



Financial Statements
June 30, 2011 and 2010

Mitchell County Regional Health Center

Mitchell County Regional Health Center

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June 30, 2011 and 2010

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Mitchell County Regional Health Center
Board of Trustees and Health Center Officials

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
John Lessard	Chairperson	November 30, 2016
Chuck Laures	Vice Chairperson	November 30, 2014
Jan Moody	Secretary/Treasurer	November 30, 2012
Jean Brumm	Member	November 30, 2016
Pat Rourick	Member	November 30, 2012
Don Hendrickson	Member	November 30, 2014
Larry Abel	Member	November 30, 2014
	<u>Health Center Officials</u>	
Sandy Leggett	Administrator	
Alan Streeter	Chief Financial Officer	



Independent Auditor's Report

The Board of Trustees
Mitchell County Regional Health Center
Osage, Iowa

We have audited the accompanying balance sheets of Mitchell County Regional Health Center as of June 30, 2011 and 2010, 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 that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mitchell County Regional Health Center as of June 30, 2011 and 2010, and the respective changes in financial position and its 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 Accounting 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 non-operating 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 non-operating revenues and expenses.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 13, 2011, on our consideration of the Health Center's internal control over financial reporting and on 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.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 10 and the Budgetary Comparison Information on pages 32 and 33 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statement in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Eide Bailly LLP

Dubuque, Iowa
October 13, 2011

This discussion and analysis of the financial performance of Mitchell County Regional Health Center provides an overall review of the Health Center's financial activities and balances as of and for the years ended June 30, 2011, 2010, and 2009. The intent of this discussion is to provide further information on the Health Center's performance as a whole. We encourage readers to consider the information presented here in conjunction with the Health Center's financial statements, including the notes thereto to enhance their understanding of the Health Center's financial status.

Overview of the Financial Statements

The financial statements are composed of the balance sheets, statements of revenues, expenses, and changes in net assets, and the statements of cash flows. The financial statements also include notes that explain in more detail some of the information in the financial statements. The financial statements are designed to provide readers with a broad overview of the Health Center's finances.

The Health Center's financial statements offer short and long term information about its activities. The balance sheets include all of the Health Center's assets and liabilities, as well as the assets of Mitchell County Hospital Auxiliary, and provide information about the nature and amounts of investments in resources (assets) and the obligations to Health Center creditors (liabilities). The balance sheets also provide the basis for evaluating the capital structure of the Health Center and assessing the liquidity and financial flexibility of the Health Center.

All of the current year's revenues and expenses are accounted for in the statements of revenues, expenses, and changes in net assets. These statements measure the success of the Health Center's operations over the past year and can be used to determine whether the Health Center has successfully recovered all of its costs through its patient service revenue and other revenue sources. Revenues and expenses are reported on an accrual basis, which means the related cash could be received or paid in a subsequent period.

The final statement is the statement of cash flows. These statements report cash receipts, cash payments and net changes in cash resulting from operations, investing and financing activities. They also provide answers to such questions as where did cash come from, what was cash used for, and what was the change in cash balance during the reporting period.

Financial Highlights

The Balance Sheet and the Statement of Revenues, Expenses, and Changes in Net Assets report the net assets of the Health Center and the changes in them. The Health Center's net assets - the difference between assets and liabilities - is a way to measure financial health or financial position. Over time, sustained increases or decreases in the Health Center's net assets are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in economic condition, population growth and new or changed governmental legislation should also be considered.

- The Balance Sheet at June 30, 2011, indicates total assets of \$19,858,780, total liabilities of \$5,129,121, and net assets of \$14,729,659.
- The Statements of Revenues, Expenses and Changes in Net Assets indicates total net patient service revenue of \$16,927,030, an increase of 3.60% over the previous fiscal year, total operating expenses of \$16,659,336, an increase of 0.81% over the previous fiscal year, resulting in a gain from operations of \$624,988 before affiliation expenses, a 366.19% increase from the previous year. A net non-operating gain of \$631,670 brings the excess of revenues over expenses to \$969,332 a 36.9% increase over the previous fiscal year.

- The Health Center's current assets exceeded its current liabilities by \$5,575,876 at June 30, 2011, providing a 2.81 current ratio.
- The Health Center recorded an excess of revenues over expenses including capital grants and contributions for fiscal year ending June 30, 2011, amounting to \$ 1,071,469.
- Total patient service revenue increased 8.27% during fiscal year 2011.
- Emergency Room and outpatient visits increased 10.69% during fiscal year 2011.
- Clinic patient visits increased 5.09% during fiscal year 2011.
- Net days in accounts receivable continue to be very favorable at 37 on June 30, 2011.

Organization Highlights

The organization continued to make many positive changes over this last fiscal year, including:

- The Health Center's Senior Management Team and Leadership have spent much of this past fiscal year focusing on the People pillar. There has been much more focus on training staff and development of leaders. With the hiring of a qualified and experienced Human Capital Director with facilitator training, the hospital has been able to provide several different classes in the organization. One area of focus has been to train all leaders and staff members on the skills of Crucial Conversations. These skill sets assist the individual to deal with conversations that consist of strong emotions, opposing opinions and high stakes. There has also been a concentration on developing and coaching our leaders on managerial skills such as how to deal with difficult situations and manage their departments as if it was their own business.
- The Health Center has also concentrated on providing education to as many staff members as possible on service excellence. For the past two years the hospital has been able to host two nationally known speakers from the Baptist Leadership Institute. These offerings have helped the staff to understand how important it is for the organization to create and maintain a great culture in order to achieve service and operational excellence. The goal of the organization is shifting from an entitlement culture to an ownership culture. This is perfectly aligned with the vision of being the provider of choice, community educator of choice and employer of choice. The turnover rate is extremely low being at 1%. The national average for turnover is closer to 14-15%. The Health Center would anticipate this rate to increase over the next few years. There has been an implementation of peer interviewing for every position that the organization hires. This has become a standard practice for every department throughout the facility.
- Two years ago the organization started their Lean journey within the organization. The first huddle board was implemented in December 2009. Today there are huddle boards in every department. When each department huddles, there has been an improvement in communication and a feeling of less excuses, less blaming and less secrets. The journey also included many rapid improvement events such as 5S events in many different departments. There has been much emphasis on managing wastes and becoming more efficient. Lean or process excellence is also perfectly aligned with the organization's vision. The next steps will be including standard work and more practical problem solving.
- The Health Center continues to focus on improving patient safety by becoming more transparent with the results and sharing those with all staff, providers, and board members. There has been a significant decrease in both medication errors and patient falls. These successes can be contributed to improvement in technology such as pharmacy profile, bar-coding patient identification bands and more sophisticated alarm systems. Other contributing factors are education to all staff members and the empowerment for the staff to problem solve.

Condensed Financial Statements

Balance Sheets

	<u>June 30,</u> <u>2011</u>	<u>June 30,</u> <u>2010</u>	<u>June 30,</u> <u>2009</u>
Assets			
Current Assets			
Cash and cash equivalents	\$ 5,433,760	\$ 4,176,329	\$ 3,520,385
Investments	258,144	255,725	254,315
Receivables			
Patient and resident, net of estimated uncollectibles	1,623,056	1,967,630	1,994,111
Succeeding year property taxes	593,759	568,994	535,274
Other	43,251	52,361	91,403
Other assets	<u>696,843</u>	<u>686,425</u>	<u>538,900</u>
Total current assets	<u>8,648,813</u>	<u>7,707,464</u>	<u>6,934,388</u>
Assets Limited as to Use or Restricted	<u>2,768,864</u>	<u>2,288,815</u>	<u>1,923,068</u>
Capital Assets, Net	<u>8,414,534</u>	<u>8,658,971</u>	<u>9,220,570</u>
Other Assets			
Debt issue costs, net of accumulated amortization	<u>26,569</u>	<u>29,665</u>	<u>32,760</u>
Total assets	<u><u>\$ 19,858,780</u></u>	<u><u>\$ 18,684,915</u></u>	<u><u>\$ 18,110,786</u></u>

Condensed Financial Statements

Balance Sheets (continued)

