

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Basic Financial Statements**  
June 30, 2005 and 2004

**Together with Independent Auditor's Report**

# LAKES REGIONAL HEALTHCARE

## Spirit Lake, Iowa

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**LAKES REGIONAL HEALTHCARE**  
**Spirit Lake, Iowa**

**OFFICIALS**

**June 30, 2005**

<b><u>Board of Trustees</u></b>	<b><u>Address</u></b>	<b><u>Term Expires</u></b>
Ivan Brown, Chairman	Spirit Lake, Iowa	December 2006
Gary Moeller, Vice-Chairman	Milford, Iowa	December 2006
Doug Dingel, Secretary/Treasurer	Terril, Iowa	December 2008
Marc Jacobsen	Arnolds Park, Iowa	December 2008
Mark Fisher	Milford, Iowa	December 2010
Deb Goetzinger	Spirit Lake, Iowa	December 2008
Denny Perry	Spirit Lake, Iowa	December 2010
<b><u>Chief Executive Officer</u></b>		
Richard Kielman	Okoboji, Iowa	Indefinite
<b><u>Chief Financial Officer</u></b>		
Gordon Larson	Spirit Lake, Iowa	Indefinite



SEIM  
JOHNSON  
SESTAK &  
QUIST, LLP

CONSULTANTS  
& ACCOUNTANTS

## Independent Auditor's Report

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Clifford C. Huntington, CPA  
Roger E. Howard, CPA  
Roger E. Thompson, CPA  
Tom H. Schnack, CPA  
Daniel L. Hassel, CPA  
Dennis K. Grindle, CPA  
Dennis R. Hein, CPA  
Brent T. Frieauf, CPA  
Barbara J. Fajen, CPA  
Brian D. Green, CPA

To the Board of Trustees  
Lakes Regional Healthcare  
Spirit Lake, Iowa:

We have audited the accompanying basic financial statements of LAKES REGIONAL HEALTHCARE as of and for the years ended June 30, 2005 and 2004, as listed in the table of contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lakes Regional Healthcare as of June 30, 2005 and 2004, and the results of its operations, changes in fund balances and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated August 26, 2005 on our consideration of Lakes Regional Healthcare's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of the report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Management's Discussion and Analysis and Budgetary Comparison Information on pages 3 through 7 and page 25 are not required parts of the basic financial statements but are supplementary information required by the Government 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.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The other supplementary information, included in Exhibits 1 through 7, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Seim, Johnson, Sestak & Quist, LLP*

Omaha, Nebraska,  
August 26, 2005.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Management's Discussion and Analysis**  
**June 30, 2005 and 2004**

This discussion and analysis of Lakes Regional Healthcare's (LRH) financial performance provides an overview of financial activities for the fiscal years ended June 30, 2005 and 2004. This discussion and analysis should be read in conjunction with financial statements, which begin on page 8.

## **Financial Highlights**

- LRH net assets increased in 2005 by \$1,453,126 or 5.1%. In 2004, net assets increased by \$1,582,547 or 5.9%.
- LRH reported operating income in 2005 of \$955,511 compared to \$1,248,615 in 2004, a decrease of 23.4%.
- LRH non-operating revenue increased by \$174,478 in 2005 compared to 2004.

## **Using This Annual Report**

LRH financial statements consist of three statements—a Balance Sheet; a Statement of Revenue, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of LRH, including resources held by LRH but restricted for specific purposes by contributors, grantors, or enabling legislation.

### **The Balance Sheet and Statement of Revenue, Expenses, and Changes in Net Assets**

Analysis of LRH finances begins on page 8. The Balance Sheet and the Statement of Revenue, Expenses, and Changes in Net Assets report information about LRH resources and activities in a way that helps answer the question of whether LRH, as a whole, is better or worse off as a result of the year's activities. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report LRH net assets and changes in them. Over time, increases or decreases in net assets are an indicator of whether its financial health is improving or deteriorating. To access the overall health of LRH, non-financial factors, such as changes in the patient base of LRH and measures of the quality of service it provides to the community, as well as local economic factors, need to be considered.

### **The Statement of Cash Flows**

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It shows where cash came from and what the cash was used for. It also provides the change in cash balance during the reporting period.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Management's Discussion and Analysis**  
June 30, 2005 and 2004

**Net Assets**

LRH net assets are the difference between assets and liabilities reported in the Balance Sheet on page 8. LRH net assets increased this past year by \$1,453,126 or 5.1% in 2005, as shown in **Table 1**.

*Table 1: Assets, Liabilities, and Net Assets*

	<u>2005</u>	<u>2004</u>	<u>Change from Prior Year</u>	<u>% Change</u>
<b>Assets:</b>				
Current assets	\$ 17,656,152	17,579,059	77,093	0.4%
Capital assets, net	17,762,007	15,797,826	1,964,181	12.4%
Other non-current assets	2,917,833	4,369,409	(1,451,576)	(33.2%)
<b>Total assets</b>	<b><u>38,335,992</u></b>	<b><u>37,746,294</u></b>	<b><u>589,698</u></b>	<b><u>1.5%</u></b>
<b>Liabilities:</b>				
Long-term debt outstanding	5,885,000	6,450,000	(565,000)	(8.7%)
Other current and noncurrent liabilities	2,803,931	3,102,359	(298,428)	(9.6%)
<b>Total liabilities</b>	<b><u>8,688,931</u></b>	<b><u>9,552,359</u></b>	<b><u>(863,428)</u></b>	<b><u>(9.0%)</u></b>
<b>Net assets:</b>				
Invested in capital assets, net of related debt	11,312,007	8,807,826	2,504,181	28.4%
Restricted for debt service	107,823	646,143	(538,320)	(83.3%)
Restricted expendable net assets	552,750	2,099,185	(1,546,435)	(73.6%)
Restricted nonexpendable net assets	25,000	25,000	--	.0%
Unrestricted	17,649,481	16,615,781	1,033,700	6.2%
<b>Total net assets</b>	<b><u>\$ 29,647,061</u></b>	<b><u>28,193,935</u></b>	<b><u>1,453,126</u></b>	<b><u>5.1%</u></b>

A component of the change in LRH assets in 2005 is the increase in patient accounts receivable. While net patient service revenue increased by \$1,227,260 or 6.0%, patient accounts receivable, net of estimated uncollectible amounts, increased by \$827,591. In 2004 compared to 2003, patient service revenue increased by \$1,640,162 while receivables decreased by \$884,381. The increase in receivables in 2005 is primarily the result of reduced collections and implementation of new payment procedures for some payors, such as Iowa Medicaid.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Management's Discussion and Analysis**  
June 30, 2005 and 2004

**Operating Results and Changes in LRH Net Assets**

In 2005, LRH net assets increased by \$1,453,126 or 5.2%, as shown in Table 2. This increase is made up of several different components.

