

FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

KOSSUTH REGIONAL
HEALTH CENTER

KOSSUTH REGIONAL HEALTH CENTER

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**KOSSUTH REGIONAL HEALTH CENTER
BOARD OF TRUSTEES AND HEALTH CENTER OFFICIALS**

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Jack Munch	Chairperson	December 31, 2008
Thomas Geelan	Treasurer	December 31, 2008
Conley Nelson	Secretary	December 31, 2012
Eileen Bormann	Member	December 31, 2012
John Cowin	Member	December 31, 2010

Health Center Officials

Scott Curtis	Administrator
Daniel Myers	Controller



CPAs & BUSINESS ADVISORS

INDEPENDENT AUDITOR'S REPORT

The Board of Trustees
Kossuth Regional Health Center
Algona, Iowa

We have audited the accompanying balance sheets of Kossuth Regional Health Center as of June 30, 2008 and 2007, and its discretely presented component unit as of December 31, 2007 and 2006, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Health Center'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 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 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 Kossuth Regional Health Center as of June 30, 2008 and 2007, and its discretely presented component unit as of December 31, 2007 and 2006, and the respective changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As indicated in the Health Center's Summary of Significant Accounting Policies in Note 1 to the financial statements, management has elected to report interest expense as an operating expense in the Statement of Revenues, Expenses, and Changes in Net Assets. Governmental Auditing Standards Board Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* does not establish a definition of operating revenues and expenses versus nonoperating revenues and expenses. Rather, governments are required to establish their own policy defining operating revenues and expenses and apply the policy consistently. The common practice for governmental health care entities is to include interest expense in nonoperating revenues and expenses.

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In accordance with *Government Auditing Standards*, we have also issued our report dated September 18, 2008, on our consideration of Kossuth Regional Health Center'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 audits.

Management's Discussion and Analysis on pages 4 through 7 and the Budgetary Comparison Schedules on pages 29 and 30 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion on it.

A handwritten signature in cursive script that reads "Eide Bailly LLP". The signature is written in black ink and is positioned above the typed address and date.

Dubuque, Iowa
September 18, 2008

**KOSSUTH REGIONAL HEALTH CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2008**

As management of the Kossuth Regional Health Center, we offer readers a narrative overview and analysis of the financial activity of the facility. We encourage readers to consider the information presented along with the subsequent audited financial statements.

Staff Highlights

In August of 2007, we added a new family practice physician, Dr. Jeffrey Doolittle to our staff. Since his arrival, he has developed a thriving practice and has been a welcome addition to the team.

We have also been successful in the recruitment of an additional family practice physician to join our practice in August of 2009. Dr Rachel Venteicher will begin after completing her third and final year of a family practice residency program. She will be a welcome addition to replace the vacancy left by Dr. Manasi Nadkarni.

Recruitment for a general surgeon continues to replace the vacancy left by Dr. Prasad Nadkarni in January of 2008. During the interim, we have received surgery support from the Mason City Clinic.

We were pleased to add Mia Hegarty, Ph.D. to our staff as we began to offer behavioral medicine services. This is being done in partnership with Mercy Medical Center - North Iowa as they are providing oversight to the program.

One of our Physician Assistants, Mark Davis, was called to active duty in Iraq. Mark was involved in serving in a medical capacity there for 2 months, and also had many stories to share from his experiences there.

Operating Highlights

A number of facilities projects were in various stages of development during the year. A sewer lift station replacement project was completed at the beginning of the year. A project to renovate the registration, waiting area, and lobby of the main hospital was completed. A major renovation and addition project at our Algona Clinic was underway during the entire year. This project added 8,000 square feet to the building and renovated a majority of the existing clinic building.

Effective July 1, 2008, the management agreement between Mercy Medical Center - North Iowa and Kossuth Regional Health Center has been revised. In this agreement, the management fee was increased as it was acknowledged that fees previously charged were not keeping pace with the actual cost of administering the management services. Also, the risk sharing terms of the agreement were adjusted to where there is no 50/50 sharing of either a gain or loss from operations unless either exceeds \$500,000 during the course of the year.

KOSSUTH REGIONAL HEALTH CENTER

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2008

The hospital successfully completed a major project to implement an electronic health record system. This project was significant in that it established a completely integrated system connecting all major ancillary systems to the patient inpatient record system as well as was done in unison with six other rural facilities that are part of the Mercy Medical Center - North Iowa Network of hospitals. This integration has enabled greater patient safety and improved quality through 24-hour review of ordered medications by pharmacists, as well as the sharing of other clinical information between providers caring for patients who have been treated in more than one network facility.

The Health Center's original hospital facility was constructed in 1949. Although a clinic was constructed near the hospital facility in 1978, there were no significant additions or renovations to the hospital facility from 1949 to 1990. Although the Health Center has undertaken certain improvements since 1990, there are areas which have not yet been substantially renovated.

In addition, some of the Health Center's infrastructure is nearing sixty years old, and is antiquated and inefficient. Finally, the facility does not adequately accommodate current service volumes, and does not provide for current and anticipated growth.

To address these critical issues, Kossuth Regional Health Center intends to proceed with a significant building project. The Project calls for the construction of a 34,000-square foot, four-level addition to the southeast of the existing Health Center facilities.

The third level will provide 25 private inpatient rooms, each with full private bath. This will replace inpatient rooms which date back to the original 1949 facility, many of them semi-private with shared or partial baths, and too small given the need to accommodate growing amounts of bedside medical technology.

The second level will provide additional pre- and post-surgical space adjacent to the existing surgery area, which was renovated and expanded in 2001. This should accommodate the continuing shift from inpatient toward outpatient surgery, and be helpful as the Health Center recruits a new full-time resident general surgeon. The new space on this level will also permit relocation and expansion of the Health Center's rehabilitation area.

The first level will house a new kitchen and cafeteria.

The lower level will accommodate mechanicals (including a chiller, air handling equipment, and electrical equipment) and employee support space (including a staff lounge and offices).

The Health Center has engaged as its architect Shive-Hattery Group, Inc. of West Des Moines and Cedar Rapids. The current project schedule calls for bids to be awarded and a guaranteed maximum price to be established in late October 2008, with groundbreaking in early November 2008. Construction of the addition is expected to require twelve months. An additional six months will be required to renovate the portions of the existing facility which will be vacated by operations to be relocated to the addition, producing a total project calendar from groundbreaking to completion of eighteen months. A site plan and floor plans are available.

**KOSSUTH REGIONAL HEALTH CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2008**

The Kossuth Regional Health Center Foundation has just launched a capital campaign in support of the Project. The development firm engaged to assist the Foundation has already completed a study to assess the likely results of the campaign. Based on the results of that study, the Foundation has established a goal of \$1 million. The Foundation expects that the campaign will exceed this goal, and that all of the proceeds will be realized by the time the Project is completed.

The hospital was pleased to have been named in the estate of Lyle "Bud" Anderson. His gift of \$100,000 to the hospital will be recognized as the first major gift associated with hospital's capital campaign and will be used to dedicate an outside courtyard area being developed for use by both patients and staff.

Financial Highlights

- The Hospital's assets exceeded its liabilities by \$13,994,862 at June 30, 2008.
- The Hospital recorded income from operations of \$237,383 for the fiscal year ending on June 30, 2008. A significant decline in profitability was seen from the previous year due to lower surgery volumes after the departure of Dr. Prasad Nadkarni on January 1, 2008. Recruitment activities for a General Surgeon are ongoing.
- 63.8 days cash on hand was reported at June 30, 2008. Cash reserves were utilized for the Algona Clinic renovation project as well as the electronic health record implementation project.
- 63 days in net patient accounts receivable was reported at June 30, 2008. In increase in the days in accounts receivable was seen after the conversion of the Clinic patient accounts software system. It is anticipated that this indicator will decline to historical levels as the system is fully implemented.
- The Hospital had 3,483 patient discharge days in 2008, an increase of 0.8% from 2007.
- The Hospital had 26,636 outpatient registrations in 2008.
- The Hospital had 42,833 visits at its Clinics in Algona and Bancroft in 2008, a decrease of 2.8% from 2007. The departure of Dr. Manasi Nadkarni in January 2008 along with the absence of Mark Davis, PA, during his deployment to Iraq had a negative impact when compared with the previous year.

