

Audubon County Memorial Hospital

Accountants' Report and Financial Statements

June 30, 2006 and 2005



Audubon County Memorial Hospital
June 30, 2006 and 2005

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Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Trustees
Audubon County Memorial Hospital
Audubon, Iowa

We have audited the accompanying balance sheet of Audubon County Memorial Hospital as of June 30, 2006 and the related statements of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Audubon County Memorial Hospital as of and for the year ended June 30, 2005, were audited by other accountants whose report dated September 8, 2005, expressed an unqualified opinion on those statements.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 audit provides a reasonable basis for our opinion.

In our opinion, the 2006 financial statements referred to above present fairly, in all material respects, the financial position of Audubon County Memorial Hospital as of June 30, 2006, and its changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 15, 2006, on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying management's discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We and the other accountants have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information in 2006 and 2005, respectively. However, we did not audit the information and express no opinion on it.

Board of Trustees
Audubon County Memorial Hospital
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Our audit was conducted for the purpose of forming an opinion on the Hospital's basic financial statements. The accompanying supplementary information as listed in the table of contents 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. The supplemental information as of and for the year ended June 30, 2005, was audited by other accountants whose report dated September 8, 2005, expressed an unqualified opinion on such information in relation to the basic financial statements as of and for the year ended June 30, 2005, taken as a whole.

/s/ **BKD, LLP**

Kansas City, Missouri
September 15, 2006

Audubon County Memorial Hospital

Management's Discussion and Analysis

Years Ended June 30, 2006 and 2005

Introduction

This management's discussion and analysis of the financial performance of Audubon County Memorial Hospital (the "Hospital") provides an overview of the Hospital's financial activities for the years ended June 30, 2006 and 2005. It should be read in conjunction with the accompanying financial statements of the Hospital.

Financial Highlights

- Cash and cash equivalents decreased between 2006 and 2005 by \$132,663 or 10% and increased between 2005 and 2004 by \$712,080 or 127%.
- The Hospital's net assets increased \$802,222 or 7% in 2006 over 2005 and increased \$927,727 or 8% in 2005 over 2004.
- The Hospital reported operating income in 2006 of \$87,336 and operating income in 2005 of \$320,845.
- Net nonoperating revenues increased by \$102,399 or 18% in 2006 compared to 2005 and increased by \$20,664 or 4% in 2005 compared to 2004.

Using This Annual Report

The Hospital's financial statements consist of three statements—a balance sheet; a statement of revenues, expenses and changes in net assets; and a statement of cash flows. These statements provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by creditors, contributors, grantors or enabling legislation. The Hospital is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Assets

One of the most important questions asked about any Hospital's finances is "Is the Hospital as a whole better or worse off as a result of the year's activities?" The Balance Sheet and the Statement of Revenues, Expenses and Changes in Net Assets report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. Using the accrual basis of accounting means that 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 the Hospital's net assets and changes in them. The Hospital's total net assets—the difference between assets and liabilities—is one measure of the Hospital's financial health or financial position. Over time, increases or decreases in the Hospital's net assets are an indicator of whether its financial health is improving or deteriorating. Other nonfinancial factors, such as changes in the Hospital's patient base, changes in legislation and regulations, measures of the quantity and quality of services provided to its patients and local economic factors, should also be considered to assess the overall financial health of the Hospital.

The Statement of Cash Flows

The Statement of Cash Flows reports cash receipts, cash payments and net changes in cash and cash equivalents resulting from four defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for and what was the change in cash and cash equivalents during the reporting period.

The Hospital's Net Assets

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheet. The Hospital's net assets increased by \$802,222 or 7% in 2006 over 2005 as shown in Table 1.

Table 1: Assets, Liabilities and Net Assets

	2006	2005	2004
Assets			
Patient accounts receivable, net	\$ 822,686	\$ 998,665	\$ 1,142,737
Other current assets	4,784,244	5,301,376	3,970,153
Capital assets, net	5,146,859	5,400,615	5,006,166
Other noncurrent assets	<u>3,526,458</u>	<u>2,123,087</u>	<u>2,569,016</u>
Total assets	<u>\$ 14,280,247</u>	<u>\$ 13,823,743</u>	<u>\$ 12,688,072</u>
Liabilities			
Current liabilities	\$ 1,122,673	\$ 1,435,391	\$ 1,194,447
Long-term debt	<u>82,500</u>	<u>115,500</u>	<u>148,500</u>
Total liabilities	<u>1,205,173</u>	<u>1,550,891</u>	<u>1,342,947</u>
Net Assets			
Invested in capital assets, net of related debt	5,031,359	5,252,115	4,824,666
Restricted expendable	45	613	613
Restricted nonexpendable	10,000	10,000	10,000
Unrestricted	<u>8,033,670</u>	<u>7,010,124</u>	<u>6,509,846</u>
Total net assets	<u>13,075,074</u>	<u>12,272,852</u>	<u>11,345,125</u>
Total liabilities and net assets	<u>\$ 14,280,247</u>	<u>\$ 13,823,743</u>	<u>\$ 12,688,072</u>

The balance sheet changed in five major areas. An additional \$230,338 in cash and certificates of deposit were added in fiscal year 2006 due to the net income received in the year. This allows Audubon County Memorial Hospital to continue to grow and improve.

Patient accounts receivable, net of allowances decreased by \$175, 979. This was due to the decrease in gross days of six. Gross days in 2005 were 53 at fiscal year end, and gross days for fiscal year 2006 were 47 at year-end. The reduction in accounts receivable allowed the Hospital to set aside additional cash to earn more interest income.

Audubon County Memorial Hospital asked for an additional \$50,000 in property taxes for fiscal year 2007, thus increasing the property taxes receivable.

Capital assets actually increased by \$345,743 between year 2005 and 2006 along with an increase in accumulated depreciation of \$599,499, for a net decrease in assets of \$253,756 between the two years.

Current liabilities have decreased by \$312,718 from fiscal year 2005 to fiscal year 2006. This is due in part to a stop loss payment for health insurance made to us in error of \$200,680 that was on the books as of June 30, 2005 and accrued payroll with 19 days of accrual for fiscal year 2005 and only 6 days of accrual for fiscal year 2006 amounting to a difference of \$91,578.

Current assets increased \$1,167,770 in 2005 over 2004, primarily due to increase in cash and cash equivalents and certificate of deposit.

Operating Results and Changes in the Hospital's Net Assets

In 2006, the Hospital's net assets increased by \$802,222 or 7% as shown in Table 2. This increase is made up of several different components.