*Table 2: Condensed Statements of Revenue, Expenses and Changes in Net Assets*

	<u>2005</u>	<u>2004</u>	<u>Change from Prior Year</u>	<u>Percent Change</u>
<b>Operating Revenue:</b>				
Net patient service revenue	\$ 21,543,142	20,315,882	1,227,260	6.0%
Provision for bad debt	(625,000)	(600,000)	(25,000)	(4.1%)
Other operating revenue	476,160	492,337	(16,177)	(3.2%)
<b>Total operating revenue</b>	<b>21,394,302</b>	<b>20,208,219</b>	<b>1,186,083</b>	<b>5.8%</b>
<b>Operating Expenses:</b>				
Salaries and benefits	10,042,325	9,404,469	637,857	6.7%
Purchased services and other	7,965,991	7,509,156	456,835	6.0%
Depreciation and amortization	2,152,529	1,930,784	221,745	11.4%
Interest	277,945	115,195	162,750	141.2%
<b>Total operating expenses</b>	<b>20,438,790</b>	<b>18,959,604</b>	<b>1,479,187</b>	<b>7.8%</b>
<b>Operating income</b>	<b>955,512</b>	<b>1,248,615</b>	<b>(293,104)</b>	<b>(23.4%)</b>
<b>Non-operating Revenue and Expenses</b>				
County tax revenue	102,996	102,996	--	--
Investment income	401,680	310,184	91,496	29.4%
Non-capital grants and contributions	35,364	28,016	7,348	26.2%
Other non-operating revenues and expenses, net	(42,425)	(107,264)	64,839	(60.4%)
<b>Total non-operating revenue (expenses), net</b>	<b>497,615</b>	<b>333,932</b>	<b>163,683</b>	<b>49.0%</b>
<b>Increase in net assets</b>	<b>1,453,126</b>	<b>1,582,547</b>	<b>(129,421)</b>	<b>(8.2%)</b>
<b>Net assets beginning of year</b>	<b>28,193,935</b>	<b>26,611,388</b>	<b>1,582,547</b>	<b>5.9%</b>
<b>Net assets end of year</b>	<b>\$ 29,647,061</b>	<b>28,193,935</b>	<b>1,453,126</b>	<b>5.2%</b>

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Management's Discussion and Analysis**  
June 30, 2005 and 2004

**Operating Income**

The first component of the overall change in LRH net assets is its operating income —generally, the difference between net patient service revenues and the expenses incurred to perform those services. In each of the past two years, LRH has reported an operating income. This is consistent with the last 13 years of operating history.

The primary components affecting operating income are:

- Increased patient days of 217 or 4.2% in 2005 and 182 or 2.7% in 2004.
- Increased outpatient revenue, \$2,609,401 or 14.0% in 2005 and \$1,339,400 or 7.7% in 2004. Increases in 2005 were due to increased volumes in many outpatient departments in conjunction with price changes. Increases in 2004 were due to increased volumes and price changes.
- Increased salary and benefit costs for employees of \$637,857 or 6.7% in 2005 and \$523,008 or 5.9% in 2004.
- Increased medical supply and drug costs of \$170,257 or 3.5% in 2005 and of \$718,858 or 17.6% in 2004.
- Increased net patient service revenues in 2005 primarily because of increased patient volumes and increased charges, similar to changes seen in 2004.

The rate of healthcare inflation has a direct impact on the cost of services provided by LRH. A component of LRH costs are expenses for medical supplies and prescription drugs. In 2005 medical supplies and prescription drug costs totaled \$4,960,499. In 2004 medical supplies and prescription drug costs totaled \$4,790,242. Some of the major factors contributing to increased medical supply and drug costs include the introduction of new drugs that cannot be obtained in generic form and changes in therapeutic mix.

LRH at times provides care for patients who have little or no health insurance or other means of repayment. The level of services provided to these patients increased by \$144,835 in 2005 compared to 2004. Because there is no expectation of repayment, charity care is not reported as patient service revenues of LRH.

**Non-operating Revenue and Expenses**

Non-operating revenue consist primarily of property taxes levied by LRH, interest revenue, and investment earnings. The county tax levy was at \$0.08993 per \$1,000 of valuation for 2005 and \$0.08920 in 2004.

**Cash Flows**

Changes in cash flows are consistent with changes in operating income and nonoperating revenue and expenses, discussed earlier. Cash flows provided by operating activities decreased in 2005 due to capital purchases, including a construction project that was completed.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Management's Discussion and Analysis**  
June 30, 2005 and 2004

## **Capital Asset and Debt Administration**

### **Capital Assets**

At the end of 2005, LRH had \$17,762,007 invested in capital assets, net of accumulated depreciation, as detailed in Note 5 to the financial statements. In 2005, the LRH purchased new equipment costing \$4,538,838. Slightly less, \$3,823,189 was spent to acquire new equipment in 2004. Both of these amounts are more than 2003, when LRH spent \$2,709,593 for new equipment.

### **Debt**

At year-end, the LRH had \$6,450,000 in capital loan notes outstanding. No new debt was issued in 2005 or 2004. The amount of debt issued is subject to limitations that apply to the County and its component units as a whole. There have been no changes in LRH debt ratings in the past two years.

### **Other Economic Factors**

The 2005 fiscal year provided LRH substantial challenges due federal program reimbursement requirements, pressures from other insurers, and the fluctuation of patient demand.

Inflation continued in 2005 with supply and equipment costs increasing at market rates and the pressure on nursing and other salary costs being driven by the shortage of supply of these health care professionals.

## **Contacting LRH Financial Management**

This financial report is designed to provide patients, suppliers, taxpayers, and creditors with a general overview of LRH finances. Questions about this report or requests for additional information should be directed to:

Gordon Larson  
Vice President and Chief Financial Officer  
Lakes Regional Healthcare  
Highway 71 South  
Spirit Lake, Iowa 51360  
712-336-8796

**LAKES REGIONAL HEALTHCARE**  
**Spirit Lake, Iowa**

**Balance Sheets**  
**June 30, 2005 and 2004**

<b>ASSETS</b>	<u><b>2005</b></u>	<u><b>2004</b></u>
Current assets:		
Cash and cash equivalents	\$ 3,246,090	8,085,257
Certificates of deposit	9,994,630	5,434,168
Assets limited as to use - required for current liabilities	107,823	646,143
Receivables -		
Patients, net of allowance for doubtful accounts of		
\$1,280,133 in 2005 and \$1,367,110 in 2004	3,448,569	2,620,978
Other	19,113	46,753
Inventories	659,702	633,858
Prepaid expenses	<u>180,225</u>	<u>111,902</u>
Total current assets	<u>17,656,152</u>	<u>17,579,059</u>
Assets limited as to use:		
By Board for -		
Capital improvements	403,330	394,661
Endowments	1,977,755	1,886,463
Under Public Hospital Revenue Capital Loan Notes Agreements	377,994	1,912,356
By Donor	<u>137,493</u>	<u>136,750</u>
	<u>2,896,572</u>	<u>4,330,230</u>
Capital assets, net of accumulated depreciation	<u>17,762,007</u>	<u>15,797,826</u>
Other assets, net	<u>21,261</u>	<u>39,179</u>
Total assets	\$ <u>38,335,992</u>	<u>37,746,294</u>

*See notes to financial statements*

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Balance Sheets**  
**June 30, 2005 and 2004**

<b>LIABILITIES AND NET ASSETS</b>	<u>2005</u>	<u>2004</u>
Current liabilities:		
Current portion of long-term debt	\$ 565,000	540,000
Accounts payable -		
Trade	347,507	443,741
Construction	184,119	599,387
Salaries, wages and accrued vacation payable	977,250	875,542
Payroll taxes withheld and accrued	87,779	82,113
Accrued interest payable	23,060	25,825
Other accrued liabilities	141,932	122,002
Deferred revenue - Mandelbaum Endowment	5,974	6,429
Estimated third-party payor settlements	<u>471,310</u>	<u>407,320</u>
Total current liabilities	2,803,931	3,102,359
Long-term debt, net of current portion	<u>5,885,000</u>	<u>6,450,000</u>
Total liabilities	<u>8,688,931</u>	<u>9,552,359</u>
Net assets:		
Invested in capital assets, net of related debt	11,312,007	8,807,826
Restricted -		
For capital acquisitions	377,994	1,912,356
For debt service	107,823	646,143
Expendable for capital acquisitions & operating activities	174,756	186,829
Nonexpendable	25,000	25,000
Unrestricted	<u>17,649,481</u>	<u>16,615,781</u>
Total net assets	<u>29,647,061</u>	<u>28,193,935</u>
Total liabilities and net assets	<u>\$ 38,335,992</u>	<u>37,746,294</u>