Overview of the Financial Statements

The audited financial statements from Eide Bailly LLP include the Balance Sheet, Statement of Revenues, Expenses, and Changes in Net Assets, Statement of Cash Flows, Notes to Financial Statements, and Supplementary Schedules.

**KOSSUTH REGIONAL HEALTH CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2008**

The Balance Sheet at June 30, 2008, indicates total assets of \$16,437,861, total liabilities of \$2,442,999 and net assets of \$13,994,862. Total current assets were \$7,871,227, and total current liabilities were \$2,236,692 for a current ratio of 3.5.

The Statement of Revenues, Expenses, and Changes in Net Assets indicates total operating revenues of \$22,684,004, and total operating expenses of \$22,446,621 for an operating profit of \$237,383. Net non-operating revenue is \$555,815. After an adjustment for affiliated agreement expenses, the total revenues in excess of expenses are \$753,396 for 2008 which increased the net assets from \$13,241,466 to \$13,994,862.

As reported in the Statement of Cash Flows, cash and cash equivalents decreased from \$1,507,455 at June 30, 2007 to \$928,353 at June 30, 2008. The net decrease in cash and cash equivalents of \$579,102 came from operating activities of -\$783,864, noncapital financing activities of \$344,423, capital and related financing activities of -\$1,994,708, and investing activities of \$1,855,047.

There are notes to the financial statements included in the audit report. All of the notes are consistent with and similar to audit reports from prior years. The reader is encouraged to examine them at his or her leisure.

The Supplementary Schedules give the reader much more detail than is disclosed in the Statement of Revenues, Expenses, and Changes in Net Assets. The revenues are detailed by department and by patient status, and also compared with the previous year. The expenses are detailed by department and by natural expense classification, and also compared to the previous year.

Capital Assets

The capital assets of Kossuth Regional Health Center, as of June 30, 2008, amounted to \$6,795,928 (net of accumulated depreciation). This investment in capital assets includes land, land improvements, buildings and equipment.

At year-end, Kossuth Regional Health Center had \$331,934 debt outstanding remaining from the Surgery Expansion project, which took place in 2001.

Requests for Information

Questions regarding the information provided in this report or requests for additional financial information should be addressed to the office of the Controller at the following address:

Kossuth Regional Health Center
Attn: Controller
1515 South Phillips Street
Algona, IA 50511

KOSSUTH REGIONAL HEALTH CENTER
BALANCE SHEETS
JUNE 30, 2008

	<u>2008</u>	<u>2007</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 928,353	\$ 1,507,455
Investments - Note 4	1,078,039	1,890,937
Assets limited as to use or restricted - Note 4	115,627	109,562
Receivables		
Patient, net of estimated uncollectibles		
of \$1,548,000 in 2008 and \$1,324,000 in 2007	3,363,666	2,704,043
Estimated third-party payor settlements	1,000,000	140,000
Succeeding year property tax receivable	298,000	298,000
Other	47,506	112,099
Supplies	518,722	524,438
Prepaid expense	521,314	417,462
Total current assets	<u>7,871,227</u>	<u>7,703,996</u>
ASSETS LIMITED AS TO USE OR RESTRICTED - Note 4		
Internally designated for hospice expenditures	222,793	224,455
Internally designated for capital improvements	1,279,492	2,042,481
Internally designated for health benefits	135,783	216,012
Restricted under debt agreement	132,638	124,580
Total assets limited as to use or restricted	<u>1,770,706</u>	<u>2,607,528</u>
LAND, BUILDINGS, AND EQUIPMENT, net - Note 5	<u>6,795,928</u>	<u>5,564,713</u>
Total assets	<u>\$ 16,437,861</u>	<u>\$ 15,876,237</u>

See notes to financial statements.

	<u>2008</u>	<u>2007</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current maturities of long-term debt - Note 6	\$ 125,627	\$ 119,562
Accounts payable		
Trade	521,138	254,585
Construction	68,162	-
Related party	304,666	838,228
Accrued expenses		
Salaries and wages	427,839	342,093
Paid leave	473,237	430,750
Payroll taxes and employee benefits	10,434	7,668
Other	7,589	11,951
Deferred revenue for succeeding year property tax receivable	<u>298,000</u>	<u>298,000</u>
 Total current liabilities	 2,236,692	 2,302,837
 LONG-TERM DEBT, less current maturities - Note 6	 <u>206,307</u>	 <u>331,934</u>
 Total liabilities	 <u>2,442,999</u>	 <u>2,634,771</u>
NET ASSETS		
Invested in capital assets, net of related debt	6,463,994	5,113,217
Restricted by debt agreement	132,638	124,580
Unrestricted	<u>7,398,230</u>	<u>8,003,669</u>
 Total net assets	 <u>13,994,862</u>	 <u>13,241,466</u>
 Total liabilities and net assets	 <u>\$ 16,437,861</u>	 <u>\$ 15,876,237</u>

KOSSUTH REGIONAL HEALTH CENTER FOUNDATION
BALANCE SHEETS
DECEMBER 31, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 130,132	\$ 90,627
NONCURRENT CASH AND INVESTMENTS	<u>1,814,378</u>	<u>1,673,084</u>
Total assets	<u>\$ 1,944,510</u>	<u>\$ 1,763,711</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Grants payable	\$ 6,836	\$ 3,665
NET ASSETS, unrestricted	<u>1,937,674</u>	<u>1,760,046</u>
Total liabilities and net assets	<u>\$ 1,944,510</u>	<u>\$ 1,763,711</u>

KOSSUTH REGIONAL HEALTH CENTER
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
OPERATING REVENUES		
Net patient service revenue (net of provision for bad debts of \$848,661 in 2008 and \$567,280 in 2007) - Notes 2 and 3	\$ 19,454,151	\$ 17,928,523
Other operating revenues	3,229,853	3,066,014
TOTAL OPERATING REVENUES	<u>22,684,004</u>	<u>20,994,537</u>
OPERATING EXPENSES		
Salaries and wages	7,155,466	6,431,784
Employee benefits	2,938,022	2,172,926
Supplies and other expenses	11,562,150	10,640,977
Depreciation	770,907	723,904
Interest and amortization	20,076	25,822
TOTAL OPERATING EXPENSES	<u>22,446,621</u>	<u>19,995,413</u>
OPERATING INCOME BEFORE AFFILIATION AGREEMENT	237,383	999,124
AFFILIATION AGREEMENT EXPENSE	<u>(118,692)</u>	<u>(499,562)</u>
OPERATING INCOME	<u>118,691</u>	<u>499,562</u>
NONOPERATING REVENUES (EXPENSES)		
County tax revenue	295,753	299,982
Investment income	211,392	248,489
Noncapital contributions and grants	38,564	105,756
Loss on sale of property and equipment	-	(13,796)
Dialysis unit rental income	10,106	10,937
NET NONOPERATING REVENUES	<u>555,815</u>	<u>651,368</u>
REVENUES IN EXCESS OF EXPENSES BEFORE CAPITAL CONTRIBUTIONS AND GRANTS		
	674,506	1,150,930
Capital contributions and grants	<u>78,890</u>	<u>7,045</u>
INCREASE IN NET ASSETS	753,396	1,157,975
NET ASSETS, BEGINNING OF YEAR	<u>13,241,466</u>	<u>12,083,491</u>
NET ASSETS, END OF YEAR	<u>\$ 13,994,862</u>	<u>\$ 13,241,466</u>

See notes to financial statements.

