

**Decatur County Hospital**  
Leon, Iowa

**Financial Statements**  
**June 30, 2012 and 2011**

**Together with Independent Auditor's Report**

# Decatur County Hospital

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# Decatur County Hospital

## Officials June 30, 2012

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| <u>Board of Trustees</u> | <u>Title</u> | <u>Term Expires</u> |
|--------------------------|--------------|---------------------|
| Guy Clark                | President    | December 2016       |
| Linda Chastain           | Treasurer    | December 2016       |
| Heidi Bell               | Secretary    | December 2014       |
| Gwen Simpson             | Trustee      | December 2012       |
| Leon Kessel              | Trustee      | December 2016       |
| Tom Thomas, III          | Trustee      | December 2012       |
| Sheri Untiedt            | Trustee      | December 2012       |

| <u>Hospital Officials</u> | <u>Title</u>            | <u>Term Expires</u> |
|---------------------------|-------------------------|---------------------|
| Lynn Milnes               | Administrator           | Indefinite          |
| Tara Spidle               | Chief Financial Officer | Indefinite          |

## Independent Auditor's Report

To the Board of Trustees of  
Decatur County Hospital  
Leon, Iowa:

We have audited the accompanying basic financial statements of Decatur County Hospital (Hospital), as of and for the years ended June 30, 2012 and 2011 as listed in the table of contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards 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 the Hospital as of June 30, 2012 and 2011, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 26, 2012 on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of the report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 – 7 and page 24 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 statements 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 about 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.

Our audits were made for the purpose of forming an opinion on the financial statements as a whole. The other supplementary information, included in Exhibits 1-6, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates 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 audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, Exhibits 1-6 are fairly stated in all material respects in relation to the financial statements as a whole.

*Seim Johnson, LLP*

Omaha, Nebraska,  
October 26, 2012.

# Decatur County Hospital

## Management's Discussion and Analysis June 30, 2012 and 2011

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### Introduction

This management's discussion and analysis of the financial performance of Decatur County Hospital (the "Hospital") provides an overview of the Hospital's financial activities for the years ended June 30, 2012 and 2011. It should be read in conjunction with the accompanying financial statements of the Hospital.

### Financial Highlights

- Cash, cash equivalents and short-term investments decreased between 2012 and 2011 by \$2,014,049 or 64% and increased between 2011 and 2010 by \$534,275 or 16%.
- The Hospital's net assets decreased \$640,625 or 7% in 2012 and increased \$904,535 or 11% in 2011.
- The Hospital reported an operating loss in 2012 of \$1,526,206 and operating loss in 2011 of \$67,887. The operating loss in 2012 was an increase of \$1,458,319 from the operating loss reported in 2011 and the operating loss in 2011 was a decrease of \$32,405 from the operating income reported in 2010.
- Net nonoperating revenues decreased by \$39,101 or 4.5% in 2012 compared to 2011 and increased by \$120,847 or 16% in 2011 compared to 2010.

### Required Financial Statements

- The basic financial statements of Decatur County Hospital report information about DCH using Governmental Accounting Standards Board (GASB) accounting principles. These statements offer short-term and long term financial information about its activities.
- The Balance Sheets include all of DCH's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations of DCH creditors (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of DCH, and assessing the liquidity and the financial flexibility of DCH.
- All of the current year's revenues and expenses are accounted for in the Statements of Revenue Expenses, and Changes in Net Assets. This statement measures changes in DCH' operations over the past 2 years and can be used to determine whether DCH has been able to recover all of its costs through its patient service revenue and other revenue sources.
- The final required financial statement is the Statement of Cash Flows. The primary purpose of this statement is to provide information about DCH's cash from operations, investing, and financing activities, and to 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 Analysis of Decatur County Hospital

The Balance Sheets and the Statements of Revenue, Expenses, and Changes in Net Assets report information about DCH's activities. These two statements report the net assets of DCH and changes in them. Increases or decreases in DCH's net assets are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in the healthcare industry, changes in Medicare and Medicaid regulations, and changes in commercial insurance contracting should also be considered.