*See notes to financial statements*

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Statements of Revenue, Expenses and Changes in Net Assets**  
**For the Years Ended June 30, 2005 and 2004**

	<b>2005</b>	<b>2004</b>
<b>OPERATING REVENUE:</b>		
Net patient service revenue before provision for bad debt	\$ 21,543,142	20,315,882
Provision for bad debt	<u>(625,000)</u>	<u>(600,000)</u>
Net patient service revenue	20,918,142	19,715,882
Other revenue	<u>476,160</u>	<u>492,337</u>
Total revenue	<u>21,394,302</u>	<u>20,208,219</u>
<b>OPERATING EXPENSES:</b>		
Salaries	7,879,837	7,397,830
Employee benefits	2,162,488	2,006,639
Purchased services and professional fees	2,333,872	2,132,943
Utilities	500,309	433,505
Supplies and other expenses	4,960,499	4,790,242
Depreciation and amortization	2,152,529	1,930,784
Insurance	171,311	152,466
Interest	<u>277,945</u>	<u>115,195</u>
Total expenses	<u>20,438,790</u>	<u>18,959,604</u>
<b>OPERATING INCOME</b>	<u>955,512</u>	<u>1,248,615</u>
<b>NONOPERATING REVENUE, NET:</b>		
Investment income	401,680	310,184
County tax revenue	102,996	102,996
Unrestricted gifts, grants and bequests	35,364	28,016
Loss on disposal of property and equipment	<u>(30,353)</u>	<u>(105,987)</u>
Nonoperating revenue, net	<u>509,687</u>	<u>335,209</u>
<b>EXCESS REVENUE OVER EXPENSES BEFORE GRANTS AND CONTRIBUTIONS</b>	1,465,199	1,583,824
<b>GRANTS AND CONTRIBUTIONS, NET</b>	<u>(12,073)</u>	<u>(1,277)</u>
<b>INCREASE IN NET ASSETS</b>	1,453,126	1,582,547
<b>NET ASSETS, beginning of year</b>	<u>28,193,935</u>	<u>26,611,388</u>
<b>NET ASSETS, end of year</b>	<u>\$ 29,647,061</u>	<u>28,193,935</u>

*See notes to financial statements*

**LAKES REGIONAL HEALTHCARE**  
**Spirit Lake, Iowa**

**Statements of Cash Flows**  
**For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Cash received from patients and third party payors	\$ 20,154,541	20,567,615
Cash paid to employees for salaries and benefits	(9,934,951)	(9,337,445)
Cash paid to suppliers and contractors	(8,136,462)	(7,533,927)
Other receipts and payments, net	<u>490,984</u>	<u>522,563</u>
Net cash provided by operating activities	<u>2,574,112</u>	<u>4,218,806</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>		
County taxes received	102,996	102,996
Unrestricted gifts, grants and bequests	<u>35,364</u>	<u>28,016</u>
Net cash provided by noncapital financing activities	<u>138,360</u>	<u>131,012</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Purchase of property and equipment, net	(4,538,838)	(3,823,189)
Payments on long-term debt	(540,000)	(515,000)
Interest paid on long-term debt	<u>(314,551)</u>	<u>(337,724)</u>
Net cash used in capital and related financing activities	<u>(5,393,389)</u>	<u>(4,675,913)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Withdrawals from assets limited as to use, net	1,972,721	3,035,902
Deposits to short-term investments	(4,560,462)	(1,744,863)
Interest on investments	<u>429,491</u>	<u>391,029</u>
Net cash provided by (used in) investing activities	<u>(2,158,250)</u>	<u>1,682,068</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>(4,839,167)</b>	<b>1,355,973</b>
<b>CASH AND CASH EQUIVALENTS - Beginning of year</b>	<u><b>8,085,257</b></u>	<u><b>6,729,284</b></u>
<b>CASH AND CASH EQUIVALENTS - End of year</b>	<b>\$ <u>3,246,090</u></b>	<u><b>8,085,257</b></u>

*See notes to financial statements*

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Statements of Cash Flows**  
**For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ 955,512	1,248,615
Adjustments to reconcile operating income to net cash provided by operating activities -		
Depreciation and amortization	2,152,529	1,930,784
Interest expense	277,945	115,195
(Increase) decrease in current assets -		
Receivables -		
Patients	(827,591)	884,381
Other	27,640	26,633
Inventories	(25,844)	(25,957)
Prepaid expenses	(68,323)	(50,156)
Estimated third-party payor settlements	--	(439,968)
Increase (decrease) in current liabilities -		
Accounts payable	(96,234)	67,934
Due to restricted funds	(12,816)	3,593
Salaries, wages and accrued vacation payable	101,708	59,526
Payroll taxes withheld and accrued	5,666	7,498
Other accrued liabilities	19,930	(16,592)
Estimated third-party payor settlements	<u>63,990</u>	<u>407,320</u>
Net cash provided by operating activities	\$ <u>2,574,112</u>	<u>4,218,806</u>

*See notes to financial statements*

# LAKES REGIONAL HEALTHCARE

## Spirit Lake, Iowa

### Notes to Financial Statements June 30, 2005 and 2004

#### (1) Description of Reporting Entity and Summary of Significant Accounting Policies

The following describes the reporting entity and is a summary of significant accounting policies of Lakes Regional Healthcare (Hospital). These policies are in accordance with accounting principles generally accepted in the United States of America. The Hospital is a county public hospital organized under Chapter 347 of the Code of Iowa and governed by a seven member Board of Trustees elected for terms of six years.

##### A. *Reporting Entity*

For financial reporting purposes, the Hospital has included all funds, organizations, account groups, agencies, boards, commissions and authorities. The Hospital has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Hospital are such that exclusion would cause the Hospital's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Hospital to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Hospital. The Hospital has no component units which meet the Governmental Accounting Standards Board criteria.

##### B. *Industry Environment*

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursements for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Hospital is in compliance with government laws and regulations as they apply to the areas of fraud and abuse. While no regulatory inquiries have been made which are expected to have a material effect on the Hospital's financial statements, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

C. *Basis of Presentation*

The Balance Sheets display the Hospital's assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

*Invested in capital assets, net of related debt* consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt attributable to the acquisition, construction or improvement of those assets.

*Restricted net assets* result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

*Unrestricted net assets* consist of net assets not meeting the definition of the two preceding categories. Unrestricted net assets often have constraints on resources imposed by management which can be removed or modified.

When both restricted and unrestricted resources are available for use, generally it is the Hospital's policy to use restricted resources first.

D. *Measurement Focus and Basis of Accounting*

Basis of accounting refers to when revenue and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Revenue is recognized when earned and expenses are recorded when the liability is incurred.