KOSSUTH REGIONAL HEALTH CENTER FOUNDATION
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
OPERATING REVENUES		
Contributions	\$ 117,061	\$ 98,057
Investment income	<u>120,561</u>	<u>186,321</u>
TOTAL OPERATING REVENUES	<u>237,622</u>	<u>284,378</u>
EXPENSES		
Fundraising	24,638	19,529
Contributions to Kossuth Regional Health Center	21,866	10,000
Supplies and other expenses	<u>13,490</u>	<u>13,255</u>
TOTAL EXPENSES	<u>59,994</u>	<u>42,784</u>
INCREASE IN UNRESTRICTED NET ASSETS	177,628	241,594
NET ASSETS, BEGINNING OF YEAR	<u>1,760,046</u>	<u>1,518,452</u>
NET ASSETS, END OF YEAR	<u>\$ 1,937,674</u>	<u>\$ 1,760,046</u>

KOSSUTH REGIONAL HEALTH CENTER
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts of patient service revenue	\$ 17,934,528	\$ 17,217,715
Payments of salaries and wages	(7,027,233)	(6,375,163)
Payments of supplies and other expenses	(14,985,605)	(13,173,127)
Other receipts and payments, net	<u>3,294,446</u>	<u>3,170,079</u>
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	<u>(783,864)</u>	<u>839,504</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Noncapital contributions and grants received	38,564	105,756
County tax revenue received	295,753	299,982
Dialysis unit rental income	<u>10,106</u>	<u>10,937</u>
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	<u>344,423</u>	<u>416,675</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of property and equipment	(1,933,960)	(904,506)
Proceeds from sale of property and equipment	-	25,000
Principal payments on long-term debt	(119,562)	(113,814)
Interest payments on long-term debt	(20,076)	(25,822)
Capital contributions and grants	<u>78,890</u>	<u>7,045</u>
NET CASH USED FOR CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(1,994,708)</u>	<u>(1,012,097)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment income	211,392	248,489
Decrease in investments	812,898	134,849
Decrease in assets limited as to use or restricted	<u>830,757</u>	<u>32,364</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>1,855,047</u>	<u>415,702</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(579,102)	659,784
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>1,507,455</u>	<u>847,671</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 928,353</u>	<u>\$ 1,507,455</u>

See notes to financial statements.

KOSSUTH REGIONAL HEALTH CENTER
STATEMENTS OF CASH FLOWS – PAGE 2
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES		
Operating income	\$ 118,691	\$ 499,562
Adjustments to reconcile operating income to net cash provided by (used for) operating activities		
Depreciation	770,907	723,904
Interest expense considered capital and related financing activity	20,076	25,822
Provision for bad debts	848,661	567,280
Changes in assets and liabilities		
Patient receivables	(1,508,284)	(950,249)
Estimated third-party payor settlements	(860,000)	(327,839)
Other receivables	64,593	104,065
Supplies	5,716	(93,873)
Prepaid expense	(103,852)	(10,402)
Accounts payable - trade and related	(267,009)	238,695
Accrued expenses	<u>126,637</u>	<u>62,539</u>
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	<u>\$ (783,864)</u>	<u>\$ 839,504</u>

KOSSUTH REGIONAL HEALTH CENTER FOUNDATION
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from donors and contributors	\$ 117,061	\$ 98,057
Interest received	12,706	11,321
Cash paid to suppliers	(38,128)	(32,784)
Payments to Kossuth Regional Health Center	<u>(18,695)</u>	<u>(10,505)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>72,944</u>	<u>66,089</u>
INVESTING ACTIVITIES		
Purchase of investments	<u>(33,439)</u>	<u>(62,513)</u>
INCREASE IN CASH AND CASH EQUIVALENTS	39,505	3,576
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>90,627</u>	<u>87,051</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 130,132</u>	<u>\$ 90,627</u>
RECONCILIATION OF INCREASE IN NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Increase in net assets	\$ 177,628	\$ 241,594
Adjustments to reconcile increase in net assets to net cash provided by operating activities		
Unrealized (gain) loss on investments	171,177	(76,149)
Realized gain on sale of investments, reinvested capital gains and dividends on investments	(279,032)	(98,851)
Increase (decrease) in grants payable	<u>3,171</u>	<u>(505)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 72,944</u>	<u>\$ 66,089</u>

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Kossuth Regional Health Center (the Health Center) consists of a 25-bed acute care hospital located in Algona, Iowa. It is organized under Chapter 347A of the Code of Iowa. The Health Center provides health care services under the name of Kossuth Regional Health Center in accordance with a Master Affiliation Agreement discussed further in Note 9. Services are provided to residents of Kossuth and surrounding counties in Iowa. The Health Center is exempt from income taxes as a political subdivision.

The Health Center's financial statements are prepared in conformity with U.S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board.

Reporting Entity

For financial reporting purposes the Health Center has included all funds, organizations, agencies, boards, commissions, and authorities. The Health Center 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 Health Center are such that exclusion would cause the Health Center'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 Health Center 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 Health Center.

Kossuth Regional Health Center Foundation (the Foundation) is a legally separate, tax-exempt component unit of the Health Center and has a year end of December 31. The Foundation's financial statements have been included as a discretely presented component unit. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the Health Center in support of its operations and programs. The Health Center does not appoint a voting majority of the Foundation's Board of Directors or in any way impose its will over the Foundation. However, the Foundation is included as a discretely presented component unit due to the nature and significance of its relationship to the Health Center.

Basis of Presentation

The balance sheet displays the Health Center'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.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

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

Measurement Focus and Basis of Accounting

Basis of accounting refers to when revenues 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 Health Center reports in accordance with accounting principles generally accepted in the United States of America as specified by the American Institute of Certified Public Accountants' *Audit and Accounting Guide for Health Care Organizations* and, as a governmental entity, also provides certain disclosures required by the Governmental Accounting Standards Board (GASB). The accompanying financial statements have been prepared on the accrual basis of accounting. Revenues are recognized when earned, and expenses are recorded when the liability is incurred.

In reporting its financial activity, the Health Center applies all applicable GASB pronouncements for proprietary funds, 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.

Use of Estimates

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

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with original maturities of three months or less when purchased, excluding assets limited as to use or restricted and investments.

Patient Receivables

Patient receivables are uncollateralized patient and third-party payor obligations. Unpaid patient receivables are not charged interest on amounts owed.

Payments of patient receivables are allocated to the specific claims 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 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.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

Management considers historical write off and recovery information in determining the estimated bad debt provision. Management also reviews accounts to determine if classification as charity care is appropriate.

Property Tax Receivable

Property tax receivable is recognized on the levy or lien date, which is the date the tax asking is certified by the County Board of Supervisors. The succeeding year 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. 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.

Supplies

Supplies are stated at lower of average cost or market.

Land, Buildings, and Equipment

Land, buildings, and equipment acquisitions in excess of \$5,000 are capitalized and are recorded at cost. Land, buildings, and equipment donated for Health Center operations are recorded as additions to net assets at fair value at the date of receipt. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. The estimated useful lives of land, buildings, and equipment are as follows:

Land improvements	8-20 years
Buildings and fixed equipment	5-56 years
Major movable equipment	3-25 years

Investments

Investments are valued at purchase costs, or fair market value at date of acquisition if donated. Investments consist of certificates of deposit with original deposits greater than three months.

Assets Limited As to Use or Restricted

Assets limited as to use or restricted include assets which have been internally designated by the Health Center's Board of Trustees, assets which are restricted by debt agreements and assets which have been restricted by contributors or grantors. Board designated assets remain under the control of the Board of Trustees, which may at its discretion later use the funds for other purposes.

Restricted funds are used to differentiate funds which are limited by the donor to specific uses from funds on which the donor places no restriction or which arise as a result of the operation of the Health Center for its stated purposes. Resources set aside for Board-designated purposes are not considered to be restricted. Resources restricted by donors or grantors for specific operating purposes are reported in nonoperating revenues to the extent expended within the period.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

Compensated Absences

Health Center employees accumulate a limited amount of earned but unused paid leave hours for subsequent use or for payment upon termination, death, or retirement. The cost of paid leave is recorded as a current liability on the balance sheet. The compensated absences liability has been computed based on rates of pay in effect at June 30, 2008.

Deferred Revenue

Although certain revenues are measurable, they are not available. Available means collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Deferred revenue represents the amount of assets that have been recognized, but the related revenue has not been recognized since the assets are not collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Deferred revenue consists of succeeding year property tax receivable.

Operating Revenues and Expenses

The Health Center's statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Health Center's principal activity. Non-exchange revenues, including interest income, taxes, grants and unrestricted contributions, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, including interest expense.

Net Patient Service Revenue

The Health Center has agreements with third-party payors that provide for payments to the Health Center at amounts different from its established rates. Payment arrangements include prospectively determined rates, reimbursed costs, discounted charges, and per diem payments. 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 and a provision for uncollectible accounts. 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.

Grants and Contributions

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 or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

Advertising Costs

Costs incurred for producing and distributing advertising are expensed as incurred. The Health Center incurred \$42,677 and \$41,862 for advertising costs for the years ended June 30, 2008 and 2007, respectively.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

Charity Care

To fulfill its mission of community service, the Health Center 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 Health Center does not pursue collection of the amounts. The resulting adjustments are recorded as adjustments to patient service revenue, depending on the timing of the charity determination.