Table 2: Operating Results and Changes in Net Assets

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Operating Revenues			
Net patient service revenue	\$ 7,322,553	\$ 7,138,050	\$ 6,701,544
Other operating revenues	<u>105,843</u>	<u>112,113</u>	<u>92,604</u>
Total operating revenues	<u>7,428,396</u>	<u>7,250,163</u>	<u>6,794,148</u>
Operating Expenses			
Salaries and wages and employee benefits	3,482,796	3,321,696	3,233,701
Medical professional fees	549,347	538,311	498,699
Depreciation and amortization	767,206	692,926	674,539
Other operating expenses	<u>2,541,711</u>	<u>2,376,385</u>	<u>2,160,575</u>
Total operating expenses	<u>7,341,060</u>	<u>6,929,318</u>	<u>6,567,514</u>
Operating Income	<u>87,336</u>	<u>320,845</u>	<u>226,634</u>
Nonoperating Revenues			
Property taxes	419,812	420,086	415,020
Interest income	231,756	142,526	113,151
Non-capital gifts	<u>22,077</u>	<u>8,634</u>	<u>22,411</u>
Total nonoperating revenues	<u>673,645</u>	<u>571,246</u>	<u>550,582</u>
Excess of Revenues Over Expenses Before Capital Grants and Contributions	760,981	892,091	777,216
Capital Grants and Contributions	<u>41,241</u>	<u>35,636</u>	<u>—</u>
Increase in Net Assets	<u>\$ 802,222</u>	<u>\$ 927,727</u>	<u>\$ 777,216</u>

Operating Income (Loss)

The first component of the overall change in the Hospital's net assets is its operating income or loss—generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. In 2006, 2005 and 2004, the Hospital has reported an operating income. This is consistent with the Hospital's recent operating history as the Hospital was formed and is operated primarily to serve residents of Audubon County and the surrounding area. The Hospital levies property taxes to provide sufficient resources to enable the facility to serve patients.

In 2006, the following changes were noted:

- Inpatient service revenue decreased \$127,503 or 7.5%. Inpatient acute days decreased 82 days or 10%; however, the Hospital increased charges for fiscal year 2006 by 5%. Two of the three primary admitting doctors had decreases in patient admittance for fiscal year 2006.
- The Hospital stopped providing obstetrics services beginning in fiscal year 2006, which meant a decrease of approximately \$40,000 in lost revenue from fiscal year 2005 for these services. This does not take into account the lost revenue from prenatal care (example: ultrasounds and lab work) or postnatal care.
- Swing bed patient days decreased by 169 days, which equates to approximately \$220,000 decrease in revenue from fiscal year 2005.
- Outpatient revenues increased by \$273,284 despite a decrease in outpatient visits of 1,529. The increase in revenue is due primarily to an increase in pharmacy revenue of \$355,000. This is attributed to an increase in chemotherapy drugs.
- Overall, net patient service revenue increased by \$184,503 or 3% from 2005 to 2006.
- Operating expenses increased by 5.9% due mostly to inflationary factors.

During 2005, the Hospital implemented an across-the-board 2% increase in charges and experienced increases in surgery, anesthesiology and medical and surgical supplies revenue.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of property taxes levied by the Hospital and interest income, all of which increased by \$102,399 or 18% from 2006 to 2005 and increased by \$20,664 or 4% from 2005 as compared to 2004. The increase in 2006 was due primarily to the receipt of increased interest income of \$89,230. The Hospital increased investments for longer terms at higher interest rates to earn the additional interest income. The additional increase was due to the receipt of additional non-capital gifts in 2006.

Grants and gifts for capital and non-capital items received in fiscal year 2006 increased by \$14,377. This year we received \$8,573 in SHIP grants, \$12,565 HRSA grants, \$23,114 from the Foundation, \$2,500 from the auxiliary and \$18,728 from trusts and memorials.

Contributions

The Hospital received contributions of \$63,318 from various individuals in 2006, an increase of \$19,048 or 43% from 2005.

The Hospital received contributions of \$44,270 from various individuals in 2005, an increase of \$21,859 or 98% from 2004.

The Hospital received contributions of \$22,411 from various individuals in 2004.

The Hospital's Cash Flows

Changes in the Hospital's cash flows are consistent with changes in the operating loss and nonoperating revenues and expenses in 2006, 2005 and 2004, discussed earlier.

Capital Asset and Debt Administration

Capital Assets

At the end of 2006, the Hospital had \$5.1 million invested in capital assets, net of accumulated depreciation, as detailed in Note 5 to the financial statements. In 2006, the Hospital purchased new capital assets costing \$537,235.

At the end of 2005, the Hospital had \$5.4 million invested in capital assets, net of accumulated depreciation, as detailed in Note 5 to the financial statements. In 2005, the Hospital purchased new capital assets costing \$1,087,254.

Debt

The only long-term debt that the Hospital has is the zero interest note payable. Audubon County Memorial Hospital pays \$33,000 on this loan annually.

Contacting the Hospital's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Hospital Administration by calling (712) 563-2611.

Audubon County Memorial Hospital

Balance Sheets

June 30, 2006 and 2005

Assets

	<u>2006</u>	<u>2005</u>
Current Assets		
Cash and cash equivalents	\$ 867,118	\$ 1,271,760
Certificates of deposit	2,907,469	3,332,962
Patient accounts receivable, net of allowance; 2006 – \$168,766, 2005 – \$178,132	822,686	998,665
Property taxes receivable	471,421	419,382
Other receivables	24,750	21,702
Estimated amounts due from third-party payers	255,000	—
Supplies	208,110	186,946
Prepaid expenses	<u>50,376</u>	<u>68,624</u>
Total current assets	<u>5,606,930</u>	<u>6,300,041</u>
Noncurrent Cash and Deposits		
Internally designated	2,455,940	2,100,474
Restricted by donors for		
Scholarships	45	613
Endowment	10,000	10,000
Certificates of deposit	<u>1,060,473</u>	<u>—</u>
	<u>3,526,458</u>	<u>2,111,087</u>
Capital Assets, Net	<u>5,146,859</u>	<u>5,400,615</u>
Other Assets	<u>—</u>	<u>12,000</u>
Total Assets	<u>\$ 14,280,247</u>	<u>\$ 13,823,743</u>