In reporting the financial activity of its proprietary funds, the Hospital applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

E. *Use of Estimates*

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

F. *Cash and Cash Equivalents*

Cash and cash equivalents for purposes of the statements of cash flows include investments in highly liquid debt instruments with original maturities of three months or less, excluding amounts limited as to use by donor and bond indenture agreements.

G. *Patient Receivables*

Patient receivables are uncollateralized customer and third-party payor obligations. Unpaid patient receivables are not assessed interest.

Payments of patient receivables are allocated to the specific claim identified on the remittance advice or, if unspecified, are applied to the earliest unpaid claim.

The carrying amount of patient receivables is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected from patients and third-party payors. Management reviews patient receivables by payor class and applies percentages to determine estimated amounts that will not be collected from third parties under contractual agreements and amounts that will not be collected from patients due to bad debts. Management considers historical write off and recovery information in determining the estimated bad debt provision.

H. *Assets Limited as to Use*

*By Board of Trustees* - Periodically, the Hospital's Board of Trustees has set aside assets for future capital improvements, endowments and employee health insurance claims. The Board retains control over these assets and may, at its discretion, subsequently use them for other purposes.

*Under Public Hospital Revenue Capital Loan Notes Agreements* - These funds are used for the payment of principal and interest on the notes and to provide funds for the construction of additions to and remodeling of the existing Hospital facilities.

*By Donor* - These funds are restricted for specified purposes as directed by the grantor or donor.

I. *Restricted Assets*

Restricted assets consist primarily of funds designated by the donor or grantor for specified purposes.

J. *Capital Assets*

Capital asset acquisitions in excess of \$1,500 are capitalized and recorded at cost. Depreciation is provided over the estimated life of each depreciable asset and is computed using the straight-line method.

Useful lives are determined using guidelines from the American Hospital Association Guide for Estimated Useful Lives of Depreciable Hospital Assets. Lives range by capital asset classification as follows:

Land improvements	10 to 50 years
Buildings and building improvements	10 to 50 years
Equipment, computers, and furniture	3 to 25 years

K. *Bond Financing Costs*

Bond financing costs related to the issuance of the Public Hospital Revenue Capital Loan Notes are included with other assets in the balance sheet and are being amortized over the life of the related notes on a straight-line basis. Amortization expense of \$1,250 and \$1,251 for 2005 and 2004, respectively, is included in the accompanying statements of revenues, expenses and changes in net assets.

L. *Compensated Absences*

Sick leave does not vest and is accounted for as an expenditure or an expense when it is paid. Vacation leave vests and may be carried forward by an employee in an amount not to exceed 480 hours. Vacation expense is accrued as an expense and a liability as it is earned. Vacation leave expenditures are recognized to the extent it is paid during the year and the vested amount is recorded as a current liability. Accrued vacation leave payable at June 30, 2005 and 2004 was \$576,563 and \$524,222, respectively.

M. *Statement of Revenue, Expenses and Changes in Net Assets*

For purposes of display, transactions deemed by management to be on-going, major or central to the provision of health care services are reported as operating revenue and expenses. Peripheral or incidental transactions are reported as nonoperating revenue and expenses.

N. *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. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

O. *Grants and Contributions*

From time to time, the Hospital receives grants and contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) 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 are reported as nonoperating revenues. Amounts restricted to capital acquisitions or that are restricted to a specific operating purpose are reported after nonoperating revenues and expenses.

P. *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. Revenue from services to these patients is automatically recorded in the accounting system at the established rates, but the Hospital does not pursue collection of the amounts. The resulting adjustments are recorded as adjustments to patient service revenue at the time of the charity determination.

Q. *County Tax Revenue*

Taxes are included in nonoperating gains when received and distributed by the County Treasurer. No provision is made in the financial statements for taxes levied in the current year to be collected in a subsequent year.

R. *2004 Financial Statements*

Certain amounts in the 2004 financial statements have been reclassified to conform to the 2005 reporting format.

**(2) Cash and Investments**

The Hospital's deposits in banks at June 30, 2005 and 2004 were entirely covered by federal depository insurance or the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Hospital is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentality's; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Trustees; prime eligible bankers acceptances; certain high-rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; and certain joint investment trusts, and warrants or improvement certificates of a drainage district.

The Hospital's investments are categorized to give an indication of the level of risk assumed by the Hospital at year end. The Hospital's investments are all category 1 which means that the investments are insured or registered or the securities are held by the Hospital or its agent in the Hospital's name. The Hospital had no investments as defined by Government Accounting Standards Board Statement 3 at June 30, 2005 and 2004.

(3) **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 payment 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 paid based on ambulatory payment classifications or fee schedule amounts. Home health services are paid at prospectively determined rates per episode of care. 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 classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Hospital. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2003.

**Medicaid.** Inpatient acute services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. Outpatient services related to Medicaid beneficiaries are paid based on ambulatory patient groups or fee schedule amounts.

The Hospital has also entered into payment agreements with certain commercial insurance carriers. The basis for payment to the Hospital under these agreements primarily includes discounts from established charges.

(4) **Assets Limited as to Use**

*By Board*

Cash deposits and certificates of deposit designated by the Board for future capital improvements, endowments and employee health insurance claims as of June 30, 2005 and 2004, are summarized as follows:

	<u>2005</u>	<u>2004</u>
Capital Improvements -		
Cash	\$ 21,316	394,661
Certificates of deposit	380,066	--
Interest receivable	<u>1,948</u>	<u>--</u>
	<u>\$ 403,330</u>	<u>394,661</u>
Endowments -		
Cash	\$ 19,399	4,263
Certificates of deposit	1,940,082	1,874,948
Interest receivable	<u>18,274</u>	<u>7,252</u>
	<u>\$ 1,977,755</u>	<u>1,886,463</u>

*Hospital Revenue Capital Loan Notes Agreements -*

In connection with the issuance of Lakes Regional Healthcare Revenue Capital Loan Notes, Series 2002, the Hospital is required to maintain the following funds:

*Bond Fund* – Established for the monthly deposit by the Hospital of 1/12<sup>th</sup> of the next annual principal payment and 1/6<sup>th</sup> of the next semi-annual interest payment (Series 2002).

*Project Fund* – Established from the proceeds of the Revenue Capital Loan Notes, Series 2002, to provide funds for the construction of additions to and remodeling of the existing Hospital facilities.

The amounts segregated as of June 30, 2005 and 2004 are as follows:

	<u>2005</u>	<u>2004</u>
Bond Fund, cash	\$ <u>107,823</u>	<u>646,143</u>
Project Fund -		
Cash and certificate of deposits	\$ 377,965	1,912,111
Interest receivable	<u>29</u>	<u>245</u>
	<u>\$ 377,994</u>	<u>1,912,356</u>

*By Donor –*

The Mandelbaum Endowment Fund consists of a bequest of \$25,000 received in June 1988. The principal amount of \$25,000 is to remain intact with the interest earned to be used for nurse training.

The Hospital Auxiliary conducts various projects to raise funds which are used to satisfy needs of the Hospital as determined by its executive Board and the Hospital Board of Trustees.