	<u>June 30,</u> <u>2011</u>	<u>June 30,</u> <u>2010</u>	<u>June 30,</u> <u>2009</u>
Liabilities and Net Assets			
Current Liabilities			
Current maturities of long-term debt	\$ 422,056	\$ 508,820	\$ 402,046
Accounts payable			
Trade	288,199	185,486	285,551
Due to Affiliated Organization	621,370	395,561	439,505
Estimated third-party payor settlements	568,000	305,000	375,000
Accrued expenses	579,553	589,068	532,295
Deferred taxes	593,759	568,994	535,274
	<u>3,072,937</u>	<u>2,552,929</u>	<u>2,569,671</u>
Long-term Debt, less current maturities	<u>2,056,184</u>	<u>2,473,796</u>	<u>2,729,697</u>
Total liabilities	<u>5,129,121</u>	<u>5,026,725</u>	<u>5,299,368</u>
Net Assets			
Invested in capital assets, net of related debt	5,962,863	5,706,020	6,121,587
Restricted			
Expendable under master affiliation agreement	362,546	303,394	266,091
Expendable under debt agreements	486,844	608,979	275,000
Unrestricted	7,917,406	7,039,797	6,148,740
Total net assets	<u>14,729,659</u>	<u>13,658,190</u>	<u>12,811,418</u>
Total liabilities and net assets	<u>\$ 19,858,780</u>	<u>\$ 18,684,915</u>	<u>\$ 18,110,786</u>

Mitchell County Regional Health Center
Management's Discussion and Analysis
June 30, 2011 and 2010

Statements of Revenues, Expenses, and Changes in Net Assets

	Year Ended June 30,		
	2011	2010	2009
Operating Revenues			
Net patient and resident service revenue	\$ 16,927,030	\$ 16,338,873	\$ 16,178,136
Other operating revenues	357,294	356,899	326,108
Total Operating Revenues	<u>17,284,324</u>	<u>16,695,772</u>	<u>16,504,244</u>
Operating Expenses			
Salaries and wages	5,616,956	5,430,034	5,290,634
Employee benefits	1,560,917	1,452,794	1,362,658
Supplies and other expenses	8,231,893	8,380,526	8,480,632
Depreciation	1,114,882	1,121,754	1,073,647
Interest and amortization	134,688	139,992	172,391
Total Operating Expenses	<u>16,659,336</u>	<u>16,525,100</u>	<u>16,379,962</u>
Operating Income Before Affiliation Agreement	624,988	170,672	124,282
Affiliation Agreement Expense	<u>(287,326)</u>	<u>(59,152)</u>	<u>(37,303)</u>
Operating Income	<u>337,662</u>	<u>111,520</u>	<u>86,979</u>
Nonoperating Revenues (Expenses)			
County tax revenue	557,007	523,901	507,591
Investment income	77,340	82,229	92,601
Loss on sale of capital assets	<u>(2,677)</u>	<u>(9,596)</u>	<u>(17,278)</u>
Net Nonoperating Revenues	<u>631,670</u>	<u>596,534</u>	<u>582,914</u>
Revenues in Excess of Expenses	969,332	708,054	669,893
Capital grants and contributions	<u>102,137</u>	<u>138,718</u>	<u>154,096</u>
Increase in Net Assets	1,071,469	846,772	823,989
Net Assets Beginning of Year	<u>13,658,190</u>	<u>12,811,418</u>	<u>11,987,429</u>
Net Assets End of Year	<u>\$ 14,729,659</u>	<u>\$ 13,658,190</u>	<u>\$ 12,811,418</u>

Capital Assets

Mitchell County Regional Health Center is currently in the planning stages of remodeling the emergency room and operating room. Phase 1 of this project is scheduled to begin construction in January of 2012, with all phases of the construction to be completed by December of 2012. The Hospital's construction plans are part of the strategic plan's focus on reviewing the current facility needs.

Long-Term Debt

At fiscal year end, Mitchell County Regional Health Center had \$2,478,240 in short-term and long-term debt. The debt was incurred to update the facility and continue to invest in new equipment and technology.

Economic and Other Factors and Next Year's Budget

The Health Center's Board and management will consider many factors when preparing the fiscal year 2012 budget. Of primary consideration in the 2012 budget are the unknowns of health care reform and the continued difficulty in the status of the economy.

Items listed below were also considered:

- Medicare and Medicaid reimbursement rates
- Managed Care contracts
- Increase in self-pay accounts receivable due to uninsured and underinsured
- Staffing benchmarks
- Increased expectations for quality at a lower price
- Salary and benefit costs
- Patient safety initiatives
- Pay-for-performance and quality indicators
- Technology advances
- Medical Staff recruitment
- Lower return on investments

Summary

Over the past fiscal year the hospital has been very transparent and proud of their successes. The goal for supplies as percent of revenue is 10.5% and ended the year with 10.22%. The goal for salaries and benefits as a percent of net revenue is 45% or below and this past fiscal year the average was 44.10%. Managing more efficiently and holding leaders accountable contributed to reaching these goals. The number of days of cash on hand is to be above 180 days. The organization is at approximately 182 days of cash on hand even though close to \$1 million was spent on capital equipment for the organization. The account receivable days for the organization are the lowest in the Mercy Health North Iowa network averaging 42.9.

The Health Center Board of Trustees continues to be engaged and extremely proud of the excellent patient care that is delivered in Mitchell County.

Contacting the Health Center's Finance Department

The Health Center's financial statements are designed to present users with a general overview of the Health Center's finances and to demonstrate the Health Center's accountability. If you have questions about the report or need additional financial information, please contact the finance department at the following address:

Mitchell County Regional Health Center
Attn: Chief Financial Officer
616 North Eighth Street
Osage, IA 50461-1456

	<u>2011</u>	<u>2010</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 5,433,760	\$ 4,176,329
Cash - custodial - Auxiliary	43,835	39,040
Investments - Note 4	258,144	255,725
Receivables		
Patient, net of estimated uncollectibles of \$993,000 in 2011 and \$987,000 in 2010	1,623,056	1,967,630
Succeeding year property tax	593,759	568,994
Other	43,251	52,361
Supplies	385,722	384,388
Prepaid expenses	267,286	262,997
Total current assets	<u>8,648,813</u>	<u>7,707,464</u>
Assets Limited as to Use or Restricted - Note 4		
Internally designated for capital improvements	1,632,148	1,317,290
Restricted under debt agreements	486,844	608,979
Restricted by master affiliation agreement with MMC-NI	649,872	362,546
Total assets limited as to use or restricted	<u>2,768,864</u>	<u>2,288,815</u>
Capital Assets, Net - Note 5	<u>8,414,534</u>	<u>8,658,971</u>
Other Assets		
Debt issue costs, net of accumulated amortization of \$26,055 in 2011 and \$22,959 in 2010	<u>26,569</u>	<u>29,665</u>
Total assets	<u>\$ 19,858,780</u>	<u>\$ 18,684,915</u>

See Notes to Financial Statements

Mitchell County Regional Health Center

Balance Sheets

June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Liabilities and Net Assets		
Current Liabilities		
Current maturities of long-term debt - Note 6	\$ 422,056	\$ 508,820
Accounts payable		
Trade	288,199	185,486
Due to Affiliated Organization - Note 11	621,370	395,561
Estimated third-party payor settlements	568,000	305,000
Custodial funds - Auxiliary	43,835	39,040
Accrued expenses		
Salaries and wages	169,322	161,236
Paid leave	292,871	310,627
Interest	13,641	15,272
Payroll taxes and employee benefits	59,884	62,893
Deferred revenue for succeeding year property tax receivable	<u>593,759</u>	<u>568,994</u>
Total current liabilities	3,072,937	2,552,929
Long-Term Debt, Less Current Maturities - Note 6	<u>2,056,184</u>	<u>2,473,796</u>
Total liabilities	<u>5,129,121</u>	<u>5,026,725</u>
Net Assets		
Invested in capital assets, net of related debt	5,962,863	5,706,020
Restricted		
Expendable under master affiliation agreement with MMC-NI	362,546	303,394
Expendable under debt agreements	486,844	608,979
Unrestricted	<u>7,917,406</u>	<u>7,039,797</u>
Total net assets	<u>14,729,659</u>	<u>13,658,190</u>
Total liabilities and net assets	<u>\$ 19,858,780</u>	<u>\$ 18,684,915</u>

Mitchell County Regional Health Center
Statements of Revenues, Expenses, and Changes in Net Assets
Years Ended June 30, 2011 and 2010