Liabilities and Net Assets

	<u>2006</u>	<u>2005</u>
Current Liabilities		
Current maturities of long-term debt	\$ 33,000	\$ 33,000
Accounts payable	271,278	248,881
Accrued expenses	346,974	668,386
Estimated amounts due to third-party payers	—	65,742
Deferred revenue for property taxes	<u>471,421</u>	<u>419,382</u>
Total current liabilities	1,122,673	1,435,391
Long-term Debt	<u>82,500</u>	<u>115,500</u>
Total liabilities	<u>1,205,173</u>	<u>1,550,891</u>
Net Assets		
Invested in capital assets, net of related debt	5,031,359	5,252,115
Restricted		
Expendable for scholarships	45	613
Nonexpendable endowment	10,000	10,000
Unrestricted	<u>8,033,670</u>	<u>7,010,124</u>
Total net assets	<u>13,075,074</u>	<u>12,272,852</u>
Total Liabilities and Net Assets	<u>\$ 14,280,247</u>	<u>\$ 13,823,743</u>

Audubon County Memorial Hospital
Statements of Revenues, Expenses and Changes in Net Assets
Years Ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Operating Revenues		
Net patient service revenue before provision for uncollectible accounts	\$ 7,509,090	\$ 7,297,803
Provision for uncollectible accounts	<u>(186,537)</u>	<u>(159,753)</u>
Net patient service revenue	7,322,553	7,138,050
Other	<u>105,843</u>	<u>112,113</u>
Total operating revenues	<u>7,428,396</u>	<u>7,250,163</u>
Operating Expenses		
Salaries and wages	2,596,412	2,553,983
Employee benefits	886,384	767,713
Medical professional fees	549,347	538,311
Supplies and other	1,761,498	1,640,189
General services	327,401	311,305
Administrative services	395,434	368,792
Insurance	57,378	56,099
Depreciation	<u>767,206</u>	<u>692,926</u>
Total operating expenses	<u>7,341,060</u>	<u>6,929,318</u>
Operating Income	<u>87,336</u>	<u>320,845</u>
Nonoperating Revenues		
Property taxes	419,812	420,086
Interest income	231,756	142,526
Noncapital gifts	<u>22,077</u>	<u>8,634</u>
Total nonoperating revenues	<u>673,645</u>	<u>571,246</u>
Excess of Revenues Over Expenses Before Capital Grants and Contributions	760,981	892,091
Capital Grants and Contributions	<u>41,241</u>	<u>35,636</u>
Increase in Net Assets	802,222	927,727
Net Assets, Beginning of Year	<u>12,272,852</u>	<u>11,345,125</u>
Net Assets, End of Year	<u>\$ 13,075,074</u>	<u>\$ 12,272,852</u>

Audubon County Memorial Hospital
Statements of Cash Flows
Years Ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Operating Activities		
Receipts from and on behalf of patients	\$ 7,177,790	\$ 7,341,206
Payments to suppliers and contractors	(3,074,625)	(3,719,411)
Payments to employees	(3,804,208)	(2,366,854)
Other receipts, net	<u>105,841</u>	<u>105,612</u>
Net cash provided by operating activities	<u>404,798</u>	<u>1,360,553</u>
Noncapital Financing Activities		
Property taxes supporting operations	419,812	420,086
Noncapital gifts	<u>22,077</u>	<u>8,634</u>
Net cash provided by noncapital financing activities	<u>441,889</u>	<u>428,720</u>
Capital and Related Financing Activities		
Principal paid on capital debt	(33,000)	(33,000)
Capital grants and gifts	41,241	35,636
Proceeds from sale of capital assets	—	2,155
Purchase of capital assets	<u>(513,448)</u>	<u>(1,087,254)</u>
Net cash used in capital and related financing activities	<u>(505,207)</u>	<u>(1,082,463)</u>
Investing Activities		
Decrease in noncurrent cash and investments	—	445,929
Interest on deposits	231,756	135,614
Purchase of deposits	(5,061,567)	(3,295,457)
Proceeds from disposition of deposits	<u>4,355,668</u>	<u>2,719,184</u>
Net cash provided by (used in) investing activities	<u>(474,143)</u>	<u>5,270</u>
Increase (Decrease) in Cash and Cash Equivalents	(132,663)	712,080
Cash and Cash Equivalents, Beginning of Year	<u>1,271,760</u>	<u>559,680</u>
Cash and Cash Equivalents, End of Year	<u>\$ 1,139,097</u>	<u>\$ 1,271,760</u>

(Continued)

Audubon County Memorial Hospital
Statements of Cash Flows
Years Ended June 30, 2006 and 2005

	2006	2005
Reconciliation of Cash and Cash Equivalents to the Balance Sheets		
Cash and cash equivalents	\$ 867,118	\$ 1,271,760
Cash in noncurrent cash and deposits		
Internally designated	271,979	—
	\$ 1,139,097	\$ 1,271,760
 Reconciliation of Net Operating Revenues (Expenses) to Net Cash Provided by Operating Activities		
Operating income	\$ 87,336	\$ 320,845
Depreciation and amortization	767,206	692,926
(Gain) loss on sale of fixed asset	(2)	(2,155)
Changes in operating assets and liabilities		
Patient accounts receivable, net	175,979	144,072
Supplies and prepaid expenses	(5,964)	(16,698)
Estimated amounts due from and to third-party payers	(320,742)	54,738
Accounts payable and accrued expenses	(299,015)	166,825
Net cash provided by operating activities	\$ 404,798	\$ 1,360,553
 Supplemental Cash Flow Information		
Trade-in value for new equipment	\$ 23,785	\$ —

Audubon County Memorial Hospital

Notes to Financial Statements

June 30, 2006 and 2005

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Audubon County Memorial Hospital (“Hospital”) is a county public hospital organized under Chapter 347 of the Code of Iowa. The Hospital primarily earns revenue by providing inpatient, outpatient and emergency care services to patients in the Audubon County area and the surrounding area in South Central Iowa.

Basis of Accounting and Presentation

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific (such as county appropriations), property taxes, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

The Hospital prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

Use of Estimates

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

Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2006 and 2005, cash equivalents consisted primarily of interest-bearing accounts.

Audubon County Memorial Hospital

Notes to Financial Statements

June 30, 2006 and 2005

Property Taxes

The Hospital received approximately 6% of its financial support from property tax revenues in the years ended June 30, 2006 and 2005, which were used to support operations. The Hospital levies the tax in March of each year based on assessed valuation of property in the County as of the second preceding January 1. Tax bills are sent by the County in August and the taxes are payable half on September 1 and March 1, and become delinquent after October 1 and April 1, respectively.