The amounts segregated as of June 30, 2005 and 2004 are as follows:

	<u>2005</u>	<u>2004</u>
Mandelbaum Endowment fund		
Certificate of deposit	\$ 25,000	25,000
Hospital auxiliary assets, primarily cash and temporary cash investments	<u>112,493</u>	<u>111,750</u>
	<u>\$ 137,493</u>	<u>136,750</u>

(5) Capital Assets

Capital assets activity for the years ended June 30, 2005 and 2004 were as follows:

	June 30, 2004	Additions	Transfers and Disposals	June 30, 2005
Capital assets, not being depreciated:				
Land	\$ 162,552	417,500	--	580,052
Construction in progress	432,779	1,298,065	(1,043,417)	687,427
Total capital assets, not being depreciated	<u>595,331</u>	<u>1,715,565</u>	<u>(1,043,417)</u>	<u>1,267,479</u>
Capital assets, being depreciated:				
Land improvements	424,338	60,113	20,000	504,451
Hospital buildings	13,112,164	136,838	937,928	14,186,930
Medical Office building	3,186,447	48,013	--	3,234,460
Fixed equipment	3,152,074	53,599	--	3,205,673
Major moveable equipment	9,340,811	2,125,748	(80,119)	11,386,440
Total capital assets, being depreciated	<u>29,215,834</u>	<u>2,424,311</u>	<u>877,809</u>	<u>32,517,954</u>
Less accumulated depreciation:				
Land improvements	171,733	26,114	--	197,847
Hospital buildings	3,934,431	538,897	--	4,473,328
Medical Office building	1,258,062	138,028	--	1,396,090
Fixed equipment	2,303,285	320,020	--	2,623,305
Major moveable equipment	6,345,828	1,126,554	(139,526)	7,332,856
Total accumulated depreciation	<u>14,013,339</u>	<u>2,149,613</u>	<u>(139,526)</u>	<u>16,023,426</u>
Total capital assets, being depreciated, net	<u>15,202,495</u>	<u>274,698</u>	<u>1,017,335</u>	<u>16,494,528</u>
Total capital assets, net	<u>\$ 15,797,826</u>	<u>1,990,263</u>	<u>(26,082)</u>	<u>17,762,007</u>
	June 30, 2003	Additions	Transfers and Disposals	June 30, 2004
Capital assets, not being depreciated:				
Land	\$ 162,552	--	--	162,552
Construction in progress	2,281,481	3,326,573	(5,175,275)	432,779
Total capital assets, not being depreciated	<u>2,444,033</u>	<u>3,326,573</u>	<u>(5,175,275)</u>	<u>595,331</u>
Capital assets, being depreciated:				
Land improvements	234,275	7,773	182,290	424,338
Hospital buildings	8,383,980	88,711	4,639,473	13,112,164
Medical Office building	3,184,500	1,947	--	3,186,447
Fixed equipment	3,249,452	--	(97,378)	3,152,074
Major moveable equipment	8,669,096	803,029	(131,314)	9,340,811
Total capital assets, being depreciated	<u>23,721,303</u>	<u>901,460</u>	<u>4,593,071</u>	<u>29,215,834</u>
Less accumulated depreciation:				
Land improvements	151,455	20,278	--	171,733
Hospital buildings	3,554,623	379,808	--	3,934,431
Medical Office building	1,120,782	137,280	--	1,258,062
Fixed equipment	2,060,672	338,884	(96,271)	2,303,285
Major moveable equipment	5,535,644	1,051,616	(241,432)	6,345,828
Total accumulated depreciation	<u>12,423,176</u>	<u>1,927,866</u>	<u>(337,703)</u>	<u>14,013,339</u>
Total capital assets, being depreciated, net	<u>11,298,127</u>	<u>(1,026,406)</u>	<u>4,930,774</u>	<u>15,202,495</u>
Total capital assets, net	<u>\$ 13,742,160</u>	<u>2,300,167</u>	<u>(244,501)</u>	<u>15,797,826</u>

Construction work in process includes costs of various projects for the Hospital related to the construction of additions to and remodeling of the existing facilities. Construction work in process at year end includes an addition to the building leased by Lakes Family Practice and costs associated with the installation of a new information technology system. The Family Practice addition is nearly complete and estimated costs to complete the IT system are \$1,600,000, with completion expected during fiscal year ending June 30, 2006. These projects will be funded primarily from cash and cash equivalents. The composition of construction work in process at June 30, 2005 and 2004 is as follows:

	<u>2005</u>	<u>2004</u>
Construction costs	\$ 480,253	401,759
Architect and engineering costs	42,211	2,557
Interest expense	--	7,814
Interest earned	--	(8,582)
Computer project	<u>164,963</u>	<u>29,231</u>
	<u>\$ 687,427</u>	<u>432,779</u>

**(6) Long-Term Debt**

Long-term debt activity of the Hospital as of June 30, 2005 and 2004 consisted of the following:

	<u>June 30, 2004</u>	<u>Borrowings</u>	<u>Payments</u>	<u>June 30, 2005</u>	<u>Due Within One Year</u>
Capital loan notes (A)	\$ <u>6,990,000</u>	<u>--</u>	<u>540,000</u>	<u>6,450,000</u>	<u>565,000</u>
	<u>June 30, 2003</u>	<u>Borrowings</u>	<u>Payments</u>	<u>June 30, 2004</u>	<u>Due Within One Year</u>
Capital loan notes (A)	\$ <u>7,505,000</u>	<u>--</u>	<u>515,000</u>	<u>6,990,000</u>	<u>540,000</u>

(A) On May 6, 2002, \$8,000,000 of Hospital Revenue Capital Loan Notes were issued by Lakes Regional Healthcare pursuant to the provisions of Chapter 331 and 347 of the Code of Iowa, as amended, and in conformity with a resolution of the Lakes Regional Healthcare Board of Trustees. The proceeds of the Notes will be used to retire the outstanding principal amount of Public Hospital Revenue Capital Loan Notes, Series 1993(B), and to provide funds for the construction of additions to and remodeling of the existing Hospital facilities. The interest rate on the notes is 4.50% and will reset on June 1 of the years 2007, 2012 and 2017 at the rate equal to the five-year United States Treasury Note Index plus .25%.

Annual debt service requirements related to the Notes assuming a 4.5% interest rate are as follows:

<u>Year</u>	<u>Interest Rates</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006	4.50	\$ 565,000	290,250	855,250
2007	4.50	590,000	264,826	854,826
2008	4.50	615,000	238,276	853,276
2009	4.50	245,000	210,600	455,600
2010	4.50	260,000	199,575	459,575
2011 - 2015	4.50	1,475,000	812,475	2,287,475
2016 – 2020	4.50	1,840,000	449,325	2,289,325
2021 – 2022	4.50	860,000	58,500	918,500
		<u>\$ 6,450,000</u>	<u>2,523,857</u>	<u>8,973,827</u>

Under the terms of the Notes Agreements, the Hospital is required to maintain certain funds which are included in the assets whose use is limited in the financial statements.

A summary of interest expense and investment income on borrowed funds during the years ended June 30, 2005 and 2004 follows:

	<u>2005</u>	<u>2004</u>
Interest cost:		
Capitalized	\$ 33,840	220,596
Expensed	277,945	115,195
	<u>\$ 311,785</u>	<u>335,791</u>
Investment income:		
Capitalized	\$ 28,266	80,798
Earned	2,588	--
	<u>\$ 30,854</u>	<u>80,798</u>

**(7) Professional Liability Insurance**

The Hospital carries a professional liability policy (including malpractice) providing coverage of \$1,000,000 for injuries per occurrence and \$3,000,000 aggregate coverage. In addition, the Hospital carries an umbrella policy which also provides \$2,000,000 per occurrence and aggregate coverage. These policies provide coverage on a claims-made basis covering only those claims which have occurred and are reported to the insurance company while the coverage is in force. In the event the Hospital should elect not to purchase insurance from the present carrier or the carrier should elect not to renew the policy, any unreported claims which occurred during the policy year may not be recoverable from the carrier.