# Decatur County Hospital

## Management's Discussion and Analysis June 30, 2012 and 2011

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### The Hospital's Net Assets

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheet. The Hospital's net assets decreased by \$640,625 or 7%, in 2012 over 2011 net assets as shown in Table 1.

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

|   | <u>2012</u>                | <u>2011</u>              | <u>2010</u>             |
|---|----------------------------|--------------------------|-------------------------|
| <b>Assets:</b>                                  |                            |                          |                         |
| Current assets                                  | \$ 3,276,387               | 5,421,418                | 5,259,501               |
| Assets limited as to use or restricted          | 6,766,220                  | 1,875,593                | 1,828,149               |
| Capital assets, net                             | 12,610,663                 | 3,901,381                | 2,620,114               |
| Other assets, net                               | 327,983                    | 8,434                    | --                      |
| <b>Total assets</b>                             | <u><u>22,981,253</u></u>   | <u><u>11,206,826</u></u> | <u><u>9,707,764</u></u> |
| <b>Liabilities:</b>                             |                            |                          |                         |
| Long-term debt outstanding                      | 11,781,396                 | 112,418                  | 166,276                 |
| Other current and noncurrent liabilities        | 2,682,116                  | 1,936,042                | 1,287,657               |
| <b>Total liabilities</b>                        | <u><u>14,463,512</u></u>   | <u><u>2,048,460</u></u>  | <u><u>1,453,933</u></u> |
| <b>Net assets:</b>                              |                            |                          |                         |
| Invested in capital assets, net of related debt | 2,813,219                  | 3,788,961                | 2,453,838               |
| Restricted - expendable                         | 85,530                     | --                       | --                      |
| Unrestricted                                    | 5,618,992                  | 5,369,405                | 5,799,993               |
| <b>Total net assets</b>                         | <u><u>\$ 8,517,741</u></u> | <u><u>9,158,366</u></u>  | <u><u>8,253,831</u></u> |

In 2012, significant changes in the Hospital's assets were due to:

- Cash and cash equivalents decreased by \$363,864 due to payments on settlement adjustments from third party payors.
- Internally designated assets increased by \$4,890,627 primarily due to investment in bond funds for the construction project.
- Net capital assets increased by \$8,709,282 due to the continuation of the construction project and an increase in construction in progress.
- Total liabilities increased from 2011 by \$12,415,052 due to the issuance of 2011A and 2011B Series bonds relating to the construction project.

In 2011, significant changes in the Hospital's assets were due to:

- Cash and cash equivalents increased by \$497,669 due to an increase in cash collections and two lump sum interim settlement adjustments from third party payors.

# Decatur County Hospital

## Management's Discussion and Analysis June 30, 2012 and 2011

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- Internally designated assets increased by \$47,444 or 3% primarily due to reinvested interest on certificates of deposits and capital campaign funds for the construction project.
- Net capital assets increased by \$1,281,267 or 49% due to the beginning of the construction project and an increase in construction in progress.
- Total liabilities increased from 2010 by \$594,527 due to an estimated third-party payor settlement of \$615,986.

### Operating Results and Changes in the Hospital's Net Assets

In 2012, the Hospital's net assets decreased by \$640,625 or 7% as shown in Table 2. This decrease is made up of several different components and represents a decrease of \$1,545,160 compared with the increase in net assets for 2011 of \$904,535. The Hospital's change in net assets decreased from \$904,535 in 2011 to (\$640,625) in 2012.