Property tax receivable is recognized on the levy or lien date, which is the date that the tax asking is certified by the County Board of Supervisors. The succeeding property tax receivable represents taxes certified by the Board of Supervisors to be collected in the next fiscal year for the purposes set out in the budget for the next fiscal year. By statute, the Board of Supervisors is required to certify the budget in March of each year for the subsequent fiscal year. However, by statute, the tax asking and budget certification for the following fiscal year becomes effective on the first day of that year. Although the succeeding year property tax receivable has been recorded, the related revenue is deferred and will not be recognized as revenue until the year for which it is levied.

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 and natural disasters. Commercial insurance coverage is purchased for claims arising from such matters other than those related to employee health claims, for which the Hospital is self-insured. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

The Hospital is self-insured for a portion of its exposure to risk of loss from employee health claims. Annual estimated provisions are accrued for the self-insured portion of employee health claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Patient Accounts Receivable

The Hospital reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Hospital provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Supplies

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital:

Land improvements	10 to 40 years
Buildings, improvements and fixed equipment	5 to 40 years
Major moveable equipment	3 to 20 years

Compensated Absences

Hospital policies permit most employees to accumulate vacation benefits that may be realized as paid time off. Expense and the related liability are recognized as benefits are earned. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at that date.

Net Assets

Net assets of the Hospital are classified in four components. Net assets invested in capital assets, net of related debt, consist of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital assets that must be used for a particular purpose as specified by creditors, grantors or donors external to the Hospital. Restricted nonexpendable net assets are noncapital assets that are required to be maintained in perpetuity as specified by parties external to the Hospital, such as permanent endowments. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the definition of invested in capital assets, net of related debt, or restricted expendable net assets.

Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and include estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

Audubon County Memorial Hospital

Notes to Financial Statements

June 30, 2006 and 2005

Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue. Charges excluded from revenue under the Hospital's charity care policy were \$40,913 and \$2,520 for 2006 and 2005, respectively.

Income Taxes

As an essential government function of the County, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Hospital is subject to federal income tax on any unrelated business taxable income.

Reclassifications

Certain reclassifications have been made to the 2005 financial statements to conform to the 2006 presentation. The reclassifications had no effect on the changes in financial position.

Note 2: Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

Medicare. Inpatient and outpatient services and defined capital cost related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Fiscal Intermediary. Estimated settlements have been reflected in the accompanying financial statements.

Medicaid. Inpatient and outpatient services rendered to Medicaid Program beneficiaries are reimbursed based upon a cost reimbursement methodology. The Hospital is reimbursed at a tentative rate with the final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicaid Program.

Approximately 60% and 64% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended June 30, 2006 and 2005, respectively.

The Hospital has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Hospital under these agreements includes discounts from established charges and prospectively determined rates.

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

Note 3: Deposits, Investments and Deposit Income

Deposits

Custodial credit risk is the risk that, in the event of a bank failure, a government's deposits may not be returned to it. The Hospital's deposit policy for custodial risk requires compliance with the provisions of state law.

The Hospital had no bank balances exposed to custodial credit risk at June 30, 2006 and 2005. The Hospital's deposits in banks at June 30, 2006 and 2005 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. Certificates of deposit are considered deposits.

Investments

The Hospital is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities 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; certain joint investment trusts and warrants or improvement certificates of a drainage district. The Hospital had no investments at June 30, 2006 and 2005.

Summary of Carrying Values

The carrying values of deposits are included in the balance sheets as follows:

	<u>2006</u>	<u>2005</u>
Carrying value		
Deposits	\$ 7,300,745	\$ 6,715,509
Other	<u>300</u>	<u>300</u>
	<u>\$ 7,301,045</u>	<u>\$ 6,715,809</u>
Included in the following balance sheet captions		
Cash and cash equivalents	\$ 867,118	\$ 1,271,760
Certificates of deposit	2,907,469	3,332,962
Noncurrent cash and deposits		
Internally designated	2,455,940	2,100,474
Restricted by donors for		
Scholarships	45	613
Endowment	10,000	10,000
Certificates of deposit	<u>1,060,473</u>	<u>—</u>
	<u>\$ 7,301,045</u>	<u>\$ 6,715,809</u>

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

Deposit Income

Income on deposits for the years ended June 30, 2006 and 2005, amounted to \$231,756 and \$142,526, respectively.

Note 4: Patient Accounts Receivable

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at June 30, 2006 and 2005 consisted of:

	2006	2005
Medicare	\$ 327,811	\$ 427,599
Medicaid	46,383	89,005
Other third-party payers	450,886	496,749
Patients	166,372	163,444
	991,452	1,176,797
Less allowance for uncollectible accounts	168,766	178,132
	\$ 822,686	\$ 998,665

Note 5: Capital Assets

Capital assets activity for the years ended June 30, 2006 and 2005 follows:

	Beginning Balance	Additions	Disposals	Transfers/ Adjustments	Ending Balance
2006					
Land	\$ 68,389	\$ —	\$ —	\$ —	\$ 68,389
Land improvements	394,425	—	—	—	394,425
Buildings	6,214,526	9,651	—	11,367	6,235,544
Fixed equipment	628,860	—	—	—	628,860
Major movable equipment	2,896,125	370,824	191,492	289,607	3,365,064
Construction in progress	144,214	156,760	—	(300,974)	0
	10,346,539	537,235	191,492	0	10,692,282
Less accumulated depreciation					
Land improvements	176,884	27,793	—	—	204,677
Buildings	2,604,004	339,583	—	—	2,943,587
Fixed equipment	404,418	26,634	—	—	431,052
Major movable equipment	1,760,618	373,196	167,707	—	1,966,107
	4,945,924	767,206	167,707	0	5,545,423
Capital assets, net	\$ 5,400,615	\$ (229,971)	\$ 23,785	\$ 0	\$ 5,146,859

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

	Beginning Balance	Additions	Disposals	Transfers/ Adjustments	Ending Balance
2005					
Land	\$ 68,389	\$ —	\$ —	\$ —	\$ 68,389
Land improvements	317,819	76,606	—	—	394,425
Buildings	5,686,006	528,520	—	—	6,214,526
Fixed equipment	628,860	—	—	—	628,860
Major movable equipment	2,662,971	421,029	187,875	—	2,896,125
Construction in progress	<u>83,115</u>	<u>61,099</u>	<u>—</u>	<u>—</u>	<u>144,214</u>
	<u>9,447,160</u>	<u>1,087,254</u>	<u>187,875</u>	<u>0</u>	<u>10,346,539</u>
Less accumulated depreciation					
Land improvements	151,645	25,239	—	—	176,884
Buildings	2,277,401	326,603	—	—	2,604,004
Fixed equipment	376,499	27,919	—	—	404,418
Major movable equipment	<u>1,635,449</u>	<u>313,044</u>	<u>187,875</u>	<u>—</u>	<u>1,760,618</u>
	<u>4,440,994</u>	<u>692,805</u>	<u>187,875</u>	<u>0</u>	<u>4,945,924</u>
Capital assets, net	<u>\$ 5,006,166</u>	<u>\$ 394,449</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 5,400,615</u>

Note 6: Medical Malpractice Insurance

The Hospital purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claims experience, no such accrual has been made.