**(8) Employee Retirement and Defined Benefit Pension Plan**

The Hospital contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by State statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa 50360-9117.

Plan members are required to contribute 3.70% of their annual salary and the Hospital is required to contribute 5.75% of annual covered payroll. Contribution requirements are established by State statute. The Hospital's contribution to IPERS for the years ended June 30, 2005, 2004 and 2003 were \$439,237, \$415,929 and \$388,701, respectively, equal to the required contributions for each year.

**(9) Rental Income**

The Hospital is the lessor of certain office space leased under various noncancelable operating leases through 2010. Rental income is recorded monthly as earned in other operating revenue. The future minimum rentals under these leases are as follows:

2006	\$	303,022
2007		210,123
2008		201,678
2009		201,678
2010		25,738

**(10) Contingencies**

The Hospital is involved in litigation arising in the normal course of business. These claims are covered under policies of their previous insurance carrier. After consultation with legal counsel, management estimates these matters will be resolved without material adverse affect on the Hospital's future financial position or results from operations.

**(11) Concentrations of Credit Risk**

The Hospital is located in Spirit Lake, Iowa. The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors was as follows:

	<u>2005</u>	<u>2004</u>
Medicare	32.1%	32.6%
Medicaid	5.5	3.7
Blue Cross	16.6	17.2
Other third-party payors	30.8	29.6
Private pay	15.0	16.9
	<u>100.0%</u>	<u>100.0%</u>

The Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. These risks are covered by commercial insurance purchased from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

**LAKES REGIONAL HEALTHCARE**  
**Spirit Lake, Iowa**

**Budgetary Comparison Schedule of Revenues, Expenses  
and Changes in Net Assets – Budget and Actual (Cash Basis)  
June 30, 2005 and 2004**

This budgetary comparison is presented as Required Supplementary Information in accordance with Governmental Accounting Standards Board Statement No. 41 for governments with significant budgetary prospective differences.

The Board of Trustees annually prepares and adopts a budget designating the amount necessary for the improvement and maintenance of the Hospital on the cash basis following required public notice and hearing in accordance with Chapters 24 and 347 of the Code of Iowa. The Board of Trustees certifies the approved budget to the appropriate county auditors. The budget may be amended during the year utilizing similar statutorily prescribed procedures. Formal and legal budgetary control is based on total expenditures.

The following is a reconciliation between reported amounts and cash disbursements and a comparison to budget:

	Actual	Accrual Adjustments	Actual	Budgeted Amounts		Variance
	Accrual Basis		Cash Basis	Original	Amended	Favorable (Unfavorable)
Estimated amount to be raised by taxation	\$ 102,996	-	102,996	101,045	101,045	1,951
Estimated other revenues / receipts	<u>21,788,921</u>	<u>(752,243)</u>	<u>21,036,678</u>	<u>21,507,355</u>	<u>21,507,355</u>	<u>(470,677)</u>
	21,891,917	(752,243)	21,139,674	21,608,400	21,608,400	(468,726)
Expenses / Disbursements	<u>20,438,791</u>	<u>3,026,012</u>	<u>23,464,803</u>	<u>20,592,305</u>	<u>23,430,549</u>	<u>(34,254)</u>
Net	1,453,126	(3,778,255)	(2,325,129)	1,016,095	(1,822,149)	\$ <u><u>(502,980)</u></u>
Balance beginning of year	<u>28,193,935</u>	<u>(9,723,630)</u>	<u>18,470,305</u>	<u>24,229,323</u>	<u>24,229,323</u>	
Balance end of year	\$ <u><u>29,647,061</u></u>	<u><u>(13,501,885)</u></u>	<u><u>16,145,176</u></u>	<u><u>25,245,418</u></u>	<u><u>22,407,174</u></u>	

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Patient Service Revenue**  
**For the Years Ended June 30, 2005 and 2004**

	2005			2004				
	Inpatient	Outpatient	Swing Bed	Total	Inpatient	Outpatient	Swing Bed	Total
<b>NURSING SERVICES:</b>								
Medical, surgical and obstetrics	\$ 2,565,621	--	--	2,565,621	2,429,367	--	--	2,429,367
Swing bed	--	--	359,932	359,932	--	--	431,588	431,588
Observation	58,632	254,103	--	312,735	47,957	246,644	--	294,601
Nursery	198,866	--	--	198,866	174,408	--	--	174,408
Coronary care	159,894	--	--	159,894	167,832	--	--	167,832
Telemetry	--	--	--	--	73,748	--	4,388	78,136
	<u>\$ 2,983,013</u>	<u>254,103</u>	<u>359,932</u>	<u>3,597,048</u>	<u>2,893,312</u>	<u>246,644</u>	<u>435,976</u>	<u>3,575,932</u>
<b>OTHER PROFESSIONAL SERVICES:</b>								
Operating and recovery rooms	1,852,983	3,832,097	1,369	5,686,449	1,599,445	3,490,896	7,439	5,097,780
Pharmacy	1,472,149	2,198,039	180,071	3,850,259	1,395,267	2,090,234	198,494	3,683,995
Central services and supply	2,416,026	1,182,579	2,974	3,601,579	2,347,614	1,100,614	10,185	3,458,413
Emergency and outpatient service	583,416	2,953,960	453	3,537,849	579,966	2,500,281	--	3,080,247
Laboratory	966,098	1,833,036	45,483	2,844,617	882,135	1,541,295	44,746	2,468,176
CT scanner	512,336	1,467,063	4,755	1,984,154	440,416	1,122,874	8,663	1,571,953
MRI	100,161	1,681,509	--	1,781,670	80,059	1,369,964	277,332	1,639,035
Respiratory therapy	1,290,995	96,680	240,106	1,627,781	1,291,152	70,551	8,603	1,011,747
Radiology	316,138	902,774	10,356	1,229,268	272,864	730,280	1,333	819,807
Anesthesiology	393,801	685,285	310	1,079,396	292,592	525,882	88,593	942,261
Physical therapy	176,185	726,881	81,248	984,314	164,403	689,265	--	850,549
Ambulance	38,320	927,153	--	965,473	37,349	813,200	--	518,075
Ultrasound	74,084	455,922	2,326	532,332	78,725	402,243	10,479	486,793
Intravenous therapy	334,700	176,173	8,166	519,039	322,249	185,347	--	518,075
Home Health	--	441,610	--	441,610	--	468,603	--	468,603
Electrocardiology	104,351	220,774	4,200	329,325	116,134	218,703	3,650	338,487
Blood	160,592	117,546	7,048	285,186	176,702	99,778	9,679	286,159
Nuclear medicine	31,993	250,629	1,418	284,040	16,009	142,313	924	159,246
Oncology	1,008	257,819	424	259,251	--	260,300	1,782	263,994
Public Health	--	254,527	--	254,527	--	214,990	--	214,990
Delivery and labor room	178,014	31,755	--	209,769	153,100	46,277	--	199,377
Hospice	184,536	--	--	184,536	214,115	--	--	214,115
Stress testing	6,172	83,791	--	89,953	5,869	92,668	--	98,537
Occupational therapy	13,104	55,554	18,899	87,557	13,257	28,076	17,983	59,316
Enterostomal therapy	16,945	53,845	7,790	78,580	8,110	20,875	4,665	33,650
Cardiac Rehab	--	76,118	204	76,322	306	132,779	--	133,085
Speech therapy	5,738	5,631	1,732	13,101	4,351	10,368	4,622	19,341
Electroencephalography	1,640	6,758	--	8,398	1,312	4,920	--	6,232
	<u>11,231,485</u>	<u>20,975,518</u>	<u>619,332</u>	<u>32,826,335</u>	<u>10,495,413</u>	<u>18,373,576</u>	<u>711,599</u>	<u>29,580,588</u>
<b>GROSS PATIENT SERVICE REVENUE</b>	<u>\$ 14,214,498</u>	<u>21,229,821</u>	<u>979,264</u>	<u>36,423,383</u>	<u>13,388,725</u>	<u>18,620,220</u>	<u>1,147,575</u>	<u>33,156,520</u>
<b>LESS:</b>								
Contractual allowances and other deductions, primarily Medicare and Medicaid				(14,555,891)				(12,655,323)
Charity care services and other discounts, based on charges forgone				(324,350)				(185,315)
<b>NET PATIENT SERVICE REVENUE BEFORE PROVISION FOR BAD DEBT</b>			\$	<u>21,543,142</u>				<u>20,315,882</u>
<b>PROVISION FOR BAD DEBT</b>				(625,000)				(600,000)
<b>NET PATIENT SERVICE REVENUE</b>			\$	<u>20,918,142</u>				<u>19,715,882</u>