	2011	2010
Operating Revenues		
Net patient service revenue (net of provision for bad debts of \$594,772 in 2011 and \$596,899 in 2010) - Notes 2 and 3	\$ 16,927,030	\$ 16,338,873
Other operating revenues	357,294	356,899
Total Operating Revenues	17,284,324	16,695,772
Operating Expenses		
Salaries and wages	5,616,956	5,430,034
Employee benefits	1,560,917	1,452,794
Supplies and other expenses	8,231,893	8,380,526
Depreciation	1,114,882	1,121,754
Interest and amortization	134,688	139,992
Total Operating Expenses	16,659,336	16,525,100
Operating Income Before Affiliation Agreement	624,988	170,672
Affiliation Agreement Expense	(287,326)	(59,152)
Operating Income	337,662	111,520
Nonoperating Revenues (Expenses)		
County tax revenue	557,007	523,901
Investment income	77,340	82,229
Loss on sale of capital assets	(2,677)	(9,596)
Net Nonoperating Revenues	631,670	596,534
Revenues in Excess of Expenses	969,332	708,054
Capital Grants and Contributions	102,137	138,718
Increase in Net Assets	1,071,469	846,772
Net Assets, Beginning of Year	13,658,190	12,811,418
Net Assets, End of Year	\$ 14,729,659	\$ 13,658,190

Mitchell County Regional Health Center
 Statements of Cash Flows
 Years Ended June 30, 2011 and 2010

	2011	2010
Cash Flows from Operating Activities		
Receipts of patient service revenue	\$ 17,534,604	\$ 16,295,354
Payments of salaries and wages	(5,629,635)	(5,410,612)
Payments of supplies and other expenses	(9,757,237)	(10,144,966)
Other receipts and payments, net	366,375	350,896
Net Cash Provided by Operating Activities	2,514,107	1,090,672
Cash Flows from Noncapital Financing Activities		
County tax revenue received	557,036	524,613
Cash Flows from Capital and Related Financing Activities		
Purchase of capital assets	(876,071)	(571,573)
Proceeds from sale of capital assets	2,949	1,821
Principal payments on long-term debt	(514,170)	(517,774)
Proceeds from issuance of long-term debt	-	358,853
Interest payments on long-term debt	(123,429)	(128,791)
Payments received on promises to give	-	44,333
Capital grants and contributions	102,137	138,718
Net Cash used for Capital and Related Financing Activities	(1,408,584)	(674,413)
Cash Flows from Investing Activities		
Investment income	77,340	82,229
Increase in investments	(2,419)	(1,410)
Proceeds from the sale of assets limited as to use or restricted	122,135	27,384
Purchase of assets limited as to use or restricted	(602,184)	(393,131)
Net Cash used for Investing Activities	(405,128)	(284,928)
Net Increase in Cash and Cash Equivalents	1,257,431	655,944
Cash and Cash Equivalents at Beginning of Year	4,176,329	3,520,385
Cash and Cash Equivalents at End of Year	\$ 5,433,760	\$ 4,176,329

Mitchell County Regional Health Center
 Statements of Cash Flows
 Years Ended June 30, 2011 and 2010

	2011	2010
Reconciliation of Operating Income to Net Cash Provided		
by Operating Activities		
Operating income	\$ 337,662	\$ 111,520
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation	1,114,882	1,121,754
Interest expense considered capital and related financing activity	121,798	127,102
Amortization	12,890	12,890
Provision for bad debts	594,772	596,899
Changes in assets and liabilities		
Patient receivables	(250,198)	(570,418)
Estimated third-party payor settlements	263,000	(70,000)
Other receivables	9,081	(6,003)
Supplies	(1,334)	(17,175)
Prepaid expenses	(4,289)	(91,310)
Accounts payable - trade and related	328,522	(144,009)
Accrued expenses	(12,679)	19,422
Net Cash Provided by Operating Activities	\$ 2,514,107	\$ 1,090,672

Note 1 - Organization and Summary of Significant Accounting Policies

Organization

Mitchell County Memorial Hospital, d/b/a Mitchell County Regional Health Center (Health Center), is a 25-bed acute care hospital located in Osage, Iowa. The Health Center provides health care services in accordance with a Master Affiliation Agreement discussed further in Note 11. Services are provided primarily to residents of Mitchell County and the surrounding area in northeastern Iowa, through hospital-based services in Osage, Iowa and physician clinic services in Osage, St. Ansgar, Stacyville, and Riceville, Iowa. The Health Center is organized under Chapter 347 of the Code of Iowa. The Health Center is exempt from income taxes as a political subdivision.

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

Tax-Exempt Status

The Health Center is an Iowa non-profit corporation and has been recognized by the Internal Revenue Service as exempt from federal income taxes under Internal Revenue Code Section 501(c)(3). The Health Center is subject to income tax on net income that is derived from business activities that are unrelated to its exempt purpose, as applicable.

The Health Center believes that it has appropriate support for any tax positions taken affecting its annual filing requirements, and as such, does not have any uncertain tax positions that are material to the financial statements. The Health Center would recognize future accrued interest and penalties related to unrecognized tax benefits and liabilities in income tax expense if such interest and penalties are incurred.

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 (GASB) 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. The Health Center has no component units which meet the Governmental Accounting Standards Board criteria.

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 the following categories/components:

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

Nonexpendable – Nonexpendable net assets are subject to externally imposed stipulations which require them to be maintained permanently by the Health Center.

Expendable – Expendable 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 preceding categories.

Unrestricted net assets often have constraints on resources imposed by management which can be removed or modified.

When both restricted and unrestricted net assets are available for use, generally it is the Health Center's policy to use restricted net assets 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's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America as prescribed 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.

The Health Center uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis, using the economic resources measurement focus. Based on GASB Codification Topic 1600, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, the Health Center has elected not to apply provisions of any pronouncements of the Financial Accounting Standards Board (FASB) issued after November 30, 1989.

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. Estimates also affect 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 or 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. 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 that the tax asking is certified by the County Board of Supervisors. Delinquent property tax receivable represents unpaid taxes for the current and prior years. The succeeding year property tax receivable represents taxes certified by the Board of Trustees 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 Trustees 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.

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.

Supplies

Supplies are valued at cost using the first-in, first-out method.

Assets Limited as to Use or Restricted

Assets limited as to use 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 for other purposes. Assets limited as to use that are available for obligations classified as current liabilities are reported in current assets.

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 operations 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 non-operating revenues (expenses) to the extent expended within the period.

Capital Assets

Capital asset acquisitions in excess of \$5,000 are capitalized and are recorded at cost. Capital assets 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. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation in the financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. The estimated useful lives of capital assets are as follows:

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

Debt Issue Costs

Debt issue costs are amortized over the period the related debt is outstanding using the straight-line method.

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 projected paid leave payouts is recorded as a current liability on the balance sheet based on pay rates that are in effect at June 30, 2011 and 2010.

Operating Revenues and Expenses

The Health Center’s statement of revenues, expenses, and changes in net assets distinguishes between operating and non-operating 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 investment income, taxes, grants, and contributions, are reported as non-operating revenues (expenses). 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 restricted to a specific operating purpose are reported as operating revenues. Amounts that are unrestricted are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses.

Investments

Investments are valued at purchase cost, or fair market value at the date of acquisition, if donated. Investments consist of non-negotiable certificates of deposit.

Investment Income

Interest on cash and deposits is included in non-operating revenues and expenses.

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.

Advertising Costs

Costs incurred for producing and distributing advertising are expensed as incurred.

County Tax Revenue

Taxes are included in non-operating 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.

Subsequent Events

The Health Center has evaluated subsequent events through October 13, 2011, the date which the financial statements were available to be issued.

Reclassifications

Certain items from the 2010 financial statements have been reclassified to conform to the current year presentation. The reclassifications had no impact on increase in net assets.

Note 2 - Charity Care and Community Benefits

The Health Center maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy. The amounts of charges foregone were \$45,509 and \$44,871 for the years ended June 30, 2011 and 2010, respectively. The estimated costs of the charges foregone, based upon an overall cost-to-charge ratio calculation, for the years ended June 30, 2011 and 2010, were \$29,000 and \$31,000, respectively.

In addition, the Health Center provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts which are less than established charges for the services provided to the recipients, and for some services the payments are less than the cost of rendering the services provided.

The Health Center also commits significant time and resources to endeavors and critical services which meet otherwise unfulfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable.

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:

Medicare: The Health Center is licensed as a Critical Access Hospital (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, 2009.

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, 2008.

Other Payors: The Health Center has also entered into payment agreements with certain commercial insurance carriers and other organizations. The basis for payment to the Health Center under these agreements may include prospectively determined rates and discounts from established charges.