Note 7: Employee Health Claims

Substantially all of the Hospital's employees and their dependents are eligible to participate in the Hospital's employee health insurance plan. The Hospital is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$30,000 per covered person. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

economic and social factors. It is reasonably possible that the Hospital's estimate will change by a material amount in the near term. Changes in the balance of claims liabilities during 2006 and 2005 are summarized as follows:

	2006	2005
Balance, beginning of year	\$ 349,287	\$ 196,593
Current year claims and changes in estimates	376,071	661,496
Claim payments	(631,058)	(508,802)
Balance, end of year	\$ 94,300	\$ 349,287

Note 8: Long-term Debt

The following is a summary of long-term debt transactions for the Hospital for the years ended June 30, 2006 and 2005:

	2006				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt					
Note payable, non-interest bearing (A)	\$ <u>148,500</u>	\$ <u>0</u>	\$ <u>(33,000)</u>	\$ <u>115,500</u>	\$ <u>33,000</u>
	2005				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt					
Note payable, non-interest bearing (A)	\$ <u>181,500</u>	\$ <u>0</u>	\$ <u>(33,000)</u>	\$ <u>148,500</u>	\$ <u>33,000</u>

(A) Note Payable, which is non-interest bearing dated September 1999, for the construction of an in-house physicians clinic and for the construction of a clinic in Exira, Iowa. The note payable calls for repayment through September 2009 with quarterly installments of \$8,250.

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

The debt service requirements as of June 30, 2006 are as follows:

Year Ending June 30,	Total to be Paid	Principal
2007	\$ 33,000	\$ 33,000
2008	33,000	33,000
2009	33,000	33,000
2010	16,500	16,500
	\$ 115,500	\$ 115,500

Note 9: Restricted and Designated Net Assets

At June 30, 2006 and 2005, restricted expendable and net assets were available for the following purposes:

	2006	2005
Scholarships	\$ <u>45</u>	\$ <u>613</u>

Note 10: Operating Leases

On January 1, 2000, the Hospital, as lessor, leased an area of the Hospital building and a clinic building in Exira, Iowa, to be used as medical office space under ten-year operating lease agreements. The leases contain provisions to automatically renew for another ten-year period, unless written termination notice is given 90 days prior to renewal. Rental income will be recognized over the term of the leases. Lease payments to be received on a monthly basis total \$2,477.

Future minimum rentals receivable at June 30, 2006, were:

2007	\$ 29,720
2008	29,720
2009	29,720
2010	14,862
Future minimum lease payments	\$ 104,022

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

Note 11: Pension Plan

Plan Description

The Hospital contributes to the Iowa Public Employees' Retirement System (IPERS), a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. Pension expense is recorded for the amount the Hospital is contractually required to contribute for the year. The plan provides retirement and death benefits, which are established by State Statute, to plan members and beneficiaries. The plan issues a publicly available financial report that includes financial statements and required supplementary information for the plan. The report may be obtained by writing to the plan at IPERS, P.O. Box 9117, Des Moines, Iowa 50306-9117.

Funding Policy

Plan members are required to contribute 3.7% of their annual covered salaries and the Hospital is required to contribute 5.75% of annual covered payroll for 2006 and 2005. Contribution requirements are established by State statute. The Hospital's contributions to the plan for 2006, 2005 and 2004 were \$149,200, \$145,700 and \$138,900, respectively, which equaled the required contributions for each year.

Note 12: Administration and Support Services Agreement

The Hospital has entered into an agreement with another health care organization to provide administration and support services. Administration and support services fees of \$203,298 and \$188,938 were incurred for the years ended June 30, 2006 and 2005, respectively. At June 30, 2006 and 2005, the Hospital had accounts payable to the organization of approximately \$20,700 and \$13,500, respectively.

Note 13: Audubon County Hospital Foundation

The Audubon County Hospital Foundation was established to raise funds to support the operations and other activities of the Audubon County Memorial Hospital. The Foundation's funds are distributed to the Hospital in amounts and periods determined by the Foundation's Board of Directors. The distributions by the Foundation to the Hospital for the years ended June 30, 2006 and 2005 were as follows:

	2006	2005
Contributions from Foundation to finance plant replacement and expansion	\$ <u>23,114</u>	\$ <u>12,739</u>

Audubon County Memorial Hospital
Notes to Financial Statements
June 30, 2006 and 2005

Note 14: Budget and Budgetary Accounting

In accordance with the Code of Iowa, the Board of Trustees annually adopts a budget on a cash basis following required public notice and hearings for all funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

The following is a reconciliation between reported amounts and cash basis presentation as well as a comparison to budget, for the year ended June 30, 2006:

	Book Basis	Actual Accrual Adjustments	Cash Basis	Budget
Amount to be raised by taxation	\$ 419,812	\$ —	\$ 419,812	\$ 419,382
Other revenues/receipts	<u>7,723,470</u>	<u>(144,763)</u>	<u>7,578,707</u>	<u>7,317,334</u>
	8,143,282	(144,763)	7,998,519	7,736,716
Expenses/disbursements	<u>7,341,060</u>	<u>304,979</u>	<u>7,646,039</u>	<u>8,312,091</u>
	802,222	(449,742)	352,480	(575,375)
Balance, beginning of year	<u>12,272,852</u>	<u>(292,928)</u>	<u>11,979,924</u>	<u>11,979,924</u>
Balance, end of year	<u>\$ 13,075,074</u>	<u>\$ (742,670)</u>	<u>\$ 12,332,404</u>	<u>\$ 11,404,549</u>

Supplementary Information

Audubon County Memorial Hospital
Schedules of Patient Service Revenues
Years Ended June 30, 2006 and 2005