**LAKES REGIONAL HEALTHCARE**  
**Spirit Lake, Iowa**

**Other Operating Revenue**  
**For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
Rental income	\$ 285,725	285,002
Meals sold	79,360	88,752
Lifeline	45,516	47,930
Meals on Wheels	40,625	47,363
Other	20,362	13,383
Dietary instruction	2,928	2,403
Medical records transcriptions	1,644	1,040
Home Health immunizations	-	3,714
Health screen	-	2,750
	<u>\$ 476,160</u>	<u>492,337</u>

LAKES REGIONAL HEALTHCARE  
Spirit Lake, Iowa

Departmental Expenses  
For the Years Ended June 30, 2005 and 2004

	2005				2004			
	Salaries and Wages	Professional Fees and Purchased Services	Supplies and Other	Total	Salaries and Wages	Professional Fees and Purchased Services	Supplies and Other	Total
<b>NURSING SERVICES:</b>								
Medical and surgical	\$ 1,631,004	1,393	134,394	1,766,791	1,627,918	2,594	122,807	1,753,319
Oncology	136,057	62	19,816	155,935	136,887	--	27,625	164,512
Coronary care	103,962	--	3,187	107,149	127,458	--	6,351	133,809
Nursery	57,691	--	1,407	59,098	52,231	--	2,321	54,552
Administration	293,894	--	19,237	313,131	130,085	--	676	130,761
	<u>\$ 2,222,608</u>	<u>1,455</u>	<u>178,041</u>	<u>2,402,104</u>	<u>2,074,579</u>	<u>2,594</u>	<u>159,780</u>	<u>2,236,953</u>
<b>OTHER PROFESSIONAL SERVICES:</b>								
Operating and recovery room	531,938	4,090	193,191	729,219	506,936	2,149	195,553	704,638
Emergency room	342,307	847,102	40,796	1,230,205	324,555	829,078	36,034	1,189,667
Pharmacy	171,659	1,971	1,210,489	1,384,119	163,663	2,232	1,130,436	1,296,351
Laboratory	369,378	86,777	258,553	714,708	341,457	72,943	258,221	672,621
Home Health	371,288	27,081	40,146	438,515	351,863	31,780	44,311	427,944
Ambulance	434,434	1,559	72,876	508,869	403,368	51	53,629	457,048
Radiology	199,316	7,743	89,232	286,291	196,572	5,555	102,773	306,900
Physical therapy	--	434,397	22,614	457,011	--	336,111	19,448	355,559
Medical records	254,861	15,235	26,144	296,240	240,641	14,850	24,310	279,801
Respiratory therapy	175,848	3,702	55,126	234,676	172,335	900	49,447	222,682
Electrocardiology	38,518	22,860	45,688	107,066	51,164	18,495	56,912	126,571
Public health	173,820	1,679	51,733	227,232	128,968	989	27,858	157,815
Same day surgery	141,523	--	12,134	153,657	138,971	--	16,066	155,039
Central services and supply	44,213	520	1,478,504	1,523,237	36,277	--	1,407,656	1,443,933
Hospice	46,691	42,177	38,351	127,219	51,792	71,379	40,882	164,053
Blood bank	--	103,144	16,802	119,946	--	104,848	15,978	120,826
Oncology	78,437	8,348	11,206	97,991	85,707	--	16,098	112,991
Anesthesiology	--	400	106,180	106,580	--	--	106,247	106,247
Ultrasound	70,566	8,093	15,931	94,590	62,857	7,424	23,777	94,058
CT scanner	17,970	2,195	16,724	36,889	56,817	--	22,756	79,573
Quality assurance	92,492	--	3,089	95,581	72,566	--	2,719	75,285
MRI	43,329	22,166	21,957	87,452	46,683	--	28,474	75,137
Nuclear medicine	--	112,895	--	112,895	--	70,774	--	70,774
Delivery and labor room	52,570	--	4,121	56,691	50,348	--	2,683	53,031
Social services	23,015	--	214	23,229	23,139	--	610	23,749
Stress testing	9,140	--	144	9,284	9,345	--	328	9,673
Speech therapy	--	10,842	--	10,842	--	8,241	--	8,241
Entero-stomal therapy	--	15,975	--	15,975	--	7,175	--	7,175
Electroencephatography	649	2,053	30	2,732	780	--	67	2,910
Library	--	--	1,005	1,005	--	--	421	421
	<u>\$ 3,743,962</u>	<u>1,783,004</u>	<u>3,832,980</u>	<u>9,359,946</u>	<u>3,518,794</u>	<u>1,597,823</u>	<u>3,683,696</u>	<u>8,800,313</u>
<b>GENERAL SERVICES:</b>								
Plant operation and maintenance	\$ 172,474	123,871	607,306	903,651	187,539	88,377	572,303	848,219
Dietary	274,416	3,716	287,527	565,659	270,455	1,003	284,947	556,405
Housekeeping	121,733	60,084	47,210	229,027	53,374	53,374	33,361	195,473
Laundry and linen	18,577	60,725	22,372	101,674	16,947	57,140	17,628	91,715
	<u>\$ 587,200</u>	<u>248,396</u>	<u>964,415</u>	<u>1,800,011</u>	<u>593,679</u>	<u>200,894</u>	<u>908,238</u>	<u>1,692,812</u>
<b>ADMINISTRATIVE SERVICES</b>								
	\$ 1,326,067	301,017	485,372	2,112,456	1,220,778	331,632	472,032	2,024,442
<b>NONDEPARTMENTAL</b>								
Employee Benefits	--	--	2,162,488	2,162,488	--	--	2,006,639	2,006,639
Depreciation and amortization	--	--	2,152,529	2,152,529	--	--	1,930,784	1,930,784
Insurance	--	--	171,311	171,311	--	--	152,466	152,466
Interest	--	--	277,945	277,945	--	--	115,195	115,195
	<u>\$ --</u>	<u>--</u>	<u>4,764,273</u>	<u>4,764,273</u>	<u>--</u>	<u>--</u>	<u>4,205,084</u>	<u>4,205,084</u>
<b>TOTAL EXPENSES</b>								
	\$ 7,879,837	2,333,872	10,225,081	20,438,790	7,397,830	2,132,943	9,428,831	18,959,604