Mitchell County Regional Health Center

Notes to Financial Statements

June 30, 2011 and 2010

Revenue from the Medicare and Medicaid programs accounted for approximately 47% and 4%, respectively, of the Health Center's net patient service revenue for each of the years ended June 30, 2011 and 2010. The net patient service revenue for the year ended June 30, 2011, increased approximately \$148,000 due to prior-year retroactive adjustments in excess of amounts previously estimated and removal of allowances previously estimated that are no longer necessary as a result of final settlements and years that are no longer subject to audits, reviews, and investigations. The net patient service revenue for the year ended June 30, 2010, decreased approximately \$25,000 due to prior-year retroactive adjustments in excess of amounts previously estimated and removal of allowances previously estimated that are no longer necessary as a result of final settlements and years that are no longer subject to audits, reviews, and investigations.

Laws and regulations governing the 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.

The Centers for Medicare and Medicaid Services (CMS) has implemented a Recovery Audit Contractor (RAC) program under which claims subsequent to October 1, 2007, are reviewed by contractors for validity, accuracy, and proper documentation. A demonstration project completed in several other states resulted in the identification of potential overpayments, some being significant. If selected for audit, the potential exists that the Health Center may incur a liability for a claims overpayment at a future date. The Health Center is unable to determine if it will be audited and, if so, the extent of the liability of overpayments, if any. As the outcome of such potential reviews is unknown and cannot be reasonably estimated, it is the Health Center's policy to adjust revenue for deductions from overpayment amounts or additions from underpayment amounts determined under the RAC audits at the time a change in reimbursement is agreed upon between the Health Center and CMS.

A summary of patient service revenue, contractual adjustments, and provision for bad debts for the years ended June 30, 2011 and 2010, is as follows:

	<u>2011</u>	<u>2010</u>
Total Patient Service Revenue	<u>\$ 25,514,811</u>	<u>\$ 23,566,812</u>
Contractual Adjustments		
Medicare	(4,749,912)	(3,834,818)
Medicaid	(376,333)	(320,237)
Other	<u>(2,866,764)</u>	<u>(2,475,985)</u>
Total contractual adjustments	<u>(7,993,009)</u>	<u>(6,631,040)</u>
Net Patient Service Revenue	17,521,802	16,935,772
Provision for Bad Debts	<u>(594,772)</u>	<u>(596,899)</u>
Net Patient Service Revenue (Net of Provision of Bad Debts)	<u><u>\$ 16,927,030</u></u>	<u><u>\$ 16,338,873</u></u>

Note 4 - Deposit and Investments

The Health Center's deposits in banks at June 30, 2011 and 2010, 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.

At June 30, 2011 and 2010, the Health Center's amounts of cash and deposits are as follows:

	2011	2010
Checking and Savings Accounts	\$ 2,588,864	\$ 2,078,815
Certificates of Deposit	438,144	465,725
Total deposits	\$ 3,027,008	\$ 2,544,540

Included in the following balance sheet captions:

Investments	\$ 258,144	\$ 255,725
Assets Limited as to Use or Restricted	2,768,864	2,288,815
	\$ 3,027,008	\$ 2,544,540

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) to 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.

Note 5 - Capital Assets

Summaries of capital assets for the years ended June 30, 2011 and 2010, are as follows:

	June 30, 2010				June 30, 2011
	Balance	Additions	Deductions	Transfers	Balance
Capital Assets Not Being Depreciated:					
Land	\$ 229,512	\$ -	\$ -	\$ -	\$ 229,512
Construction in progress	68,429	464,638	-	(417,521)	115,546
Total capital assets not being depreciated	<u>297,941</u>	<u>464,638</u>	<u>-</u>	<u>(417,521)</u>	<u>345,058</u>
Capital Assets Being Depreciated:					
Land improvements	505,847	-	-	-	505,847
Building	12,034,714	-	-	113,758	12,148,472
Leasehold improvements	55,257	-	-	-	55,257
Major movable equipment	5,386,245	411,433	450,694	303,763	5,650,747
Total capital assets being depreciated	<u>17,982,063</u>	<u>411,433</u>	<u>450,694</u>	<u>417,521</u>	<u>18,360,323</u>
Less Accumulated Depreciation for:					
Land improvements	373,922	23,625	-	-	397,547
Building	5,241,881	459,362	-	-	5,701,243
Leasehold improvements	54,621	424	-	-	55,045
Major movable equipment	3,950,609	631,472	445,069	-	4,137,012
Total accumulated depreciation	<u>9,621,033</u>	<u>1,114,883</u>	<u>445,069</u>	<u>-</u>	<u>10,290,847</u>
Total Capital Assets Being Depreciated, Net	<u>8,361,030</u>	<u>(703,450)</u>	<u>5,625</u>	<u>417,521</u>	<u>8,069,476</u>
Total Capital Assets, Net	<u>\$ 8,658,971</u>	<u>\$ (238,812)</u>	<u>\$ 5,625</u>	<u>\$ -</u>	<u>\$ 8,414,534</u>

Construction in progress at June 30, 2011, represents cost incurred for various projects at the Health Center. It primarily consists of preliminary planning costs for an Operating Room/Emergency Room remodeling project and a new phone system. Both of these projects will be funded with Health Center funds.

Mitchell County Regional Health Center
Notes to Financial Statements
June 30, 2011 and 2010

	June 30, 2009				June 30, 2010
	<u>Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Transfers</u>	<u>Balance</u>
Capital Assets Not Being Depreciated:					
Land	\$ 229,512	\$ -	\$ -	\$ -	\$ 229,512
Construction in progress	4,781	429,674	-	(366,026)	68,429
Total capital assets not being depreciated	<u>234,293</u>	<u>429,674</u>	<u>-</u>	<u>(366,026)</u>	<u>297,941</u>
Capital Assets Being Depreciated:					
Land improvements	488,847	17,000	-	-	505,847
Building	11,974,362	19,888	-	40,464	12,034,714
Leasehold improvements	55,257	-	-	-	55,257
Major movable equipment	5,285,734	105,011	330,062	325,562	5,386,245
Total capital assets being depreciated	<u>17,804,200</u>	<u>141,899</u>	<u>330,062</u>	<u>366,026</u>	<u>17,982,063</u>
Less Accumulated Depreciation For:					
Land improvements	337,142	36,780	-	-	373,922
Building	4,772,449	469,432	-	-	5,241,881
Leasehold improvements	54,197	424	-	-	54,621
Major movable equipment	3,654,135	615,117	318,643	-	3,950,609
Total accumulated depreciation	<u>8,817,923</u>	<u>1,121,753</u>	<u>318,643</u>	<u>-</u>	<u>9,621,033</u>
Total Capital Assets Being Depreciated, Net	<u>8,986,277</u>	<u>(979,854)</u>	<u>11,419</u>	<u>366,026</u>	<u>8,361,030</u>
Total Capital Assets, Net	<u>\$ 9,220,570</u>	<u>\$ (550,180)</u>	<u>\$ 11,419</u>	<u>\$ -</u>	<u>\$ 8,658,971</u>

Note 6 - Long-Term Debt

A schedule of changes in long-term debt for 2011 and 2010, is as follows:

	Balance June 30, 2010	Additions	(Payments) Amortization	Balance June 30, 2011	Amounts Due Within One Year
Hospital Refunding Revenue					
Note, Series 2002	\$ 2,338,646	\$ -	\$ (195,308)	\$ 2,143,338	\$ 217,639
USDA Loan	267,430	-	(101,643)	165,787	103,806
Promissory Notes	157,365	-	(23,790)	133,575	24,701
Notes Payable	10,000	-	(10,000)	-	-
Obligations Under Capital					
Leases - Note 7	273,430	-	(177,857)	95,573	75,910
	<u>3,046,871</u>	<u>-</u>	<u>(508,598)</u>	<u>2,538,273</u>	<u>422,056</u>
Deferred Loss on Bond					
Refinancing	(93,044)	-	9,794	(83,250)	-
Accumulated Amortization on Deferred Loss	<u>28,789</u>	<u>-</u>	<u>(5,572)</u>	<u>23,217</u>	<u>-</u>
Total Long-Term Debt	<u>\$ 2,982,616</u>	<u>\$ -</u>	<u>\$ (504,376)</u>	2,478,240	<u>\$ 422,056</u>
Less Current Maturities				<u>(422,056)</u>	
Long-Term Debt, Less Current Maturities				<u>\$ 2,056,184</u>	