Investment Income

Interest on cash and deposits is included in nonoperating revenues and expenses.

County Tax Revenue

Taxes are included in nonoperating revenues 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.

Reclassification

Certain items from the 2007 financial statements have been reclassified to conform to the current year presentation.

Other Significant Accounting Policies

Other significant accounting policies are set forth in the financial statements and the notes thereto.

NOTE 2 - CHARITY CARE

The Health Center maintains records to identify and monitor the level of charity care it provides. The amounts of charges foregone for services and supplies furnished under its charity care policy during the years ended June 30, 2008 and 2007, were \$60,235 and \$36,152, respectively. The estimated costs of the charges foregone, based upon Health Center's overall cost to charge ratio calculation, for the years ended June 30, 2008 and 2007, were \$41,000 and \$23,000, respectively.

NOTE 3 - NET PATIENT SERVICE REVENUE

The Health Center has agreements with third-party payors that provide for payments to the Health Center at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

Medicare

The Health Center is licensed as a Critical Access Health Center (CAH). The Health Center is reimbursed for most inpatient and outpatient services at cost with final settlement determined after submission of annual cost reports by the Health Center and are subject to audits thereof by the Medicare fiscal intermediary. The Health Center's Medicare cost reports have been settled by the Medicare fiscal intermediary through the year ended June 30, 2006. The Health Center'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 Health Center.

Medicaid

Inpatient and outpatient services rendered to Medicaid program beneficiaries are paid based on a cost reimbursement methodology. The Health Center is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Health Center and audits thereof by the Medicaid fiscal intermediary. The Health Center's Medicaid cost reports have been processed by the Medicaid fiscal intermediary through June 30, 2005.

Other Payors

The Health Center has also entered into payment agreements with Blue Cross and other commercial insurance carriers. The basis for reimbursement under these agreements may include discounts from established charges and prospectively determined rates.

Laws and regulations governing Medicare, Medicaid, and other programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Revenue from the Medicare and Medicaid programs accounted for approximately 52% and 7%, respectively, of the Health Center's net patient service revenue for the year ended June 30, 2008, and 56% and 6%, respectively, of the Health Center's net patient service revenue, for the year ended June 30, 2007.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

A summary of patient service revenue, contractual adjustments, and provision for bad debts for the years ended June 30, 2008 and 2007, is as follows:

	<u>2008</u>	<u>2007</u>
Total patient service revenue	<u>\$ 28,231,182</u>	<u>\$ 26,936,176</u>
Contractual adjustments:		
Medicare	(4,759,367)	(5,484,309)
Medicaid	(830,790)	(725,655)
Other	<u>(2,338,213)</u>	<u>(2,230,409)</u>
Total contractual adjustments	<u>(7,928,370)</u>	<u>(8,440,373)</u>
Net patient service revenue	20,302,812	18,495,803
Provision for bad debts	<u>(848,661)</u>	<u>(567,280)</u>
Net patient service revenue (net of provision for bad debts)	<u>\$ 19,454,151</u>	<u>\$ 17,928,523</u>

NOTE 4 - CASH AND DEPOSITS

The Health Center's deposits in banks at June 30, 2008 and 2007, 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 Health Center is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; 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; certain joint investment trusts, and warrants or improvement certificates of a drainage district.

Investments reported are not subject to risk categorization. Amounts classified as investments in the financial statements are presented as cash and deposits in this note.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

At June 30, 2008 and 2007, the Health Center's carrying amounts of cash and deposits are as follows:

	<u>2008</u>	<u>2007</u>
Checking and savings accounts	\$ 376,003	\$ 982,594
Certificates of deposit	<u>2,588,369</u>	<u>3,625,433</u>
Total deposits	<u>\$ 2,964,372</u>	<u>\$ 4,608,027</u>

Included in the following balance sheet captions:

Investments	\$ 1,078,039	\$ 1,890,937
Assets limited as to use or restricted	<u>1,886,333</u>	<u>2,717,090</u>
	<u>\$ 2,964,372</u>	<u>\$ 4,608,027</u>

Interest rate risk is the exposure to fair value losses resulting from rising interest rates. The Health Center's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Health Center. Maturities are consistent with this policy.

At December 31, 2007 and 2006, the Foundation's carrying amounts of cash and deposits are as follows:

	<u>2007</u>	<u>2006</u>
Checking and savings accounts	\$ 98,152	\$ 52,814
Certificates of deposit	54,449	51,842
Mutual funds	<u>1,791,909</u>	<u>1,659,055</u>
Total deposits	<u>\$ 1,944,510</u>	<u>\$ 1,763,711</u>

NOTE 5 - LAND, BUILDINGS, AND EQUIPMENT

Summaries of land, buildings, and equipment at June 30, 2008 and 2007, are as follows:

	June 30, 2007				June 30, 2008
	<u>Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Transfers</u>	<u>Balance</u>
Land, buildings, and equipment					
Land and land improvements	\$ 628,709	\$ -	\$ -	\$ -	\$ 628,709
Buildings	6,683,391	70,061	(460)	383,393	7,136,385
Fixed equipment	2,579,375	91,474	(18,085)	186,764	2,839,528
Major movable equipment	4,652,469	217,942	(34,217)	-	4,836,194
Construction in progress	<u>426,020</u>	<u>1,622,647</u>	<u>-</u>	<u>(570,157)</u>	<u>1,478,510</u>
Total	<u>14,969,964</u>	<u>\$ 2,002,124</u>	<u>\$ (52,762)</u>	<u>\$ -</u>	<u>16,919,326</u>

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

	June 30, 2007				June 30, 2008
	Balance	Additions	Deductions	Transfers	Balance
Accumulated depreciation					
Land improvements	\$ 355,202	\$ 26,774	\$ -	\$ -	\$ 381,976
Buildings	3,382,829	265,754	(459)	-	3,648,124
Fixed equipment	2,162,516	101,391	(18,085)	-	2,245,822
Major movable equipment	3,504,704	376,989	(34,217)	-	3,847,476
Total	9,405,251	\$ 770,908	\$ (52,761)	\$ -	10,123,398
Land, buildings, and equipment, net	\$ 5,564,713				\$ 6,795,928
	June 30, 2006				June 30, 2007
	Balance	Additions	Deductions	Transfers	Balance
Land, buildings, and equipment					
Land and land improvements	\$ 526,301	\$ -	\$ -	\$ 102,408	\$ 628,709
Buildings	6,479,290	-	(84,465)	288,566	6,683,391
Fixed equipment	2,526,381	91,517	(38,523)	-	2,579,375
Major movable equipment	4,702,534	153,079	(203,144)	-	4,652,469
Construction in progress	157,084	659,910	-	(390,974)	426,020
Total	14,391,590	\$ 904,506	\$ (326,132)	\$ -	14,969,964
Accumulated depreciation					
Land improvements	332,241	\$ 22,961	\$ -	\$ -	355,202
Buildings	3,184,523	243,798	(45,492)	-	3,382,829
Fixed equipment	2,111,206	90,029	(38,719)	-	2,162,516
Major movable equipment	3,340,712	367,116	(203,124)	-	3,504,704
Total	8,968,682	\$ 723,904	\$ (287,335)	\$ -	9,405,251
Land, buildings, and equipment, net	\$ 5,422,908				\$ 5,564,713

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

The majority of construction in progress at June 30, 2008, represents costs incurred for various construction projects at the Health Center. The projects include a clinic expansion, electronic medical records project, three story project, and signage update. The clinic expansion and electronic medical records project are expected to be completed in the fall of 2008 at an estimated total cost of \$780,000 and \$1,500,000, respectively. The three story project is expected to be completed in the spring of 2010 with an estimated total cost of \$11,000,000. It will be financed primarily through the issuance of long-term debt. The signage update project is expected to be completed in the winter of 2009 at an estimated total cost of \$50,000. The projects other than the three story project will be financed with the Health Center's cash reserves.