	2006			2005		
	Total	Inpatient	Outpatient	Total	Inpatient	Outpatient
Daily Patient Services						
Medical and surgical	\$ 426,779	\$ 326,691	\$ 100,088	\$ 451,871	\$ 351,195	\$ 100,676
Skilled nursing care	138,416	138,416		184,698	184,698	
Coronary care	3,005	3,005		4,004	4,004	
Obstetric	874	874		19,136	19,136	
Nursery	656	656		13,104	13,104	
Intermediate nursing care				450	450	
	<u>569,730</u>	<u>469,642</u>	<u>100,088</u>	<u>673,263</u>	<u>572,587</u>	<u>100,676</u>
Nursing Services						
Emergency	242,314	8,726	233,588	237,521	5,312	232,209
Operating room	1,035,851	37,069	998,782	943,719	25,775	917,944
Recovery room	104,284	4,042	100,242	99,705	3,465	96,240
Delivery and labor room	95		95	13,798	4,918	8,880
	<u>1,382,544</u>	<u>49,837</u>	<u>1,332,707</u>	<u>1,294,743</u>	<u>39,470</u>	<u>1,255,273</u>
Other Professional Services						
Anesthesiology	388,539	17,264	371,275	388,848	23,387	365,461
Radiology	2,624,675	264,969	2,359,706	2,738,438	274,559	2,463,879
Blood service	31,280	15,221	16,059	39,458	13,454	26,004
Laboratory	1,438,252	222,259	1,215,993	1,348,816	178,812	1,170,004
Intravenous therapy	13,785	6,970	6,815	14,964	8,841	6,123
Respiratory therapy	57,125	26,605	30,520	58,942	32,120	26,822
Physical therapy	306,851	46,944	259,907	319,091	53,328	265,763
Speech therapy	10,278	2,888	7,390	8,305	3,895	4,410
Occupational therapy	5,561	3,741	1,820	8,429	5,638	2,791
Electrocardiology	91,233	30,989	60,244	93,649	23,480	70,169
Cardiology	64,123		64,123	69,245	596	68,649
Cardiac rehabilitation	14,917		14,917	17,587		17,587
Electroencephalography	2,237		2,237	1,522		1,522
Medical and surgical supplies	588,729	135,873	452,856	688,681	145,475	543,206
Pharmacy	1,538,007	279,751	1,258,256	1,228,495	324,823	903,672
Sleep study	39,100	65	39,035	34,506		34,506
Clinic	69,194		69,194	63,397	56	63,341
	<u>7,283,886</u>	<u>1,053,539</u>	<u>6,230,347</u>	<u>7,122,373</u>	<u>1,088,464</u>	<u>6,033,909</u>
Patient Service Revenue	9,236,160	\$ <u>1,573,018</u>	\$ <u>7,663,142</u>	9,090,379	\$ <u>1,700,521</u>	\$ <u>7,389,858</u>
Contractual Adjustments	(1,727,070)			(1,792,576)		
Net Patient Service Revenue Before						
Provision for Uncollectible Accounts	7,509,090			7,297,803		
Provision for Uncollectible Accounts	(186,537)			(159,753)		
Net Patient Service Revenue	\$ <u>7,322,553</u>			\$ <u>7,138,050</u>		

Audubon County Memorial Hospital
Schedules of Other Operating Revenues
Years Ended June 30, 2006 and 2005

	2006	2005
Other Revenues		
Cafeteria meals	\$ 19,582	\$ 16,333
Space rental	30,140	32,030
Grants	1,594	6,832
Other	54,525	54,763
Gain on sale of capital assets	2	2,155
	\$ 105,843	\$ 112,113

Audubon County Memorial Hospital
Schedules of Operating Expenses
Years Ended June 30, 2006 and 2005

	2006			2005		
	Total	Salaries	Other	Total	Salaries	Other
Daily Patient Services						
Nursing administration	\$ 73,816	\$ 64,460	\$ 9,356	\$ 68,575	\$ 63,654	\$ 4,921
Medical and surgical	694,466	674,223	20,243	693,414	674,887	18,527
Obstetric	494	494		7,649	7,551	98
Nursery	276	276		5,139	5,092	47
Operating room	303,925	74,850	229,075	206,879	74,952	131,927
Delivery and labor room	25	25		3,032	3,019	13
Emergency service	<u>260,793</u>	<u>259,620</u>	<u>1,173</u>	<u>256,472</u>	<u>255,206</u>	<u>1,266</u>
	<u>1,333,795</u>	<u>1,073,948</u>	<u>259,847</u>	<u>1,241,160</u>	<u>1,084,361</u>	<u>156,799</u>
Other Professional Services						
Laboratory	465,740	208,311	257,429	477,529	208,837	268,692
Central supply	262,664	15,674	246,990	368,226	14,774	353,452
Intravenous therapy	2,658		2,658	3,481		3,481
Electrocardiology	7,910	1,546	6,364	10,522	2,639	7,883
Electroencephalography	675	121	554	533	113	420
Cardiac rehabilitation	6,681	6,580	101	10,978	7,981	2,997
Cardiology	6,190		6,190	8,998		8,998
Radiology	825,698	175,964	649,734	841,324	175,867	665,457
Pharmacy	657,324	98,142	559,182	467,739	89,537	378,202
Anesthesiology	138,889		138,889	144,972		144,972
Respiratory therapy	39,870	30,317	9,553	35,713	30,188	5,525
Physical therapy	148,566	43,373	105,193	157,721	40,885	116,836
Speech therapy	5,504		5,504	4,605		4,605
Occupational therapy	4,718	4,718		6,773		6,773
Sleep study	18,000		18,000	18,100		18,100
Specialty clinics	142,760	131,162	11,598	132,702	125,461	7,241
Medical records	<u>142,931</u>	<u>109,872</u>	<u>33,059</u>	<u>139,459</u>	<u>111,392</u>	<u>28,067</u>
	<u>2,876,778</u>	<u>825,780</u>	<u>2,050,998</u>	<u>2,829,375</u>	<u>807,674</u>	<u>2,021,701</u>
General Services						
Operation of plant	320,266	106,576	213,690	296,390	92,578	203,812
Dietary	211,593	131,195	80,398	195,021	120,532	74,489
Housekeeping	101,848	80,613	21,235	99,053	77,629	21,424
Laundry	<u>33,618</u>	<u>21,540</u>	<u>12,078</u>	<u>36,484</u>	<u>24,904</u>	<u>11,580</u>
	<u>667,325</u>	<u>339,924</u>	<u>327,401</u>	<u>626,948</u>	<u>315,643</u>	<u>311,305</u>
Administrative Services	<u>752,194</u>	<u>356,760</u>	<u>395,434</u>	<u>715,097</u>	<u>346,305</u>	<u>368,792</u>
Employee Benefits	<u>886,384</u>		<u>886,384</u>	<u>767,713</u>		<u>767,713</u>
Insurance	<u>57,378</u>		<u>57,378</u>	<u>56,099</u>		<u>56,099</u>
Depreciation	<u>767,206</u>		<u>767,206</u>	<u>692,926</u>		<u>692,926</u>
	<u>\$ 7,341,060</u>	<u>\$ 2,596,412</u>	<u>\$ 4,744,648</u>	<u>\$ 6,929,318</u>	<u>\$ 2,553,983</u>	<u>\$ 4,375,335</u>