	Balance June 30, 2009	Additions	(Payments) Amortization	Balance June 30, 2010	Amounts Due Within One Year
Hospital Refunding Revenue					
Note, Series 2002	\$ 2,541,184	\$ -	\$ (202,538)	\$ 2,338,646	\$ 195,308
USDA Loan	-	358,853	(91,423)	267,430	101,864
Promissory Notes	180,290	-	(22,925)	157,365	23,791
Notes Payable	37,364	-	(27,364)	10,000	10,000
Obligations Under Capital					
Leases	441,382	-	(167,952)	273,430	177,857
	<u>3,200,220</u>	<u>358,853</u>	<u>(512,202)</u>	<u>3,046,871</u>	<u>508,820</u>
Deferred Loss on Bond					
Refinancing	(102,838)	-	9,794	(93,044)	-
Accumulated Amortization on Deferred Loss	<u>34,361</u>	<u>-</u>	<u>(5,572)</u>	<u>28,789</u>	<u>-</u>
Total Long-Term Debt	<u>\$ 3,131,743</u>	<u>\$ 358,853</u>	<u>\$ (507,980)</u>	2,982,616	<u>\$ 508,820</u>
Less Current Maturities				<u>(508,820)</u>	
Long-Term Debt, Less Current Maturities				<u>\$ 2,473,796</u>	

The Health Center is subject to certain covenants under the bond agreement including a requirement to maintain certain measures of financial performance and maintain a sinking fund account. The Health Center was in compliance with these covenants for the years ended June 30, 2011 and 2010.

Mitchell County Regional Health Center

Notes to Financial Statements

June 30, 2011 and 2010

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

Year Ending June 30,	Long-term debt		
	Principal	Interest	Total
2012	\$ 422,056	\$ 77,648	\$ 499,704
2013	334,398	59,750	394,148
2014	260,583	50,882	311,465
2015	268,669	42,677	311,346
2016	277,020	34,206	311,226
2017-2020	975,547	55,175	1,030,722
	<u>\$ 2,538,273</u>	<u>\$ 320,338</u>	<u>\$ 2,858,611</u>

Hospital Refunding Revenue Note, Series 2002:

The Health Center entered into a note payable with First Citizens National Bank, Mason City, Iowa, on February 1, 2003, in the amount of \$3,520,000. The purpose of the note payable was to refund the 1997 Hospital Revenue Bonds in order to reduce the overall effective interest rates on the outstanding bond obligation. Payments of principal and interest are payable monthly through February 2020, with variable interest to be adjusted on August 1, 2011 based on 130% of the 7 year U.S. Treasury Note. The effective interest rate on the note through August 1, 2011 is 4.750%. Effective August 1, 2011, the new interest rate will be 2.964%. The note is collateralized by patient service revenue of the Health Center.

USDA Loan:

The Health Center entered into a Distance Learning and Telemedicine Combination Loan and Grant with the United States Department of Agriculture (Rural Utilities Service) on February 13, 2008, for a maximum amount of \$659,000 (\$527,200 in loan proceeds and \$131,800 in grant funds). The Health Center has drawn \$358,853 from the Distance Learning and Telemedicine (DLT) loan funds and \$89,713 from the DLT grant. Payments of principal and interest at 1.89% are payable monthly through February of 2013. The Health Center is to maintain cash deposits equal to the outstanding principal balance as collateral.

Promissory Notes:

The Health Center entered into two promissory notes with Heartland Power Cooperative, Thompson, Iowa, on September 1, 2005, in the amounts of \$240,000 and \$60,000. These notes have been discounted using an imputed interest rate of 5%. The discount of \$51,077 is reported with long-term debt and will be amortized over the life of the related debt using the straight-line method. The purpose of the promissory notes was to build the new St. Ansgar Clinic in St. Ansgar, Iowa. The notes are due in annual installments of \$24,000 at zero percent interest and \$6,000 including interest at 2% through September 2015, respectively.

Notes Payable:

The Health Center entered into two notes for certain equipment. The first note, entered into during fiscal year 2005, was for telemetry equipment and was for a term of five years and bore interest at a rate of 3.95%, with payments of principal and interest of \$1,569 due monthly. The note was collateralized by the patient service revenue of the Health Center. The second note, entered into during the 2006 fiscal year, was due to MMC-NI (Note 11) and was for a cataract microscope with a term of five years and zero percent interest with payments of principal of \$1,250 due monthly.

Obligations Under Capital Leases:

The Health Center entered into four capital leases for equipment. The first lease, entered into during fiscal year 2007, is for a period of five years and bears interest at a rate of 6.0%, with payments of principal and interest of \$10,362 due monthly. The second lease, entered into during fiscal year 2007, is for a period of five years and bears interest at a rate of 6.0%, with payments of principal and interest of \$1,884 due monthly. The third lease, entered into during fiscal year 2008, is for a period of five years and bears interest at a rate of 3.59%, with payments of principal and interest of \$1,457 due monthly. The fourth lease, entered into during fiscal year 2008, is for a period of five years and bears interest at a rate of 5.75%, with payments of principal and interest of \$2,019 due monthly.

Note 7 - Leases

The Health Center leases certain equipment under noncancelable long-term lease agreements. Certain leases have been recorded as capitalized leases and others as operating leases. Total lease expense for the years ended June 30, 2011 and 2010, for all operating leases was \$96,217 and \$129,049 respectively. The capitalized leased assets consist of:

	2011	2010
Major Movable Equipment	\$ 818,383	\$ 818,383
Less accumulated amortization (included as depreciation on the accompanying financial statements)	(786,710)	(634,016)
	\$ 31,673	\$ 184,367

Minimum future lease payments for noncancelable capital and operating leases are as follows:

Year Ending June 30,	Capital Leases	Operating Leases
2012	\$ 78,444	\$ 75,682
2013	20,185	55,946
2014	-	39,075
2015	-	32,747
Total minimum lease payments	98,629	\$ 203,450
Less interest	(3,056)	
Present value of minimum lease payments - Note 6	\$ 95,573	

Note 8 - Lease Commitment

During 2009, the Health Center entered into a lease agreement with the City of St. Ansgar for the St. Ansgar Community Center. The Health Center agreed to lease the building to the City of St. Ansgar for \$1 per year for twenty years, with an additional ten-year renewal option.

Note 9 - Foundation

The Mitchell County Memorial Foundation (Foundation) was formed to solicit funds to further the quality and availability of health care services in the Mitchell County area. The Foundation is authorized by the Health Center to solicit contributions on its behalf. In the absence of donor restrictions, the Foundation has discretionary control over the amounts to be distributed to the providers of health care services, the timing of such distributions, and the purposes for which the funds are to be used.

Since Mitchell County Regional Health Center has an economic interest in the Foundation, a summary of the Foundation's assets, liabilities, and net assets as of June 30, 2011 and 2010, and its results of operations, and changes in net assets for the years then ended follows:

	<u>(Unaudited)</u> 2011	<u>(Unaudited)</u> 2010
Assets	<u>\$ 128,982</u>	<u>\$ 116,671</u>
Net Assets	<u>\$ 128,982</u>	<u>\$ 116,671</u>
Revenues	\$ 28,674	\$ 58,806
Expenses	<u>16,363</u>	<u>72,311</u>
Revenues in excess of (less than) expenses	12,311	(13,505)
Net Assets, Beginning of Year	<u>116,671</u>	<u>130,176</u>
Net Assets, End of Year	<u>\$ 128,982</u>	<u>\$ 116,671</u>

For the years ended June 30, 2011 and 2010, the Foundation contributed approximately \$13,500 and \$69,000, respectively, to the Health Center for various projects.

Note 10 - Pension and Retirement Benefit

The Health Center contributes to the Iowa Public Employees Retirement System (IPERS), which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members are required to contribute 4.50% of their annual covered salary, and the Health Center is required to contribute 6.95% of annual covered payroll for the year ended June 30, 2011. Plan members were required to contribute 4.30% and 4.10% of their annual covered salary, and the Health Center was required to contribute 6.65% and 6.35% of annual covered payroll for the years ended June 30, 2010 and 2009, respectively. Contribution requirements are established by state statute. The Health Center's contributions to IPERS for the years ended June 30, 2011, 2010, and 2009, were \$385,693, \$356,945, and \$331,986, respectively, equal to the required contributions for each year.

Note 11 - Related Party Transactions

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 Mitchell County and surrounding counties in northeastern 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 as well as staff employees in support of the physician medical services. Amounts paid to MMC-NI for the provision of these services amounted to \$2,163,831 and \$2,338,323 for the years ended June 30, 2011 and 2010, respectively.