NOTE 6 - LONG-TERM DEBT

A schedule of changes in long-term debt for 2008 and 2007, is as follows:

	June 30, 2007			June 30, 2008	Amounts Due
	Balance	Additions	Payments	Balance	Within One Year
Promissory note payable	\$ 30,000	\$ -	\$ (10,000)	\$ 20,000	\$ 10,000
Hospital revenue note	421,496	-	(109,562)	311,934	115,627
Total long-term debt	<u>\$ 451,496</u>	<u>\$ -</u>	<u>\$ (119,562)</u>	<u>331,934</u>	<u>\$ 125,627</u>
Less current maturities				(125,627)	
Long-term debt, less current maturities				<u>\$ 206,307</u>	
	June 30, 2006			June 30, 2007	Amounts Due
	Balance	Additions	Payments	Balance	Within One Year
Promissory note payable	\$ 40,000	\$ -	\$ (10,000)	\$ 30,000	\$ 10,000
Hospital revenue note	525,311	-	(103,815)	421,496	109,562
Total long-term debt	<u>\$ 565,311</u>	<u>\$ -</u>	<u>\$ (113,815)</u>	451,496	<u>\$ 119,562</u>
Less current maturities				(119,562)	
Long-term debt, less current maturities				<u>\$ 331,934</u>	

Promissory Note Payable

On March 1, 2000, the Health Center entered into a promissory note payable agreement with Humboldt County Rural Electric Cooperative. The note provided for the Health Center to receive \$100,000 to be used in the operating suite renovation project. The note is a non-interest bearing note and calls for the repayment of principal in 10 annual installments beginning on March 1, 2001.

Hospital Revenue Note

On March 1, 2000, the Health Center entered into an agreement with Iowa State Bank, Algona, Iowa, for the issuance of a \$1,000,000 Hospital Revenue Note. The net proceeds from the note were used to fund the Health Center's operating suite renovation project. Beginning on February 1, 2001 and continuing through January 1, 2011, principal and interest is due the first of each month at the 5.4% interest. The note is collateralized by the revenues of the Health Center.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

Aggregate future payments of principal and interest on the long-term debt obligations are as follows:

<u>Year Ending June 30,</u>	<u>Long-term Debt</u>	
	<u>Principal</u>	<u>Interest</u>
2009	\$ 125,627	\$ 14,011
2010	132,028	7,610
2011	<u>74,279</u>	<u>1,343</u>
	<u>\$ 331,934</u>	<u>\$ 22,964</u>

NOTE 7 - LEASES

The Health Center leases certain equipment and building space under noncancelable long-term lease agreements. Total lease expense for the years ended June 30, 2008 and 2007, for all leases was \$175,088 and \$46,696, respectively.

Minimum future lease payments for the noncancelable leases are as follows:

<u>Year Ending June 30,</u>	<u>Equipment</u>	<u>Building</u>
	2009	\$ 140,103
2010	140,103	-
2011	<u>93,378</u>	<u>-</u>
	<u>\$ 373,584</u>	<u>\$ 11,228</u>

The above schedule reflects minimum future lease payments for building space through October 2008. Effective November 2008 through October 2016, minimum future lease payments will be adjusted to 60% of the Landlord's remaining principle and interest payments related to the building.

NOTE 8 - PENSION AND RETIREMENT BENEFITS

The Health Center contributes to the Iowa Public Employees Retirement Center (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, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

Plan members are required to contribute 3.90% of their annual covered salary, and the Health Center is required to contribute 6.05% of their annual covered payroll for the year ended June 30, 2008. Plan members were required to contribute 3.70% of their annual covered salary, and the Health Center was required to contribute 5.75% of annual covered payroll for the years ended June 30, 2007 and 2006. Contribution requirements are established by State statute. The Health Center's contribution to IPERS for the years ended June 30, 2008, 2007, and 2006, were \$417,676, \$360,425, and \$330,082, respectively, equal to the required contributions for each year.

NOTE 9 - RELATED ORGANIZATIONS

Master Affiliation Agreement

The Health Center has a Master Affiliation Agreement with Mercy Medical Center – North Iowa (MMC-NI) to provide hospital, physician, and other health care services in Kossuth and surrounding counties in north central Iowa. As a part of this Master Affiliation Agreement, the Health Center entered into a Professional Service Agreement with MMC-NI whereby MMC-NI provides professional medical services for the Health Center. Amounts paid to MMC-NI for the provision of these services amounted to \$3,389,068 and \$3,046,826 for the years ended June 30, 2008 and 2007, respectively.

Operating gains and losses from the consolidated operation of the Health Center and MMC-NI services are shared equally in accordance with the formulas outlined in the Master Affiliation Agreement. Total operating gains to be allocated to MMC-NI amounted to \$118,692 and \$499,562, respectively, for the years ended June 30, 2008 and 2007, for the various services and distributions related to these agreements.

Management Services Agreement

The Health Center has a contractual arrangement with MMC-NI under which MMC-NI provides administrative staff, management consultation, and other services to the Health Center. The arrangement does not alter the authority or responsibility of the Board of Trustees of the Health Center. Expenses for the administrative and management services for the years ended June 30, 2008 and 2007, were \$439,340 and \$400,015, respectively.

Due to and from Affiliated Organization

As of June 30, 2008 and 2007, the Health Center's records reflect an amount due to MMC-NI of \$304,666 and \$838,228, respectively, for the various services and distributions related to these agreements.

Other Related Organizations

Auxiliary

The Kossuth County Hospital Auxiliary was established to advance and to promote the welfare of Kossuth Regional Health Center through ways and means approved by the Board of Directors of the Health Center auxiliary and endorsed by the Health Center administrator. The Auxiliary's unrestricted resources are distributed to the Health Center in amounts and in periods determined by the Auxiliary's Board of Directors.

Foundation

The Kossuth Regional Health Center Foundation was established to solicit funds and make contributions to the Kossuth Regional Health Center. The Foundation made contributions to the Health Center during the years ended June 30, 2008 and 2007, of \$21,866 and \$10,000, respectively.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

NOTE 10 - CONTINGENCIES

Malpractice Insurance

The Health Center has insurance coverage to provide protection for professional liability losses on a claims made basis subject to a limit of \$1 million per claim and an aggregate limit of \$3 million. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term, but reported subsequently, will be uninsured.

Self-Funded Employee Health Insurance Plan

The Health Center has a self-funded employee health insurance plan covering substantially all employees. The plan is responsible to pay all administration expenses and benefits up to the reinsurance limits. Liabilities of \$232,000 and \$200,000 have been established to record the incurred but not reported claims outstanding at June 30, 2008 and 2007, respectively.

Healthcare Legislation and Regulation

The healthcare 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 healthcare program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violation of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Management believes that the Health Center is in substantial compliance with fraud and abuse as well as other applicable government laws and regulations. While no regulatory inquiries have been made, compliance with such laws and regulations is subject to government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

NOTE 11 - RISK MANAGEMENT

The Health Center 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. The Health Center assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

The Health Center's employees participate in a self-funded health plan (Plan). The amounts payable from the Plan at June 30, 2008 and 2007, total \$232,000 and \$200,000, respectively, which is for incurred but not reported (IBNR) and reported but not paid claims. The amounts are based on estimates of the amounts necessary to pay current year claims. The Plan has purchased stop loss coverage.

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

NOTE 12 - CONCENTRATION OF CREDIT RISK

The Health Center grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. The mix of receivables from third-party payors and patients at June 30, 2008 and 2007, was as follows:

	<u>2008</u>	<u>2007</u>
Medicare	32%	33%
Medicaid	6	6
Blue Cross	18	19
Other third-party payors and patients	<u>44</u>	<u>42</u>
	<u>100%</u>	<u>100%</u>

KOSSUTH REGIONAL
HEALTH CENTER

KOSSUTH REGIONAL HEALTH CENTER
BUDGETARY COMPARISON SCHEDULE OF REVENUES, EXPENSES, AND CHANGES IN NET
ASSETS – BUDGET AND ACTUAL (CASH BASIS)
YEAR ENDED JUNE 30, 2008

	Actual Accrual Basis	Accrual Adjustments	Actual Cash Basis	Budget	Variance Favorable (Unfavorable)
Estimated amount to be raised by taxation	\$ 295,753	\$ -	\$ 295,753	\$ 298,000	\$ (2,247)
Estimated other revenues/receipts	<u>23,022,956</u>	<u>(1,455,030)</u>	<u>21,567,926</u>	<u>24,314,369</u>	<u>(2,746,443)</u>
	23,318,709	(1,455,030)	21,863,679	24,612,369	(2,748,690)
Expenses/disbursements	<u>22,565,313</u>	<u>1,521,123</u>	<u>24,086,436</u>	<u>24,413,435</u>	<u>326,999</u>
Net	753,396	(2,976,153)	(2,222,757)	198,934	<u>\$ (2,421,691)</u>
Balance beginning of year	<u>13,241,466</u>	<u>(7,125,984)</u>	<u>6,115,482</u>	<u>4,989,591</u>	
Balance end of year	<u>\$13,994,862</u>	<u>\$ (10,102,137)</u>	<u>\$ 3,892,725</u>	<u>\$ 5,188,525</u>	

KOSSUTH REGIONAL HEALTH CENTER
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING
YEAR ENDED JUNE 30, 2008

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 resulting from the Health Center preparing a budget on the cash basis of accounting.