Audubon County Memorial Hospital
Schedules of Patient Receivables and
Allowance for Uncollectible Accounts
Years Ended June 30, 2006 and 2005

Schedules of Patient Receivables

	Amounts		Percent to Total	
	2006	2005	2006	2005
Days Since Discharge				
0 – 30	\$ 686,266	\$ 819,180	58%	61%
31 – 60	279,962	286,314	24	21
61 – 90	83,082	122,541	7	9
91 and over	<u>130,151</u>	<u>123,739</u>	<u>11</u>	<u>9</u>
	1,179,461	1,351,774	<u>100%</u>	<u>100%</u>
Less:				
Contractual allowances	188,009	174,977		
Allowance for uncollectible accounts	<u>168,766</u>	<u>178,132</u>		
	<u>\$ 822,686</u>	<u>\$ 998,665</u>		
Net Patient Service Revenue per Calendar day (Excluding provision for bad debt)	<u>\$ 19,838</u>	<u>\$ 19,994</u>		
Days of Net Patient Service Revenue in Accounts Receivable at Year End	<u>41</u>	<u>50</u>		

Allowance for Uncollectible Accounts

	2006	2005
Balance, beginning of year	\$ 178,132	\$ 218,939
Provision for year	186,537	159,753
Recoveries of accounts previously written off	<u>317,938</u>	<u>254,514</u>
	682,607	633,206
Less accounts written off	<u>513,841</u>	<u>455,074</u>
Balance, end of year	<u>\$ 168,766</u>	<u>\$ 178,132</u>

Audubon County Memorial Hospital
Schedules of Supplies and Prepaid Expense
Years Ended June 30, 2006 and 2005

Supplies

	2006	2005
General stores	\$ 81,520	\$ 74,403
Pharmacy	103,508	98,001
Laboratory	<u>23,082</u>	<u>14,542</u>
	<u>\$ 208,110</u>	<u>\$ 186,946</u>

Prepaid Expense

	2006	2005
Insurance	\$ 14,619	\$ 31,381
Service Contracts	28,179	29,656
Other	<u>7,578</u>	<u>7,587</u>
	<u>\$ 50,376</u>	<u>\$ 68,624</u>

Audubon County Memorial Hospital

Schedule of Officials

Year Ended June 30, 2006

Name	Title	Term Expires
Board of Trustees		
Jay D. Mendenhall	Chairman	December 31, 2006
Mark Kessler	Vice Chairman	December 31, 2010
Linda Blomme	Secretary	December 31, 2006
Paul Schultz, DDS	Treasurer	December 31, 2006
Wayne Hansen	Member	December 31, 2010
Daniel Smith	Member	December 31, 2008
Connie S. Faga	Member	December 31, 2008
Hospital Officials		
Tom Smith	CEO/Administrator	
Joan Fancher	Assistant Administrator	
Karen McGuire	Chief Financial Officer	

Audubon County Memorial Hospital
Schedules of Financial and Statistical Data
Years Ended June 30, 2006 and 2005

	2006	2005
Patient Days		
Acute	741	823
Swing bed	422	591
Nursery	2	42
	1,165	1,456
Admissions (Acute)	243	281
Discharges (Acute)	243	281
Average Length of Stay in Days (Acute)	3.05	2.93
Beds	25	25
Occupancy percentage	8.12%	9.02%



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

Board of Trustees
Audubon County Memorial Hospital
Audubon, Iowa

We have audited the financial statements of Audubon County Memorial Hospital as of and for the year ended June 30, 2006, and have issued our report thereon dated September 15, 2006. 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. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. 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. A reportable condition is described in the accompanying schedule of findings and responses as item 06-1.

A material weakness is a reportable 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. However, we believe the reportable condition described above is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether 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, noncompliance with which could have a direct and material effect on the

determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We also noted certain additional matters that are reported below or we reported to the Hospital's management in a separate letter dated September 15, 2006.

Compliance with Certain Provisions of Iowa Law

The following comments about the Hospital's compliance with certain provisions of Iowa law for the year ended June 30, 2006 are based exclusively on knowledge obtained from procedures performed during our independent audit of the financial statements of the Hospital for the year ended June 30, 2006. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily examined. In addition, it should be noted that our audit was not directed primarily toward obtaining knowledge of compliance with the following items. Our procedures do not provide a legal determination on the Hospital's compliance with those requirements.

Official Depository Banks

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, 2006.

Certified Budget

Budget hearings were held and publications were made in accordance with Chapter 24.9 of the Code of Iowa. Hospital disbursements during the year ended June 30, 2006 did not exceed amounts budgeted.

Questionable Expenditures

We did not note any questionable expenditures that we believe may constitute an unlawful expenditure from public funds or questionable disbursements that may not meet the public purpose requirements as defined in an Attorney General's opinion dated April 25, 1979. However, the following was noted:

Criteria or Specific Requirement – Management is responsible for establishing policies regarding questionable expenditures.

Condition – The Board of Trustees has not adopted written policies surrounding questionable expenditures that establish expenses considered to meet the public purpose and the required documentation for those expenditures.

Context – Written policies are not in effect.

Effect – Employees may not be aware of potential questionable expenditures and the need to document their public purpose.

Cause – Written policies are not in place.

Recommendation – Management should establish policies to inform employees of what is considered expenses that meet the public purpose and require documentation of that purpose.

Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendations. Management will perform suggested action to enact policies to conform to this requirement.

Travel Expense

No expenditures of Hospital money for travel expenses of spouses of Hospital officials and/or employees were noted. Mileage reimbursement was approved for employees not in excess of the IRS limits; however, we noted the following:

Criteria or Specific Requirement – Board of Trustees is responsible for establishing and approving proper mileage reimbursement.

Condition – Board of Trustees approval of mileage reimbursement rate was not documented.

Context – Board of Trustees did not have an approved policy or resolution establishing the mileage reimbursement rate.

Effect – Mileage reimbursement could be paid at unapproved rate.

Cause – The Board of Trustees did not recognize the need to approve the mileage reimbursement in accordance with the provisions of Iowa law.