Under the Master Affiliation Agreement, operating gains that are less than \$125,000 are allocated entirely to the Health Center "to be invested by the Hospital as it sees fit." Operating gains in excess of \$125,000 and all operating losses are shared equally between the Health Center and MMC-NI. Per the agreement, MMC-NI's share of any gains "shall be reinvested in physician, clinical, and management services in Mitchell County." Total operating gains (losses) to be allocated to MMC-NI amounted to \$287,326 and \$59,152 for the year ended June 30, 2011 and 2010, respectively.

Management Services Agreement

The Health Center has a contractual agreement 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, 2011 and 2010, were \$711,822 and \$730,115, respectively.

Due to and from Affiliated Organization

The Health Center purchases various other patient care related services from MMC-NI in addition to those mentioned above. As of June 30, 2011 and 2010, the Health Center's records reflect an amount due to MMC-NI of \$621,370 and \$395,561, respectively, for the various services and distributions related to these agreements.

Note 12 - 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.

Litigations, Claims, and Other Disputes

The Health Center is subject to the usual contingencies in the normal course of operations and relating to the performance of its tasks under its various programs. In the opinion of management, the ultimate settlement of litigations, claims, and disputes in process will not be material to the financial position of the Health Center.

Health Care Legislation and Regulation

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, 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 health care providers. Violation of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Note 13 - 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.

Note 14 - 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, 2011 and 2010, was as follows:

	<u>2011</u>	<u>2010</u>
Medicare	36%	37%
Medicaid	3%	2%
Blue Cross	25%	23%
Other Third-Party Payors and Patients	<u>36%</u>	<u>38%</u>
	<u><u>100%</u></u>	<u><u>100%</u></u>



Required Supplementary Information
June 30, 2011

Mitchell County Regional Health Center

Mitchell County Regional Health Center
 Budgetary Comparison Schedule of Revenues, Expenses, and Changes in Net Assets –
 Budget and Actual (Cash Basis)
 Year Ended June 30, 2011

	Actual Accrual Basis	Accrual Adjustments	Actual Cash Basis	Budget	Variance Favorable (Unfavorable)
Estimated Amount to be Raised by Taxation	\$ 557,007	\$ 29	\$ 557,036	\$ 568,994	\$ (11,958)
Estimated Other Revenues/Receipts	<u>17,461,124</u>	<u>622,281</u>	<u>18,083,405</u>	<u>17,736,112</u>	<u>347,293</u>
	18,018,131	622,310	18,640,441	18,305,106	335,335
Expenses/Disbursements	<u>16,946,662</u>	<u>(46,120)</u>	<u>16,900,542</u>	<u>18,177,592</u>	<u>1,277,050</u>
Net	1,071,469	668,430	1,739,899	127,514	<u>\$ 1,612,385</u>
Balance, Beginning of Year	<u>13,658,190</u>	<u>(6,937,321)</u>	<u>6,720,869</u>	<u>7,738,751</u>	
Balance, End of Year	<u>\$ 14,729,659</u>	<u>\$ (6,268,891)</u>	<u>\$ 8,460,768</u>	<u>\$ 7,866,265</u>	

This budgetary comparison is presented as Required Supplementary Information in accordance with Governmental Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective 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 Health Center did not amend its original budget during the year ended June 30, 2011.

For the year ended June 30, 2011, the Health Center's expenditures did not exceed the amount budgeted.



Supplementary Information
June 30, 2011 and 2010

Mitchell County Regional Health Center



Independent Auditor's Report on Supplementary Information

The Board of Trustees
Mitchell County Regional Health Center
Osage, Iowa

Our audits were performed for the purpose of forming an opinion on the basic financial statements as a whole. The schedules of net patient service revenue, other operating revenues, operating expenses, patient receivables, allowance for doubtful accounts, collection statistics, supplies and prepaid expenses, and statistical information, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedules of net patient service revenue, other operating revenues, operating expenses, and supplies and prepaid expenses are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole. The schedules of patient receivables, allowance for doubtful accounts, collection statistics, and statistical information have not been subjected to the auditing procedures applied in the audits of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

Eide Bailly LLP

Dubuque, Iowa
October 13, 2011

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	Total	
	2011	2010
Patient Care Services		
Medical and surgical	\$ 1,329,104	\$ 1,390,903
Swing-bed	319,046	325,454
Subtotal	<u>1,648,150</u>	<u>1,716,357</u>
Other Professional Services		
Operating and recovery room	1,283,692	1,235,889
Labor and delivery room	-	90
Anesthesiology	856,407	795,528
Radiology	4,706,837	4,116,990
Laboratory	2,682,290	2,478,150
Blood supplies	109,685	104,591
Respiratory therapy	17,233	15,867
Physical therapy	634,662	567,638
Speech therapy	102,004	78,890
Electrocardiography	658,409	610,001
Medical and surgical supplies	449,963	450,352
Pharmacy	1,857,783	2,046,906
Cardiac rehabilitation	138,860	148,210
Sleep lab	199,240	221,892
Emergency room	2,155,541	1,806,590
Ambulance	664,626	594,823
Osage clinic	4,862,489	4,226,505
St. Ansgar clinic	2,038,681	1,957,211
Stacyville clinic	146,649	131,906
Riceville clinic	347,119	307,297
Subtotal	<u>23,912,170</u>	<u>21,895,326</u>
Total	25,560,320	23,611,683
Charity care	<u>(45,509)</u>	<u>(44,871)</u>
Total patient service revenue	<u>\$ 25,514,811</u>	<u>\$ 23,566,812</u>

Mitchell County Regional Health Center
Schedules of Net Patient Service Revenue
Years Ended June 30, 2011 and 2010

Inpatient		Outpatient	
2011	2010	2011	2010
\$ 1,204,940	\$ 1,266,003	\$ 124,164	\$ 124,900
319,046	325,454	-	-
<u>1,523,986</u>	<u>1,591,457</u>	<u>124,164</u>	<u>124,900</u>
59,954	135,758	1,223,738	1,100,131
-	-	-	90
30,209	69,515	826,198	726,013
330,353	272,763	4,376,484	3,844,227
284,868	325,630	2,397,422	2,152,520
34,202	44,662	75,483	59,929
4,386	1,153	12,847	14,714
161,664	137,985	472,998	429,653
48,695	30,099	53,309	48,791
68,869	57,340	589,540	552,661
55,280	74,513	394,683	375,839
623,829	693,145	1,233,954	1,353,761
-	-	138,860	148,210
-	-	199,240	221,892
220,800	198,883	1,934,741	1,607,707
81,987	76,021	582,639	518,802
471,893	445,952	4,390,596	3,780,553
504,675	488,517	1,534,006	1,468,694
44,289	39,860	102,360	92,046
83,007	83,188	264,112	224,109
<u>3,108,960</u>	<u>3,174,984</u>	<u>20,803,210</u>	<u>18,720,342</u>
<u>\$ 4,632,946</u>	<u>\$ 4,766,441</u>	<u>\$ 20,927,374</u>	<u>\$ 18,845,242</u>

Mitchell County Regional Health Center
Schedules of Net Patient Service Revenue
Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Total Patient Service Revenue	<u>\$ 25,514,811</u>	<u>\$ 23,566,812</u>
Contractual Adjustments		
Medicare	(4,749,912)	(3,834,818)
Medicaid	(376,333)	(320,237)
Other	<u>(2,866,764)</u>	<u>(2,475,985)</u>
Total contractual adjustments	<u>(7,993,009)</u>	<u>(6,631,040)</u>
Net Patient Service Revenue	17,521,802	16,935,772
Provision for Bad Debts	<u>(594,772)</u>	<u>(596,899)</u>
Net Patient Service Revenue (Net of Provision of Bad Debts)	<u><u>\$ 16,927,030</u></u>	<u><u>\$ 16,338,873</u></u>

Mitchell County Regional Health Center
Schedules of Other Operating Revenues
Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Other Operating Revenues		
Rental income	\$ 128,582	\$ 125,268
Meals sold	82,518	77,414
Grant revenues	64,760	66,886
Pharmacy rebates	27,635	24,234
Laboratory revenues	14,661	19,026
Vending machines	12,368	12,261
Medical records transcription fees	1,631	1,742
Other	<u>25,139</u>	<u>30,068</u>
Total Other Operating Revenues	<u>\$ 357,294</u>	<u>\$ 356,899</u>

Mitchell County Regional Health Center
Schedules of Operating Expenses
Years Ended June 30, 2011 and 2010

