
|  | <b><u>Liabilities and Net Assets</u></b> |                     |                     |                       |                       |
| Current liabilities:   |  |                     |                     |                       |                       |
| Current portion of long-term debt  | \$ 1,415,000                             | \$ -                | \$ -                | \$ -                  | \$ 1,415,000          |
| Bank credit lines  | 8,501,760                                | 2,515,782           | -                   | -                     | 11,017,542            |
| Accounts payable   | 4,309,087                                | 28,196              | -                   | -                     | 4,337,283             |
| Accrued liabilities  | 7,803,364                                | -                   | -                   | -                     | 7,803,364             |
| Due to affiliate   | 2,610,539                                | 2,366,414           | 3,821,331           | (8,798,284)           | -                     |
| Estimated third-party payor settlements  | 1,311,429                                | -                   | -                   | -                     | 1,311,429             |
| Total current liabilities  | <u>25,951,179</u>                        | <u>4,910,392</u>    | <u>3,821,331</u>    | <u>(8,798,284)</u>    | <u>25,884,618</u>     |
| Long-term debt, less current portion   | 15,721,840                               | -                   | -                   | -                     | 15,721,840            |
| Total liabilities  | <u>41,673,019</u>                        | <u>4,910,392</u>    | <u>3,821,331</u>    | <u>(8,798,284)</u>    | <u>41,606,458</u>     |
| Net assets:  |  |                     |                     |                       |                       |
| Invested in capital assets, net of related debt  | 43,884,773                               | -                   | -                   | -                     | 43,884,773            |
| Restricted:  |  |                     |                     |                       |                       |
| For debt service   | 2,314,094                                | -                   | -                   | -                     | 2,314,094             |
| Expendable for specific operating activities   | 481,152                                  | -                   | -                   | -                     | 481,152               |
| Unrestricted   | 80,639,043                               | 2,934,569           | (482,367)           | -                     | 83,091,245            |
| Total net assets   | <u>127,319,062</u>                       | <u>2,934,569</u>    | <u>(482,367)</u>    | <u>-</u>              | <u>129,771,264</u>    |
| Total liabilities and net assets   | <u>\$ 168,992,081</u>                    | <u>\$ 7,844,961</u> | <u>\$ 3,338,964</u> | <u>\$ (8,798,284)</u> | <u>\$ 171,377,722</u> |

See Independent Auditors' Report.

**BEAUFORT MEMORIAL HOSPITAL AND OTHER COMBINED ENTITY**

Combining Statement of Revenues, Expenses, and Changes in Net Assets

For the Year Ended September 30, 2008

|  | <u>Beaufort</u>              | <u>Broad River</u>         | <u>BMI</u>                 | <u>Eliminations</u> | <u>Combined</u>              |
|--|------------------------------|----------------------------|----------------------------|---------------------|------------------------------|
| Operating revenues:  |                              |                            |                            |                     |                              |
| Net patient service revenue, net of provision for<br>bad debts of \$15,424,973     | \$ 127,811,525               | \$ -                       | \$ -                       | \$ -                | \$ 127,811,525               |
| Other operating revenue  | <u>2,187,866</u>             | <u>215,075</u>             | <u>385,200</u>             | <u>(600,275)</u>    | <u>2,187,866</u>             |
| Total operating revenues   | <u>129,999,391</u>           | <u>215,075</u>             | <u>385,200</u>             | <u>(600,275)</u>    | <u>129,999,391</u>           |
| Operating expenses:  |                              |                            |                            |                     |                              |
| Salaries and wages   | 52,101,204                   | -                          | -                          | -                   | 52,101,204                   |
| Employee benefits  | 13,937,448                   | -                          | -                          | -                   | 13,937,448                   |
| Contract labor   | 3,803,936                    | -                          | 128,218                    | -                   | 3,932,154                    |
| Supplies   | 23,661,129                   | 184                        | -                          | -                   | 23,661,313                   |
| Purchased services   | 9,146,925                    | 215,075                    | -                          | (600,275)           | 8,761,725                    |
| Physician fees   | 2,724,206                    | -                          | -                          | -                   | 2,724,206                    |
| Depreciation and amortization  | 8,150,706                    | -                          | 503,292                    | -                   | 8,653,998                    |
| Other  | <u>10,503,736</u>            | <u>16,278</u>              | <u>-</u>                   | <u>-</u>            | <u>10,520,014</u>            |
| Total operating expenses   | <u>124,029,290</u>           | <u>231,537</u>             | <u>631,510</u>             | <u>(600,275)</u>    | <u>124,292,062</u>           |
| Operating income (loss)  | <u>5,970,101</u>             | <u>(16,462)</u>            | <u>(246,310)</u>           | <u>-</u>            | <u>5,707,329</u>             |
| Nonoperating revenues (expenses):  |                              |                            |                            |                     |                              |
| Investment income  | 3,068,568                    | -                          | -                          | -                   | 3,068,568                    |
| Interest expense   | (1,229,501)                  | (385)                      | (129,394)                  | -                   | (1,359,280)                  |
| Loss on disposal of capital assets   | (812,487)                    | -                          | -                          | -                   | (812,487)                    |
| Share of income of investees, net  | -                            | 985,245                    | -                          | -                   | 985,245                      |
| County apportionment   | 643,382                      | -                          | -                          | -                   | 643,382                      |
| Noncapital gifts and bequests  | <u>626,011</u>               | <u>-</u>                   | <u>-</u>                   | <u>-</u>            | <u>626,011</u>               |
| Total nonoperating revenues (expenses)   | <u>2,295,973</u>             | <u>984,860</u>             | <u>(129,394)</u>           | <u>-</u>            | <u>3,151,439</u>             |
| Excess (deficit) of revenues over expenses before capital grants and contributions | 8,266,074                    | 968,398                    | (375,704)                  | -                   | 8,858,768                    |
| Capital grants and contributions   | <u>633,757</u>               | <u>-</u>                   | <u>-</u>                   | <u>-</u>            | <u>633,757</u>               |
| Increase (decrease) in net assets  | 8,899,831                    | 968,398                    | (375,704)                  | -                   | 9,492,525                    |
| Net assets, beginning of year  | <u>118,419,231</u>           | <u>1,966,171</u>           | <u>(106,663)</u>           | <u>-</u>            | <u>120,278,739</u>           |
| Net assets, end of year  | \$ <u><u>127,319,062</u></u> | \$ <u><u>2,934,569</u></u> | \$ <u><u>(482,367)</u></u> | \$ <u><u>-</u></u>  | \$ <u><u>129,771,264</u></u> |

See Independent Auditors' Report.