**Table 2: Operating Results and Changes in Net Assets**

|   | <u>2012</u>         | <u>2011</u>      | <u>2010</u>      |
|---|---------------------|------------------|------------------|
| <b>Operating revenue:</b>   |                     |                  |                  |
| Net patient service revenue   | \$ 9,004,437        | 8,788,407        | 9,204,516        |
| Provision for bad debt  | (414,330)           | (411,322)        | (395,634)        |
| Other operating revenues  | (819,316)           | 208,775          | 211,301          |
| <b>Total operating revenue</b>  | <u>7,770,791</u>    | <u>8,585,860</u> | <u>9,020,183</u> |
| <b>Operating expenses:</b>  |                     |                  |                  |
| Salaries and benefits   | 4,660,379           | 4,579,598        | 4,820,268        |
| Purchased services and other  | 3,682,105           | 3,617,625        | 3,815,199        |
| Depreciation and amortization   | 945,049             | 446,890          | 404,954          |
| Interest  | 9,464               | 9,634            | 15,244           |
| <b>Total operating expenses</b>   | <u>9,296,997</u>    | <u>8,653,747</u> | <u>9,055,665</u> |
| <b>Operating loss</b>   | <u>(1,526,206)</u>  | <u>(67,887)</u>  | <u>(35,482)</u>  |
| <b>Nonoperating revenue and expenses</b>  |                     |                  |                  |
| Property taxes  | 731,693             | 702,302          | 632,161          |
| Investment income   | 42,029              | 60,554           | 84,096           |
| Non-capital grants and contributions  | 40,849              | 90,816           | 16,568           |
| <b>Total nonoperating revenue, net</b>  | <u>814,571</u>      | <u>853,672</u>   | <u>732,825</u>   |
| <b>Excess revenue over (under) expenses<br/>before grants and contributions</b> | (711,635)           | 785,785          | 697,343          |
| <b>Grants and contributions</b>   | <u>71,010</u>       | <u>118,750</u>   | <u>101,870</u>   |
| <b>Increase (decrease) in net assets</b>  | (640,625)           | 904,535          | 799,213          |
| <b>Net assets beginning of year</b>   | <u>9,158,366</u>    | <u>8,253,831</u> | <u>7,454,618</u> |
| <b>Net assets end of year</b>   | <u>\$ 8,517,741</u> | <u>9,158,366</u> | <u>8,253,831</u> |

# Decatur County Hospital

## Management's Discussion and Analysis June 30, 2012 and 2011

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### Operating Loss

The first component of the overall change in the Hospital's net assets is its operating income or loss - generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. In 2012, 2011, and 2010, the Hospital reported an operating loss. The Hospital was formed and is operated primarily to serve residents of Decatur County and the surrounding area and the results of operations often reflect losses from operations. As a result of the operating losses, the Hospital levies property taxes to provide sufficient resources to enable the facility to serve patients.

The operating loss of \$1,526,206 for 2012 was an increase of \$1,458,319 from the operating loss in 2011 of \$67,887. The primary components of the change in operating results in 2012 are:

- Net patient service revenue increased \$216,030 from 2011 and total operating expenses in 2012 increased \$1,458,325 from 2011.
- Gross patient service revenue increased \$599,903 or 5% in 2012 as compared to 2011; however, contractual adjustments increased \$425,743 from 2011 primarily due to an increase in Medicare allowances.
- Salaries and wages and employee benefits increased 2% or \$80,781 in 2012 due to increase in benefit expenses. The number of full time equivalents was 82 in 2012 and 2011.
- Professional fees increase in 2012 by \$133,358 or 9% due emergency room visit increases, and increase within pharmacy and anesthesia due to increased coverage within pharmacy and a rate increase for the contracted CRNA.
- Depreciation and amortization expense increased in 2012 by \$498,159 primarily due to a change in the remaining estimated useful life of old hospital building resulting in realizing an additional \$514,000 of depreciation during 2012.