The Board of Trustees annually prepares and adopts a budget designating the amount necessary for the improvement and maintenance of the Health Center 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 budget was not amended during the year ended June 30, 2008.

For the year ended June 30, 2008, the Health Center's expenditures did not exceed the amount budgeted.

**KOSSUTH REGIONAL
HEALTH CENTER**



CPAs & BUSINESS ADVISORS

INDEPENDENT AUDITOR'S REPORT ON SUPPLEMENTARY INFORMATION

The Board of Trustees
Kossuth Regional Health Center
Algona, Iowa

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information, except for the Schedules of Statistical Information on page 39 marked "unaudited," has been subjected to the auditing procedures applied in the audits 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.

A handwritten signature in black ink that reads "Eide Bailly LLP".

Dubuque, Iowa
September 18, 2008

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KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF NET PATIENT SERVICE REVENUE
YEARS ENDED JUNE 30, 2008 AND 2007

	TOTAL	
	2008	2007
PATIENT CARE SERVICES		
Adults and pediatrics	\$ 1,529,946	\$ 1,406,155
Intensive care unit	33,478	48,488
Swing-bed	340,497	295,862
Intermediate care	1,162	840
Nursery	<u>108,603</u>	<u>103,395</u>
Subtotal	<u>2,013,686</u>	<u>1,854,740</u>
OTHER PROFESSIONAL SERVICES		
Operating room	1,935,964	2,021,886
Labor and delivery room	65,400	60,664
Anesthesiology	802,800	982,104
Radiology	1,867,308	1,740,610
Laboratory	3,272,383	3,252,366
Respiratory therapy	241,649	181,855
Cardiac rehabilitation	186,692	155,829
Physical therapy	1,499,429	1,461,420
Occupational therapy	323,181	301,817
Speech therapy	13,761	8,464
Electrocardiology	1,560	761
Scans	2,974,831	2,618,709
Medical and surgical supplies	809,735	982,165
Pharmacy	1,942,735	2,067,108
Intravenous therapy	451,388	504,094
Clinics	7,185,840	6,591,442
Emergency room	1,037,187	919,731
Home health	71,635	39,903
Hospice	1,540,377	1,185,069
Immunizations	5,860	6,452
Diabetic education	<u>48,016</u>	<u>35,139</u>
Subtotal	<u>26,277,731</u>	<u>25,117,588</u>
Total	28,291,417	26,972,328
Charity Care	<u>(60,235)</u>	<u>(36,152)</u>
Total patient service revenue	28,231,182	26,936,176
Adjustments to patient service revenue	<u>(8,777,031)</u>	<u>(9,007,653)</u>
NET PATIENT SERVICE REVENUE	<u>\$ 19,454,151</u>	<u>\$ 17,928,523</u>

INPATIENT		OUTPATIENT	
2008	2007	2008	2007
\$ 1,416,555	\$ 1,312,214	\$ 113,391	\$ 93,941
33,478	48,488	-	-
340,497	295,862	-	-
1,162	840	-	-
<u>108,603</u>	<u>103,395</u>	<u>-</u>	<u>-</u>
<u>1,900,295</u>	<u>1,760,799</u>	<u>113,391</u>	<u>93,941</u>
182,969	252,096	1,752,995	1,769,790
64,530	60,178	870	486
173,254	239,608	629,546	742,496
100,830	108,386	1,766,478	1,632,224
530,128	593,588	2,742,255	2,658,778
221,780	169,313	19,869	12,542
551	341	186,141	155,488
336,962	310,434	1,162,467	1,150,986
188,792	159,296	134,389	142,521
3,636	2,113	10,125	6,351
1,560	761	-	-
279,918	244,366	2,694,913	2,374,343
228,029	275,371	581,706	706,794
703,355	739,128	1,239,380	1,327,980
242,909	271,605	208,479	232,489
-	-	7,185,840	6,591,442
28,584	24,295	1,008,603	895,436
-	-	71,635	39,903
149,090	112,753	1,391,287	1,072,316
-	-	5,860	6,452
-	-	<u>48,016</u>	<u>35,139</u>
<u>3,436,877</u>	<u>3,563,632</u>	<u>22,840,854</u>	<u>21,553,956</u>
\$ <u>5,337,172</u>	\$ <u>5,324,431</u>	\$ <u>22,954,245</u>	\$ <u>21,647,897</u>

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF ADJUSTMENTS TO PATIENT SERVICE REVENUE
AND OTHER OPERATING REVENUES
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
ADJUSTMENTS TO PATIENT SERVICE REVENUE		
Contractual adjustments - Medicare	\$ 4,759,367	\$ 5,484,309
Contractual adjustments - Medicaid	830,790	725,655
Provision for bad debts	848,661	567,280
Other allowances and adjustments	<u>2,338,213</u>	<u>2,230,409</u>
TOTAL ADJUSTMENTS	<u>\$ 8,777,031</u>	<u>\$ 9,007,653</u>
OTHER OPERATING REVENUES		
Retail pharmacy	\$ 2,668,913	\$ 2,398,628
Grants	393,539	444,168
Rental income	65,340	77,221
Cafeteria	53,929	42,411
Prisoner meals	11,465	60,687
Meals on Wheels	5,102	23,015
Medical records fees	3,136	2,988
Miscellaneous	<u>28,429</u>	<u>16,896</u>
TOTAL OTHER OPERATING REVENUES	<u>\$ 3,229,853</u>	<u>\$ 3,066,014</u>

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF OPERATING EXPENSES
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
ADULTS AND PEDIATRICS		
Salaries and wages	\$ 1,331,887	\$ 1,111,807
Other	<u>401,255</u>	<u>192,319</u>
	<u>1,733,142</u>	<u>1,304,126</u>
NURSERY		
Salaries and wages	11,290	11,380
Other	<u>3,499</u>	<u>6,310</u>
	<u>14,789</u>	<u>17,690</u>
OPERATING ROOM		
Salaries and wages	319,980	305,943
Other	<u>232,357</u>	<u>218,795</u>
	<u>552,337</u>	<u>524,738</u>
LABOR AND DELIVERY ROOMS		
Salaries and wages	21,208	14,204
Other	<u>4,790</u>	<u>5,871</u>
	<u>25,998</u>	<u>20,075</u>
ANESTHESIOLOGY		
Other	<u>373,230</u>	<u>433,241</u>
RADIOLOGY		
Salaries and wages	305,760	274,085
Other	<u>202,260</u>	<u>313,976</u>
	<u>508,020</u>	<u>588,061</u>
LABORATORY		
Salaries and wages	315,313	283,380
Other	<u>428,518</u>	<u>433,069</u>
	<u>743,831</u>	<u>716,449</u>
BLOOD		
Salaries and wages	19,267	14,549
Other	<u>71,609</u>	<u>93,967</u>
	<u>90,876</u>	<u>108,516</u>
RESPIRATORY THERAPY		
Salaries and wages	6,918	8,757
Other	<u>85,621</u>	<u>64,749</u>
	<u>92,539</u>	<u>73,506</u>
CARDIAC REHABILITATION		
Salaries and wages	16,974	9,531
Other	<u>34,931</u>	<u>32,297</u>
	<u>51,905</u>	<u>41,828</u>

(continued on next page)