	2011	2010
Nursing Administration		
Salaries and wages	\$ 84,414	\$ 122,021
Supplies and other expenses	15,147	10,041
	<u>99,561</u>	<u>132,062</u>
Adults and Pediatrics		
Salaries and wages	962,967	962,240
Supplies and other expenses	77,228	86,296
	<u>1,040,195</u>	<u>1,048,536</u>
Operating and Recovery Rooms		
Salaries and wages	158,231	202,202
Supplies and other expenses	201,959	238,647
	<u>360,190</u>	<u>440,849</u>
Anesthesiology		
Salaries and wages	208,310	220,606
Supplies and other expenses	83,739	61,820
	<u>292,049</u>	<u>282,426</u>
Radiology		
Salaries and wages	338,169	72,005
Supplies and other expenses	411,608	757,570
	<u>749,777</u>	<u>829,575</u>
Laboratory		
Salaries and wages	346,173	354,043
Supplies and other expenses	314,607	322,940
	<u>660,780</u>	<u>676,983</u>
Blood Supplies		
Salaries and wages	3,952	4,008
Supplies and other expenses	65,642	66,019
	<u>69,594</u>	<u>70,027</u>
Respiratory Therapy		
Salaries and wages	1,042	1,245
Supplies and other expenses	193	198
	<u>1,235</u>	<u>1,443</u>
Physical Therapy		
Salaries and wages	205,745	196,284
Supplies and other expenses	11,502	12,489
	<u>217,247</u>	<u>208,773</u>
Speech Therapy		
Supplies and other expenses	34,355	25,551

Mitchell County Regional Health Center
Schedules of Operating Expenses
Years Ended June 30, 2011 and 2010

	2011	2010
Cardiac Rehabilitation		
Salaries and wages	\$ 54,857	\$ 59,455
Supplies and other expenses	1,304	6,938
	<u>56,161</u>	<u>66,393</u>
Electrocardiography		
Supplies and other expenses	104,983	104,287
	<u>104,983</u>	<u>104,287</u>
Medical and Surgical Supplies		
Salaries and wages	18,726	18,852
Supplies and other expenses	141,484	179,773
	<u>160,210</u>	<u>198,625</u>
Pharmacy		
Salaries and wages	122,641	113,538
Supplies and other expenses	448,930	550,595
	<u>571,571</u>	<u>664,133</u>
Emergency Room		
Salaries and wages	322,231	348,900
Supplies and other expenses	304,437	292,280
	<u>626,668</u>	<u>641,180</u>
Ambulance		
Salaries and wages	144,575	146,552
Supplies and other expenses	33,643	38,826
	<u>178,218</u>	<u>185,378</u>
Sleep Lab		
Salaries and wages	7,177	7,460
Supplies and other expenses	36,941	37,593
	<u>44,118</u>	<u>45,053</u>
Osage Clinic		
Salaries and wages	587,143	585,493
Supplies and other expenses	2,433,688	2,164,402
	<u>3,020,831</u>	<u>2,749,895</u>
St. Ansgar Clinic		
Salaries and wages	224,298	257,235
Supplies and other expenses	1,142,045	1,093,968
	<u>1,366,343</u>	<u>1,351,203</u>
Stacyville Clinic		
Salaries and wages	16,222	20,179
Supplies and other expenses	101,178	93,053
	<u>117,400</u>	<u>113,232</u>

Mitchell County Regional Health Center
Schedules of Operating Expenses
Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Riceville Clinic		
Salaries and wages	\$ 55,079	\$ 60,035
Supplies and other expenses	153,101	144,827
	<u>208,180</u>	<u>204,862</u>
Health Information Management		
Salaries and wages	293,215	296,886
Supplies and other expenses	28,538	19,660
	<u>321,753</u>	<u>316,546</u>
Food and Nutrition		
Salaries and wages	172,102	172,695
Supplies and other expenses	93,224	95,209
	<u>265,326</u>	<u>267,904</u>
Operation of Plant		
Salaries and wages	199,836	186,876
Supplies and other expenses	384,064	386,814
	<u>583,900</u>	<u>573,690</u>
Environmental Services		
Salaries and wages	132,046	138,196
Supplies and other expenses	34,276	42,911
	<u>166,322</u>	<u>181,107</u>
Laundry		
Salaries and wages	16,029	18,651
Supplies and other expenses	39,703	41,647
	<u>55,732</u>	<u>60,298</u>
Administrative Services		
Salaries and wages	941,776	864,377
Supplies and other expenses	1,534,374	1,506,172
	<u>2,476,150</u>	<u>2,370,549</u>
Unassigned Expenses		
Depreciation	1,114,882	1,121,754
Interest and amortization	134,688	139,992
Employee benefits	1,560,917	1,452,794
	<u>2,810,487</u>	<u>2,714,540</u>
Total Operating Expenses	<u>\$ 16,659,336</u>	<u>\$ 16,525,100</u>

Mitchell County Regional Health Center
Schedules of Patient Receivables and Allowance for Doubtful Accounts and Collecton Statistics (Unaudited)
June 30, 2011 and 2010

Age of Accounts	<u>2011</u>		<u>2010</u>	
	Amount	Percent to Total	Amount	Percent to Total
30 Days or Less	\$ 1,676,917	64.10%	\$ 1,791,107	60.63%
31 to 90 Days	569,734	21.78%	621,465	21.03%
91 to 150 Days	161,883	6.19%	171,727	5.81%
150 Days and over	<u>207,522</u>	<u>7.93%</u>	<u>370,191</u>	<u>12.53%</u>
	2,616,056	<u>100.00%</u>	2,954,490	<u>100.00%</u>
Less: Allowance for doubtful accounts	(299,000)		(347,009)	
Allowance for contractual adjustments	<u>(694,000)</u>		<u>(639,851)</u>	
Net	<u>\$ 1,623,056</u>		<u>\$ 1,967,630</u>	

**Analysis of Allowance for Doubtful Accounts
Years Ending June 30, 2011 and 2010**

	<u>2011</u>	<u>2010</u>
Beginning Balance	\$ 347,009	\$ 316,418
Add: Provision for bad debts	594,772	596,899
Recoveries previously written off	<u>273,136</u>	<u>230,748</u>
	867,908	827,647
Less: Accounts written off	<u>(915,917)</u>	<u>(797,056)</u>
Ending Balance	<u>\$ 299,000</u>	<u>\$ 347,009</u>

Collection Statistics

	<u>2011</u>	<u>2010</u>
Net Accounts Receivable - Patients	\$ 1,623,056	\$ 1,967,630
Number of Days Charges Outstanding (1)	37	43
Uncollectible Accounts (2)	\$ 696,491	\$ 702,256
Percentage of Uncollectible Accounts to Total Charges	2.7%	3.0%

(1) Based on average daily net patient service revenue for April, May, and June.

(2) Includes provision of bad debts, charity care, and collection fees.

Mitchell County Regional Health Center
Schedules of Supplies and Prepaid Expenses
June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Supplies		
Central supply	\$ 297,748	\$ 306,900
Pharmacy	<u>87,974</u>	<u>77,488</u>
Total supplies	<u>\$ 385,722</u>	<u>\$ 384,388</u>
Prepaid Expenses		
Insurance	\$ 76,170	\$ 72,171
Dues and other	<u>191,116</u>	<u>190,826</u>
Total prepaid expenses	<u>\$ 267,286</u>	<u>\$ 262,997</u>

Mitchell County Regional Health Center
Schedules of Statistical Information (Unaudited)
Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Patient Days		
Acute	1,271	1,399
Swing-bed	<u>823</u>	<u>768</u>
Totals	<u><u>2,094</u></u>	<u><u>2,167</u></u>
Admissions		
Acute	406	410
Swing-bed	<u>88</u>	<u>75</u>
Totals	<u><u>494</u></u>	<u><u>485</u></u>
Discharges		
Acute	405	410
Swing-bed	<u>90</u>	<u>74</u>
Totals	<u><u>495</u></u>	<u><u>484</u></u>
Average Length of Stay		
Acute	<u>3.1</u>	<u>3.4</u>
Swing-bed	<u><u>9.1</u></u>	<u><u>10.4</u></u>
Licensed Beds	<u><u>25</u></u>	<u><u>25</u></u>
Emergency Room and Outpatient Visits	<u><u>19,861</u></u>	<u><u>17,943</u></u>
Clinic Visits		
Osage (excluding optometry)	21,180	19,663
Optometry	3,803	3,652
St. Ansgar	9,145	9,259
Stacyville	628	600
Riceville	1,887	1,694



**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
Mitchell County Regional Health Center
Osage, Iowa

We have audited the accompanying balance sheets of Mitchell County Regional Health Center (Health Center) as of and for the year ended June 30, 2011, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the year then ended and have issued our report thereon dated October 13, 2011. 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 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.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Health Center's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings and Responses that we consider to be significant deficiencies in internal control over financial reporting. We consider the deficiencies in internal control described in Part I of the accompanying Schedule of Findings and Responses to be significant deficiencies in internal control over financial reporting. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements of Mitchell County Regional 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, 2011, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of Mitchell County Regional 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.