The operating loss of \$67,887 for 2011 was an increase of \$32,405 from the operating loss in 2010 of \$35,482. The primary components of the change in operating results in 2011 are:

- Net patient service revenue decreased \$431,797 or 5% from 2010 and total operating expenses in 2011 decreased \$401,918 or 4% from 2010.
- Gross patient service revenue increased \$1,028,976 or 9% in 2011 as compared to 2010; however, contractual adjustments increased \$1,445,085 from 2010 primarily due to an increase in Medicare allowances.
- Salaries and wages and employee benefits decreased 5% or \$240,670 in 2011 due to decrease in full time equivalents (FTEs). The number of FTEs were 82 in 2011 and 88 in 2010, a 7% decrease.
- Professional fees decreased in 2011 by \$151,975 or 9% due to therapy services being performed in-house, and decrease within pharmacy and anesthesia due to decreased patient volumes.
- Depreciation expense increased in 2011 by \$41,936 or 10% primarily due to additions of approximately \$450,000.

### Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of property taxes levied by the Hospital, interest income and grants and contributions. Property taxes increased \$29,391 from 2011, or 4%. Investment income decreased \$18,525, or 31%. Grants and contributions decreased \$49,967, or 55%.

# Decatur County Hospital

## Management's Discussion and Analysis June 30, 2012 and 2011

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### **The Hospital's Cash Flows**

Changes in the Hospital's cash flows are consistent with changes in the operating results and nonoperating revenues and expenses in 2012 and 2011, discussed earlier.

### **Capital Asset and Debt Administration**

#### Capital Assets

At the end of 2012 and 2011, the Hospital had \$12,610,663 and \$3,901,381, respectively, invested in capital assets, net of accumulated depreciation, as detailed in *Note 5* to the financial statements. In 2012 and 2011, the Hospital purchased new capital assets costing \$11,409,947 and \$1,734,156, respectively. Of the 2012 purchases, \$11,521,150 relate to ongoing construction in process project.

#### Debt

At June 30, 2012 and 2011, the Hospital had \$11,781,396 and \$112,418, respectively, in loans and capital lease obligations outstanding. New debt issued in 2012 was for 2011A and 2011B Series bonds relating to the construction project and for a new ultrasound lease. New debt issued in 2011 was for new copier capital leases.

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

This financial report is designed to provide our patients, suppliers, taxpayers and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Hospital Administration by calling 641.446.4871.

# Decatur County Hospital

## Balance Sheets June 30, 2012 and 2011

|   | <u>2012</u>          | <u>2011</u>       |
|---|----------------------|-------------------|
| <b>ASSETS</b>   |                      |                   |
| Current assets:   |                      |                   |
| Cash and cash equivalents   | \$ 882,558           | 1,246,422         |
| Short-term investments  | 237,512              | 1,887,697         |
| Receivables -   |                      |                   |
| Patients, net of estimated uncollectible accounts<br>of \$175,000 in 2012 and \$208,000 in 2011 | 1,018,586            | 1,112,727         |
| Property taxes  | 664,489              | 711,319           |
| Other   | 98,646               | 96,445            |
| Inventories   | 228,634              | 214,654           |
| Prepaid expenses  | <u>145,962</u>       | <u>152,154</u>    |
| Total current assets  | 3,276,387            | 5,421,418         |
| Assets limited as to use or restricted  | 6,766,220            | 1,875,593         |
| Capital assets, net of accumulated depreciation   | 12,610,663           | 3,901,381         |
| Deferred financing costs  | <u>327,983</u>       | <u>8,434</u>      |
| Total assets  | <u>\$ 22,981,253</u> | <u>11,206,826</u> |
| <b>LIABILITIES AND NET ASSETS</b>   |                      |                   |
| Current liabilities:  |                      |                   |
| Current portion of long-term debt   | \$ 32,785            | 76,441            |
| Accounts payable-   |                      |                   |
| Trade   | 211,636              | 182,839           |
| Construction  | 1,355,903            | 60,898            |
| Salaries, wages and accrued vacation payable  | 375,675              | 365,000           |
| Accrued interest  | 37,635               | --                |
| Estimated third-party payor settlements   | 36,778               | 615,986           |
| Deferred revenue for property taxes   | <u>664,489</u>       | <u>711,319</u>    |
| Total current liabilities   | 2,714,901            | 2,012,483         |
| Long-term debt, net of current portion  | <u>11,748,611</u>    | <u>35,977</u>     |
| Total liabilities   | <u>14,463,512</u>    | <u>2,048,460</u>  |
| Commitments and contingencies:  |                      |                   |
| Net assets:   |                      |                   |
| Invested in capital assets, net of related debt   | 2,813,219            | 3,788,963         |
| Restricted - expendable   | 85,530               | --                |
| Unrestricted  | <u>5,618,992</u>     | <u>5,369,403</u>  |
| Total net assets  | <u>8,517,741</u>     | <u>9,158,366</u>  |
| Total liabilities and net assets  | <u>\$ 22,981,253</u> | <u>11,206,826</u> |