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF OPERATING EXPENSES – PAGE 2
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
PHYSICAL THERAPY		
Salaries and wages	\$ 124,403	\$ 117,568
Other	<u>409,271</u>	<u>426,807</u>
	<u>533,674</u>	<u>544,375</u>
OCCUPATIONAL THERAPY		
Salaries and wages	123,407	120,341
Other	<u>10,282</u>	<u>12,801</u>
	<u>133,689</u>	<u>133,142</u>
SPEECH THERAPY		
Salaries and wages	11,256	-
Other	<u>409</u>	<u>5,824</u>
	<u>11,665</u>	<u>5,824</u>
ELECTROCARDIOLOGY		
Salaries and wages	3,315	4,831
Other	<u>1,552</u>	<u>1,468</u>
	<u>4,867</u>	<u>6,299</u>
SCANS		
Salaries and wages	341	891
Other	<u>543,839</u>	<u>473,393</u>
	<u>544,180</u>	<u>474,284</u>
MEDICAL AND SURGICAL SUPPLIES		
Other	<u>165,905</u>	<u>222,060</u>
PHARMACY AND INTRAVENOUS THERAPY		
Salaries and wages	18,160	-
Other	<u>599,689</u>	<u>664,926</u>
	<u>617,849</u>	<u>664,926</u>
RETAIL PHARMACY		
Salaries and wages	237,250	214,395
Other	<u>2,187,760</u>	<u>1,994,370</u>
	<u>2,425,010</u>	<u>2,208,765</u>
CLINICS		
Salaries and wages	1,657,356	1,511,213
Other	<u>3,147,977</u>	<u>2,758,812</u>
	<u>4,805,333</u>	<u>4,270,025</u>
REJUVENATION CLINIC		
Salaries and wages	197	-
Other	<u>6,138</u>	<u>6,839</u>
	<u>6,335</u>	<u>6,839</u>

(continued on next page)

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF OPERATING EXPENSES – PAGE 3
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
EMERGENCY SERVICES		
Salaries and wages	\$ 189,229	\$ 166,170
Other	<u>486,053</u>	<u>466,809</u>
	<u>675,282</u>	<u>632,979</u>
HOME HEALTH		
Salaries and wages	759,935	767,265
Other	<u>242,704</u>	<u>213,248</u>
	<u>1,002,639</u>	<u>980,513</u>
HOSPICE		
Salaries and wages	138,391	112,608
Other	<u>71,550</u>	<u>54,082</u>
	<u>209,941</u>	<u>166,690</u>
MEDICAL RECORDS		
Salaries and wages	216,211	209,815
Other	<u>54,024</u>	<u>42,595</u>
	<u>270,235</u>	<u>252,410</u>
DIETARY		
Salaries and wages	208,124	178,816
Other	<u>112,445</u>	<u>117,807</u>
	<u>320,569</u>	<u>296,623</u>
OPERATION OF PLANT		
Salaries and wages	181,012	170,040
Other	<u>367,755</u>	<u>289,810</u>
	<u>548,767</u>	<u>459,850</u>
HOUSEKEEPING		
Salaries and wages	148,901	137,121
Other	<u>27,914</u>	<u>22,842</u>
	<u>176,815</u>	<u>159,963</u>
LAUNDRY AND LINEN		
Other	<u>63,619</u>	<u>62,478</u>
ADMINISTRATIVE SERVICES		
Salaries and wages	789,381	687,074
Other	<u>1,225,194</u>	<u>1,009,412</u>
	<u>2,014,575</u>	<u>1,696,486</u>
UNASSIGNED EXPENSES		
Depreciation	770,907	723,904
Interest and amortization	20,076	25,822
Employee benefits	<u>2,938,022</u>	<u>2,172,926</u>
	<u>3,729,005</u>	<u>2,922,652</u>
TOTAL OPERATING EXPENSES	<u>\$ 22,446,621</u>	<u>\$ 19,995,413</u>

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF PATIENT RECEIVABLES AND ALLOWANCE FOR DOUBTFUL ACCOUNTS
JUNE 30, 2008 AND 2007

ANALYSIS OF AGING

Age of Accounts	2008		2007	
	Amount	Percent to Total	Amount	Percent to Total
30 days or less	\$ 2,617,394	53.29%	\$ 2,288,338	56.80%
31 to 60 days	803,834	16.37%	721,278	17.91%
61 to 90 days	407,128	8.29%	283,399	7.04%
91 days and over	1,083,192	22.05%	735,253	18.25%
	<u>4,911,548</u>	<u>100.00%</u>	<u>4,028,268</u>	<u>100.00%</u>
Less: Allowance for doubtful accounts	612,432		459,391	
Allowance for contractual adjustments	<u>935,450</u>		<u>864,834</u>	
Net	<u>\$ 3,363,666</u>		<u>\$ 2,704,043</u>	
Net patient service revenue per calendar day	<u>\$ 53,299</u>		<u>\$ 49,119</u>	
Days of net revenue in net accounts receivable at year end	<u>63</u>		<u>55</u>	

ANALYSIS OF ALLOWANCE FOR DOUBTFUL ACCOUNTS

	2008		2007	
	Amount	Percent of Net Patient Service Revenue	Amount	Percent of Net Patient Service Revenue
Beginning balance	<u>\$ 459,391</u>		<u>\$ 402,169</u>	
Add:				
Provision for bad debts	848,661	4.36%	567,280	3.16%
Recoveries previously written off	<u>187,875</u>	<u>0.97%</u>	<u>162,818</u>	<u>0.91%</u>
	<u>1,036,536</u>		<u>730,098</u>	
Less:				
Accounts written off	<u>(883,495)</u>	<u>4.54%</u>	<u>(672,876)</u>	<u>3.75%</u>
Ending balance	<u>\$ 612,432</u>		<u>\$ 459,391</u>	

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF SUPPLIES AND PREPAID EXPENSE
JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
SUPPLIES		
Retail pharmacy	\$ 254,882	\$ 233,518
Central supply	77,072	104,903
Pharmacy	46,782	31,175
Clinics	42,942	50,404
Other departments	<u>97,044</u>	<u>104,438</u>
Total supplies	<u>\$ 518,722</u>	<u>\$ 524,438</u>
PREPAID EXPENSE		
Insurance	\$ 117,789	\$ 51,955
Other	<u>403,525</u>	<u>365,507</u>
Total prepaid expense	<u>\$ 521,314</u>	<u>\$ 417,462</u>

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULES OF STATISTICAL INFORMATION (UNAUDITED)
YEARS ENDED JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
PATIENT DAYS		
Acute	2,156	2,214
Swing-bed	1,113	1,023
Newborn	214	218
Totals	<u>3,483</u>	<u>3,455</u>
ADMISSIONS		
Acute	686	716
Swing-bed	134	125
Totals	<u>820</u>	<u>841</u>
DISCHARGES		
Acute	688	713
Swing-bed	136	123
Totals	<u>824</u>	<u>836</u>
ACUTE AVERAGE LENGTH OF STAY	<u>3.1</u>	<u>3.1</u>
SWING-BED AVERAGE LENGTH OF STAY	<u>8.2</u>	<u>8.3</u>
ACUTE BEDS	<u>25</u>	<u>25</u>
PERCENTAGE OF OCCUPANCY		
Acute, based on 25 beds	<u>23.63%</u>	<u>24.26%</u>
Swing-bed, based on 25 beds	<u>12.20%</u>	<u>11.21%</u>



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**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**

The Board of Trustees
Kossuth Regional Health Center
Algona, Iowa

We have audited the accompanying balance sheets of Kossuth Regional Health Center (Health Center) as of June 30, 2008 and 2007, and its discretely presented component unit as of December 31, 2007 and 2006, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended and have issued our report thereon dated September 18, 2008. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Health Center's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of the Health Center's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Health Center's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Health Center's ability to initiate, authorize, record, process, or report financial data reliably in accordance with accounting principles generally accepted in the United States of America such that there is more than a remote likelihood a misstatement of the Health Center's financial statements that is more than inconsequential will not be prevented or detected by the Health Center's internal control. We consider the deficiencies in internal control described in Part I of the accompanying Schedule of Findings to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies that results in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by the Health Center's internal control.

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Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements of the Health Center 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 or other matters that are required to be reported under *Government Auditing Standards*.

Comments involving statutory and other legal matters about the Health Center's operations for the year ended June 30, 2008, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Health Center and are reported in Part II of the accompanying Schedule of Findings and Responses. 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.

Kossuth Regional Health Center's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Responses. While we have expressed our conclusions on the Health Center's responses, we did not audit Kossuth Regional Health Center's responses, and accordingly, we express no opinion on them.

We also noted a certain additional matter that we reported to management in a separate letter dated September 18, 2008.