**LAKES REGIONAL HEALTHCARE**  
**Spirit Lake, Iowa**

**Patient Receivables and Allowance for Doubtful Accounts**  
**For the Years Ended June 30, 2005 and 2004**

ANALYSIS OF AGING:

Days Since Discharge	2005		2004	
	Amount	Percent of Total	Amount	Percent of Total
0 - 60	\$ 4,181,314	65.86 %	3,466,226	65.88
61 - 90	457,168	7.20	417,682	7.94
91 - 180	605,877	9.54	533,040	10.13
181 - 364	766,087	12.07	534,297	10.16
> 1 year	225,960	3.56	246,991	4.69
> 2 years	112,550	1.77	63,139	1.20
	<u>6,348,956</u>	100.00 %	<u>5,261,375</u>	100.00
Less:				
Allowance for doubtful accounts	(1,280,133)		(1,367,110)	
Allowance for contractual adjustments	<u>(1,620,254)</u>		<u>(1,273,287)</u>	
	<u>\$ 3,448,569</u>		<u>\$ 2,620,978</u>	

	2005	2004
NET DAYS REVENUE IN PATIENT ACCOUNTS RECEIVABLE	58.43 days	47.22 days
ALLOWANCE FOR DOUBTFUL ACCOUNTS:		
Balance, beginning of year	\$ 1,367,110	1,688,840
Provision of uncollectible accounts	625,000	600,000
Recoveries of accounts previously written off	168,782	191,595
Accounts written off	<u>(880,759)</u>	<u>(1,113,325)</u>
Balance, end of year	<u>\$ 1,280,133</u>	<u>1,367,110</u>

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Inventory / Prepaid Expenses**  
**For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<b>INVENTORY:</b>		
Surgical services	\$ 326,186	311,441
Pharmacy	132,169	123,636
Central storeroom	113,127	123,899
Laboratory	29,439	22,608
Radiology	24,152	26,050
Dietary	17,718	15,447
Fuel oil	14,520	8,480
Respiratory therapy/stress testing	2,391	2,297
	<u>\$ 659,702</u>	<u>633,858</u>
 <b>PREPAID EXPENSES:</b>		
Insurance	\$ 143,605	77,708
Maintenance contracts	35,165	32,605
Other	1,455	1,589
	<u>\$ 180,225</u>	<u>111,902</u>

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Financial and Statistical Highlights**  
For the Years Ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Patient days:		
Adult and pediatric-		
Medicare	3,664	3,526
Other	<u>1,646</u>	<u>1,567</u>
	5,310	5,093
Swing bed-		
Skilled	994	1,199
Newborn	<u>449</u>	<u>434</u>
Total	<u>6,753</u>	<u>6,726</u>
Patient discharges:		
Adult and pediatric-		
Medicare	924	879
Other	<u>612</u>	<u>541</u>
	1,536	1,460
Swing bed-		
Skilled	238	264
Newborn	<u>195</u>	<u>192</u>
Total	<u>1,969</u>	<u>1,916</u>
Average length of stay:		
Adult and pediatric-		
Medicare	3.97 days	4.01 days
Other	2.67 days	2.90 days
Swing bed-		
Skilled	4.18 days	4.54 days
Newborn	2.3 days	2.3 days
Surgical procedures	4,301	4,246
Emergency room visits	6,409	5,856
Number of employees - full-time equivalents	200.81	200.34



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**Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards**

To the Board of Trustees  
Lakes Regional Healthcare  
Spirit Lake, Iowa:

We have audited the financial statements of LAKES REGIONAL HEALTHCARE as of and for the year ended June 30, 2005, and have issued our report thereon, dated August 26, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Hospital's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting.

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Hospital's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. We noted no matters involving the internal control over financial reporting and its operation that we consider to be a reportable condition.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We noted no matters involving the internal control over financial reporting and its operation that we consider to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about the Hospital's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance that are required to be reported under Government Auditing Standards. However, we note certain immaterial instances of non-compliance or other matters that are described in Part III of the accompanying Schedule of Findings and Questioned Costs.

Comments involving statutory and other legal matters about the Hospital's operations for the year ended June 30, 2005 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Hospital. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes. Prior year statutory comments have been resolved.

This report, a public record by law, is intended solely for the information and use of the officials, employees and constituents of the Hospital and other parties to whom the Hospital may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Lakes Regional Healthcare during the course of the audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

*Seim, Johnson, Sostek & Quist LLP*

Omaha, Nebraska,  
August 26, 2005.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Schedule of Findings and Questioned Costs**  
For the Year Ended June 30, 2005

**Part I: Summary of the Independent Auditor's Results**

- (a) An unqualified opinion was issued on the financial statements.
- (b) No reportable conditions or material weaknesses in internal control over financial reporting were disclosed by the audit of the financial statements.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.

**Part II: Findings Related to the Financial Statements**

**INSTANCES OF NON-COMPLIANCE:**

No matters were reported.

**REPORTABLE CONDITIONS:**

No reportable conditions were identified.

**Part III: Other Findings Related to Required Statutory Reporting**

Official Depositories: A resolution naming official depositories has been adopted by the Board. The maximum deposit amounts stated in the resolution were not exceeded during the year ended June 30, 2005.

Certified Budget: Hospital disbursements during the year ended June 30, 2005 exceeded amounts budgeted. During 2005, the Hospital continued to invest in capital assets. The expenditures related to these items were not appropriately estimated in the original budget.

Recommendation: The Hospital should review current activity and amounts budgeted. If differences are noted, the budget should be amended to ensure disbursements do not exceed amounts budgeted.

Response: We will amend the budget for changes noted during the year.

Conclusion: Response accepted.

Questionable Expenditure: We noted no expenditures that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

Travel Expense: No expenditures of Hospital money for travel expenses of spouses of Hospital officials and/or employees were noted.

Business Transactions: No business transactions between the Hospital and Hospital officials and/or employees were noted to violate Chapter 347.15 of the Code of Iowa which limits a trustee's pecuniary interest in the purchase or sale of any commodities or supplies procured for or disposed of by said hospital to \$1,500 without publicly invited and opened written competitive bids.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Schedule of Findings and Questioned Costs**  
**For the Year Ended June 30, 2005**

Board Minutes: - No transactions were found that we believe should have been approved in the Board minutes but were not.

Deposits and Investments: We noted no instances of noncompliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of the Code of Iowa and the Hospital's investment policy.

Publication of Bills Allowed and Salaries: Chapter 347.13(14) of the Code of Iowa states in part, "There shall be published quarterly in each of the official newspapers of the county as selected by the board of supervisors pursuant to Section 349.1 the schedule of bills allowed and there shall be published annually in such newspaper the schedule of salaries paid by job classification and category..." We noted no instances of noncompliance with the publication of bills allowed and salaries. The Hospital publishes a list of expenditures quarterly which are summarized by major classification and vendor. They also publish a schedule of salaries annually by category.

**LAKES REGIONAL HEALTHCARE**  
Spirit Lake, Iowa

**Audit Staff**  
**For the Year Ended June 30, 2005**

This audit was performed by:

Roger E. Thompson, FHFMA, CPA, Partner

Brian D. Green, FHFMA, CPA, Partner

Joseph L. Harnisch, Staff Auditor

Steven M. Eck, Staff Auditor