The 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 the Health Center's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees, and constituents of Mitchell County Regional Health Center and other parties to whom the Health Center may report. This report is not intended to be and should not be used by anyone other than these specified parties.

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

Dubuque, Iowa
October 13, 2011

Part I: Findings Related to the Financial Statements:

Significant Deficiencies:

I-A-11 Segregation of Duties

Criteria – One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible.

Condition – Certain employees perform duties that are incompatible.

Cause – A 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.

Effect – Limited segregation of duties could result in misstatements that may not be prevented or detected on a timely basis in the normal course of operations.

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 Mitchell County Regional 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 to obtain the maximum internal control possible under the circumstances.

Conclusion – Response accepted.

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

I-B-11 Preparation of Financial Statements

Criteria – A properly designed system of internal control over financial reporting includes the preparation of an entity's financial statements and accompanying notes to the financial statements by internal personnel of the entity. Management is responsible for establishing and maintaining internal control over financial reporting and procedures related to the fair presentation of the financial statements in accordance with U.S. generally accepted accounting principles (GAAP).

Condition – Mitchell County Regional 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 GAAP. 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.

Cause – We realize that obtaining the expertise necessary to prepare the financial statements, including all necessary disclosures, in accordance with GAAP can be considered costly and ineffective.

Effect – The effect of this condition is that the year-end financial reporting is prepared by a party outside of the Health Center. The outside party does not have the constant contact with ongoing financial transactions that internal staff have. Furthermore, it is possible that new standards may not be adopted and applied timely to the interim financial reporting. It is the responsibility of Health Center 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.

Recommendation – We recommend that management continue reviewing operating procedures in order to obtain the maximum internal control over financial reporting possible under the circumstances to enable staff to draft the financial statements internally.

Response – This finding and recommendation is not a result of any change in the Health Center's procedures, rather it is due to an auditing standard implemented by the American Institute of Certified Public Accountants. 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-11 Certified Budget** – Disbursements during the year ended June 30, 2011, did not exceed the amount budgeted.
- II-B-11 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-11 Travel Expense** – No expenditures of Health Center money for travel expenses of spouses of Health Center officials and/or employees were noted.
- II-D-11 Business Transactions** – We noted no material business transactions between the Health Center and Health Center officials and/or employees.
- II-E-11 Board Minutes** – No transactions were found that we believe should have been approved in the Board minutes but were not.
- II-F-11 Deposits and Investments** – No instances of non-compliance with the deposit and investment provisions of Chapters 12B and 12C of the Code of Iowa and the Health Center’s investment policy were noted.
- II-G-11 Publication of Bills Allowed and Salaries** – Chapter 347.13(11) of the Code of Iowa states “There shall be published quarterly in each of the official newspapers of the county as selected by the board of supervisors pursuant to section 349.1 the schedule of bills allowed and there shall be published annually in such newspapers the schedule of salaries paid by job classification and category...” The Health Center published a schedule of bills allowed and a schedule of salaries paid as required by the Code of Iowa.



The Board of Trustees
Mitchell County Regional Health Center
Osage, Iowa

We have audited the financial statements of Mitchell County Regional Health Center, for the year ended June 30, 2011. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated June 27, 2011. Professional standards also require that we communicate to you the following information related to our audit.

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 Mitchell County 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, 2011. We noted no transactions entered into by the Health Center during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

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 depreciation expense.

Collectibility of Patient Receivables – Management's estimate of the collectibility of patient receivables is based on historical trends for uncollectible accounts and contractual adjustments.

Estimated Third-party Payor Settlements – Management's estimate of the amounts either owed to or receivable from third-party payors is based on both final and tentatively settled cost reports. 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 that 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.

Depreciation Expense – Management’s estimate of depreciation expense is based on the estimated useful lives assigned using industry recommended averages and historical experience. Depreciation is calculated using the straight-line method.

We evaluated the key factors and assumptions used to develop these estimates related to the collectibility of patient receivables, amounts either owed to or receivable from third-party payors, and depreciation expense in determining that they are reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures 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. The following significant adjustments detected as a result of audit procedures were corrected by management:

	<u>Increase (Decrease) to Net Assets</u>
To Adjust Estimated Third-Party Payor Settlements	\$ 65,847
To Recognize a Capital Contribution under the Affiliation Agreement	59,152
To Adjust Contractual Allowances and Allowance for Bad Debts	(67,373)
Other Adjustments	(7,718)

The net effect of the adjustments was to increase net assets by \$49,908.

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 October 13, 2011.

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 Information in Documents Containing Audited Financial Statements

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Other Matters

Following are additional comments for informational purposes only:

Transmission of Electronic Health Information and the Implementation of ICD-10

The International Classification of Diseases (ICD) has gone through its tenth revision (ICD-10). The replacement of ICD-9 is mandated effective October 1, 2013. Where ICD-9 contains more than 17,000 codes, ICD-10 contains more than 141,000 codes and accommodates a significant number of new diagnoses and procedures. The use of ICD-10-Clinical Modifications (CM) and ICD-10-Procedure Coding System (PCS) applies to all “Covered Entities,” which includes, in part, hospitals, physicians, nursing homes, home health agencies, health plans, and health care clearinghouses that transmit electronic health information in connection with the HIPAA (Health Insurance Portability and Accountability Act) transaction standards.

The adoption of ICD-10-CM and ICD-10-PCS will enable providers and others to better study the relationship of cost to specific medical conditions. Greater specificity in clinical coding provides an important reference point for improving understanding of medical treatment and should enable system designers to create new and better health information systems.

In relation to the adoption of ICD-10, further regulation was also issued which calls for an updated version of the current HIPAA electronic transaction standard (Version 5010). The newer version replaces the existing HIPAA transaction standards on January 1, 2012. The newer version (5010) of the electronic standards is necessary in order to distinguish the reporting of the new ICD-10 codes.

The failure to successfully implement ICD-10 could create coding and billing backlogs, cause cash flow delays, increase claims rejections/denials, lead to unintended shifts in payment and place payer contracts and/or market share arrangements at risk due to poor quality rating or high costs.

We encourage facilities to plan for the implementation of ICD-10 by:

- Conducting an information systems inventory
- Assessing vendor readiness and support
- Creating staff awareness
- Assessing and planning for staff training needs
- Evaluating health plan contract implications
- Budget planning (system transitions, education, decreased productivity, potential denials)
- Identifying gaps in health record documentation

Eide Bailly has staff available that can assist your facility in assessment of the above noted areas, such as information technology, coding, education and financial planning for ICD-10. We have a certified ICD10-CM trainer on our Health Care Consulting team who is available to provide education to pertinent personnel in the facility.

Accounting for Leases

On August 17, 2010, the Financial Accounting Standards Board (FASB) issued proposed accounting standards update 1850-100, *Leases*. This proposal has been discussed over the last several years and seeks to change the way in which substantially all leases are reflected in the financial statements. Under the guidance in the proposed standard, the lessee would recognize an asset representing its right to use the leased ('underlying') asset for the lease term (the 'right-of-use' asset) and a liability to make lease payments. Substantially all leases currently considered operating leases would now be recognized on the balance sheet. Assets and liabilities recognized by lessees and lessors would be measured on a basis that:

- a) Assumes the longest possible lease term that is more likely than not to occur, taking into account the effect of any options to extend or terminate the lease.
- b) Uses an expected outcome technique to reflect the lease payments, including contingent rentals and expected payments under term option penalties and residual value guarantees, specified by the lease.
- c) Is updated when changes in facts or circumstances indicate that there would be a significant change in those assets or liabilities since the previous reporting period.

We recommend that you review the proposed guidance and consider responding to the questions included in the proposed standard if these changes are of concern.

The Board of Trustees
Mitchell County Regional Health Center
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This information is intended solely for the use of the Board of Trustees and management of Mitchell County Regional Health Center, and is not intended to be and should not be used by anyone other than these specified parties.

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

Dubuque, Iowa
October 13, 2011

xc: Ms. Sandy Leggett