This report, a public record by law, is intended solely for the information and use of the officials, employees, and constituents of Kossuth Regional Health Center and other parties to whom Kossuth Regional Health Center, may report. 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 Kossuth Regional Health Center during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

A handwritten signature in black ink that reads "Erik Sully LLP". The signature is written in a cursive, flowing style.

Dubuque, Iowa
September 18, 2008

KOSSUTH REGIONAL HEALTH CENTER
SCHEDULE OF FINDINGS AND RESPONSES
YEAR ENDED JUNE 30, 2008

Part I: Findings Related to the Financial Statements:

SIGNIFICANT DEFICIENCIES:

I-A-08 Segregation of Duties – One important aspect of internal controls is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The limited number of office personnel prevents a proper segregation of accounting functions necessary to assure optimal internal control. This is not an unusual condition in organizations of your size.

Recommendation –We realize that with a limited number of office employees, segregation of duties is difficult. We also recognize that in some instances it may not be cost effective to employ additional personnel for the purpose of segregating duties. However, the Health Center should continually review its internal control procedures, other compensating controls and monitoring procedures to obtain the maximum internal control possible under the circumstances. Management involvement through the review of reconciliation procedures can be an effective control to ensure these procedures are being accurately completed on a timely basis. Furthermore, the Health Center should periodically evaluate its procedures to identify potential areas where the benefits of further segregation of duties or addition of other compensating controls and monitoring procedures exceed the related costs.

Response – Management agrees with the finding and has reviewed the operating procedures of the Health Center. Due to the limited number of office employees, management will continue to monitor the Health Center’s operations and procedures. Furthermore, we will continually review the assignment of duties, other compensating controls, and monitoring procedures to obtain the maximum internal control possible under the circumstances.

Conclusion – Response accepted.

I-B-08 Preparation of Financial Statements – Management is responsible for establishing and maintaining internal controls over financial reporting and procedures related to the fair presentation of the financial statements in accordance with U.S. generally accepted accounting principles (GAAP). The Health Center does not have an internal control system designed to provide for the preparation of the financial statements, including the accompanying footnotes and statement of cash flows, as required by generally accepted accounting principles. The guidance in Statement of Auditing Standards No. 112, *Communicating Internal Control Related Matters Identified in an Audit*, requires us to communicate this matter to those charged with governance.

As auditors, we were requested to draft the financial statements and accompanying notes to the financial statements. The outsourcing of these services is not unusual in an organization of your size.

Recommendation – We realize that obtaining the expertise necessary to prepare the financial statements, including all necessary disclosures, in accordance with generally accepted accounting principles can be considered costly and ineffective. However, it is the responsibility of the Health Center’s management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

**KOSSUTH REGIONAL HEALTH CENTER
SCHEDULE OF FINDINGS AND RESPONSES
YEAR ENDED JUNE 30, 2008**

Part I: Findings Related to the Financial Statements: (continued)

Response – Management feels that committing the resources necessary to remain current on GAAP and GASB reporting requirements and corresponding footnote disclosures would lack benefit in relation to the cost, but will continue evaluating on a going forward basis.

Conclusion – Response accepted.

Part II: Other Findings Related to Required Statutory Reporting:

- II-A-08 Certified Budget – Health Center disbursements during the year ended June 30, 2008, did not exceed the amount budgeted.
- II-B-08 Questionable Expenditures – We noted no expenditures that we believe would be in conflict with the requirements of public purpose as defined in an Attorney General’s opinion dated April 25, 1979.
- II-C-08 Travel Expense – No expenditures of Health Center money for travel expenses of spouses of Health Center officials and/or employees were noted.
- II-D-08 Business Transactions – We noted no material business transactions between the Health Center and Health Center officials and/or employees.
- II-E-08 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.
- II-F-08 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of the Code of Iowa and the Health Center’s investment policy were noted.
- II-G-08 Publication of Bills Allowed and Salaries – The Health Center is organized under Chapter 347A and is not required to follow this section of the Iowa Code.



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To the Board of Trustees
Kossuth Regional Health Center
Algona, Iowa

We have audited the financial statements of Kossuth Regional Health Center (Health Center) for the year ended June 30, 2008, and have issued our report thereon dated September 18, 2008. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under Auditing Standards Generally Accepted in the United States of America and Government Auditing Standards

As stated in our engagement letter dated June 4, 2008, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

As part of our audit, we considered the internal control of Kossuth Regional Health Center. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Health Center's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our engagement letter and discussion with management about planning matters.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by Kossuth Regional Health Center are described in Note 1 to the financial statements. No new accounting policies were adopted, and the application of existing policies was not changed during the year ended June 30, 2008. We noted no transactions entered into by the Health Center during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

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Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements relate to the collectibility of patient receivables, the amounts either owed to or receivable from third-party payors, and the liability for self-insured employee medical insurance for claims incurred but not reported at year-end.

Management's estimate of the collectibility of patient receivables is based on historical trends for uncollectible accounts and contractual adjustments. The estimate of the amounts either owed to or receivable from third-party payors is based on both final and tentatively settled cost reports. The estimate for the claims incurred but not reported at year-end related to the Health Center's self-insured employee health plan is based on historical trends. We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole. However, laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. There is a reasonable possibility that recorded estimates will change by a material amount in the near term. Management believes the estimates for all open years are adequate. Any differences between the estimates and the final settlements will be recorded in the period the final settlements are made and will not be treated as prior period adjustments.

The disclosures in the financial statements are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

We discussed all adjustments to the financial statements with the Health Center's staff during the audit. The following adjustments were made during the fiscal year 2008 audit:

Increase in net assets prior to audit adjustments	\$ 745,889
To adjust self-funded health insurance liability	(127,455)
To adjust estimated third-party payor settlements	127,110
To adjust payable to affiliate	21,084
To record additional account payable	<u>(13,232)</u>
Increase in net assets as reported	<u>\$ 753,396</u>

There were no significant passed adjustments.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated September 18, 2008.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Health Center's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Health Center's auditors. However, these discussions occurred in the normal course of our professional relationship, and our responses were not a condition to our retention.

Other Comment

We have included an additional comment regarding the Health Center's operations.

This information is intended solely for the use of the officials, employees, and constituents of Kossuth Regional Health Center, and is not intended to be and should not be used by anyone other than these specified parties.

As always, we will be happy to discuss these or any other topics at your convenience. We would like to take this opportunity to express our appreciation to you and your staff for the fine cooperation that we received during the course of the audit. We look forward to many years of continued service to Kossuth Regional Health Center.

A handwritten signature in cursive script that reads "Eide Sully LLP".

Dubuque, Iowa
September 18, 2008

KOSSUTH REGIONAL HEALTH CENTER

YEAR ENDED JUNE 30, 2008
OTHER COMMENTS

Revised Guidelines on Good Governance for Tax Exempt Entities

The issue of corporate governance of tax exempt organizations has emerged as a major focal point for the Internal Revenue Service (IRS) and is a key factor addressed in the newly revised Form 990, Return of Organization Exempt from Income Tax effective for 2008. These guidelines can be found in the IRS document "Governance and Related Topics – 501(c)(3) Organizations," at the following link: http://www.irs.gov/pub/irs-tege/governance_practices.pdf. While tax law does not mandate the guidelines, they are a clear indication of the IRS' strong commitment to monitoring governance practices of the tax-exempt community. The IRS has indicated its belief that a well-governed charity is more likely to obey the tax laws, safeguard charitable assets, and serve charitable interests than one without some of the recommended guidelines. The IRS document is in line with the redesigned Form 990 governance questions and focuses on six specific topics:

- Mission
- Organizational Documents
- Governing Body
- Governance & Management Policies
- Financial Statements & Form 990 Reporting
- Transparency and Accountability

The IRS intends to monitor the organizations' practices by utilizing primarily yes/no questions and detailed descriptions of policies and procedures on the new Form 990.

Although these guidelines are directed towards 501(c)(3) organizations, all tax-exempt entities should consider the same governance practices. We recommend all tax-exempt organizations review the guidelines in detail, as well as the specific questions in Part VI of the 2008 Form 990 and consider whether current practices should be modified or new practices adopted. By reviewing the Health Center's governance practices now, the Health Center will be prepared to respond to the governance-related questions on the 2008 Form 990, if applicable, and portray a positive image to the IRS and the public.