Recommendation – The Board of Trustees should establish a policy to approve the mileage reimbursement rate on a periodic basis.

Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendations. Management will perform suggested action to conform to this requirement.

Business Transactions

We noted no transactions between Hospital and Hospital officials or employees other than those exempted by law; i.e., bankers on the Board of Trustees.

Trustee Minutes

No transactions were found that we believe should have been approved in the Trustee minutes but were not.

Deposits and Investments

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

Unclaimed Property

Prior to November 1, 2005, the Hospital was required to file an annual report of unclaimed property with the state treasurer in accordance with Chapter 556.11 of the Code of Iowa. We noted the following exception:

Criteria or Specific Requirement – Hospital management is responsible for filing a report of unclaimed property or a negative report if no unclaimed property is on hand.

Condition – A report noting no unclaimed property was not filed in 2006 for the year ended June 30, 2005.

Context – The Hospital had no unclaimed property, but no report was filed.

Effect – Requirements were not met under Chapter 556.11 of the Code of Iowa.

Cause – Necessary reporting was not made in the current fiscal year.

Recommendation – Management should ensure necessary reporting is completed each year.

Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendations. Management will perform suggested action to ensure all reporting is made in accordance with the Code of Iowa.

Disbursements for Equipment and Supplies

We did not note any disbursements for equipment or supplies that we believe were not in accordance with Chapter 347.13(3) of the Code of Iowa.

Compensation of Hospital Administrator, Assistants and Employees

No instances were noted in which compensation for the administrator, assistants or employees was determined other than in accordance with Chapter 347.13(5) of the Code of Iowa.

Internal Revenue Service Information Returns and Outside Services

We noted no instances where the Hospital failed to properly prepare a Form 1099 for outside services of \$600 or more or failed to properly classify workers as independent contractors versus employees.

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This report is intended solely for the information and use of the governing body and management and the State of Iowa, and is not intended to be and should not be used by anyone other than these specified parties.

/s/ **BKD, LLP**

Kansas City, Missouri
September 15, 2006

Audubon County Memorial Hospital
Schedule of Findings and Responses
Year Ended June 30, 2006

Reference Number	Finding
06-1	<p>Criteria or Specific Requirement—Management is responsible for establishing and maintaining effective internal control over financial reporting.</p> <p>Condition—One individual has incompatible duties in the purchases cycle.</p> <p>Context—The individual responsible for processing cash disbursements has duties that include access to assets, recording and monitoring responsibilities.</p> <p>Effect—Potentially material misstatements in the financial statements or material misappropriations of assets due to error or fraud could occur and not be prevented or detected in a timely manner.</p> <p>Cause—Duties in the purchases cycle are not adequately segregated and monitoring or other compensating controls are insufficient.</p> <p>Recommendation—Management should periodically evaluate the costs versus the benefits of further segregation of duties or addition of monitoring or other compensating controls and implement those changes it deems appropriate for which benefits are determined to exceed costs.</p> <p>Views of Responsible Officials and Planned Corrective Actions—Management concurs with the findings and recommendations. Management will perform suggested evaluation and make any changes that are cost effective and operationally feasible within the next year.</p>



Board of Trustees
Audubon County Memorial Hospital
Audubon, Iowa

As part of our audit of the financial statements of Audubon County Memorial Hospital for the year ended June 30, 2006, we studied and evaluated the Hospital's internal control structure. Because the study and evaluation was only part of the overall audit plan regarding the financial statements, it was not intended to be a complete review of all your accounting procedures and, therefore, would not necessarily disclose all reportable conditions or opportunities for improvement. A reportable condition involves matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure 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 observed the following matters and offer these comments and suggestions.

Segregation of Duties

Certain matters regarding internal controls were included in the Independent Accountants' Report on Compliance and Internal Control Over Financial Reporting and on Compliance and Other Matters Based on the Audit of the Financial Statements Performed in Accordance with *Government Auditing Standards*.

Segregation of accounting duties is an essential element of effective internal controls, involving the separation of custody of assets from related recording of transactions. Segregation of conflicting duties within the Hospital's accounting department may be difficult because of the limited number of personnel. However, there may be compensating controls management could implement to reduce the possibility of errors or irregularities going undetected in the normal course of business. We encourage you to limit, to the extent possible, performance of incompatible duties by individuals in the Hospital's accounting department.

We noted the CFO has duties that include access to assets, recording responsibilities and monitoring of transactions in the accounts payable cycles. We recommend another person be responsible for checks after they are signed.

Standard Accounting Policies and Procedures

There is little written documentation of accounting or data processing procedures. Internal control is strengthened by identifying and documenting accounting procedures and responsibilities of accounting personnel. This is also important for the compliance program. We understand the Hospital is in the process of documenting policies and procedures. We recommend continuing the effort to develop written documentation of controls and procedures to strengthen the Hospital's ability to continue to operate efficiently, especially in the event of unexpected employee turnover.

Required Vacations

Employees handling cash are not required to take a one week of uninterrupted vacation while someone else completes their duties. We recommend employees handling cash should take one week of uninterrupted vacation.

Risk Assessment Audit Standards

During the past year, the AICPA issued the Risk Assessment Suite of Standards (Statements of Auditing Standards numbers 104 through 111). These Statements establish standards and provide guidance concerning the auditor's assessment of risks of material misstatement in a financial statement audit and provide guidance on the design and performance of the audit procedures whose nature, timing and extent are designed to address the assessed risks. In addition, the Statements establish standards and guidance on planning and supervision, the nature of audit evidence and evaluating whether the audit evidence obtained affords a reasonable basis for an opinion on the financial statements.

Overall, the primary objective of these Statements is to enhance the auditor's application of the audit risk model in conducting audits by specifying a more in-depth understanding of the organization and its environment, including its internal control, to identify the risks of material misstatement in the financial statements and what the organization is doing to mitigate the risks. These standards are effective for fiscal years beginning on or after December 15, 2006.

These Standards will have a significant impact on the Hospital's audit once they become effective, which will most likely be June 30, 2008.

* * * * *

We appreciate the opportunity to present these comments and suggestions. This letter does not express an opinion on the Hospital's overall internal control structure; it does, however, include items that we believe merit your consideration. We can discuss these matters further at your convenience and provide any implementation assistance for changes or improvements you may require.

This letter is intended solely for the information and use of the Board of Trustees and management and is not intended to be and should not be used by anyone other than these specified parties.

/s/ **BKD, LLP**

Kansas City, Missouri
September 15, 2006