See notes to financial statements

## Decatur County Hospital

### Statements of Revenue, Expenses and Changes in Net Assets For the Years Ended June 30, 2012 and 2011

|   | <u>2012</u>         | <u>2011</u>      |
|---|---------------------|------------------|
| OPERATING REVENUE:  |                     |                  |
| Net patient service revenue before provision for bad debt                       | \$ 9,004,437        | 8,788,407        |
| Provision for bad debt  | <u>(414,330)</u>    | <u>(411,322)</u> |
| Net patient service revenue   | 8,590,107           | 8,377,085        |
| Other operating revenue   | 142,824             | 197,920          |
| Gain (loss) on disposal of property and equipment                               | <u>(962,140)</u>    | <u>10,855</u>    |
| Total operating revenue   | <u>7,770,791</u>    | <u>8,585,860</u> |
| EXPENSES:   |                     |                  |
| Salaries  | 3,437,230           | 3,392,607        |
| Employee benefits   | 1,223,149           | 1,186,991        |
| Purchased services and professional fees  | 1,688,988           | 1,555,630        |
| Supplies and other  | 1,993,117           | 2,061,995        |
| Depreciation and amortization   | 945,049             | 446,890          |
| Interest expense  | <u>9,464</u>        | <u>9,634</u>     |
| Total operating expenses  | <u>9,296,997</u>    | <u>8,653,747</u> |
| OPERATING LOSS  | <u>(1,526,206)</u>  | <u>(67,887)</u>  |
| NONOPERATING REVENUE:   |                     |                  |
| Property taxes  | 731,693             | 702,302          |
| Investment income   | 42,029              | 60,554           |
| Noncapital grants and contributions   | <u>14,781</u>       | <u>90,816</u>    |
| Nonoperating revenue  | <u>788,503</u>      | <u>853,672</u>   |
| EXCESS REVENUE OVER (UNDER) EXPENSES BEFORE<br>CAPITAL GRANTS AND CONTRIBUTIONS | (737,703)           | 785,785          |
| CAPITAL GRANTS AND CONTRIBUTIONS  | <u>97,078</u>       | <u>118,750</u>   |
| INCREASE (DECREASE) IN NET ASSETS   | (640,625)           | 904,535          |
| NET ASSETS, Beginning of year   | <u>9,158,366</u>    | <u>8,253,831</u> |
| NET ASSETS, End of year   | <u>\$ 8,517,741</u> | <u>9,158,366</u> |

*See notes to financial statements*

# Decatur County Hospital

## Statements of Cash Flows For the Years Ended June 30, 2012 and 2011

|   | <u>2012</u>        | <u>2011</u>        |
|---|--------------------|--------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                  |                    |                    |
| Cash received from patients and third-party payors                            | \$ 8,105,040       | 9,463,444          |
| Cash paid for employee salaries and benefits                                  | (4,649,704)        | (4,586,625)        |
| Cash paid to suppliers and contractors  | (3,661,096)        | (3,644,399)        |
| Other receipts and payments, net  | 156,691            | 203,133            |
| Net cash provided by (used in) operating activities                           | <u>(49,069)</u>    | <u>1,435,553</u>   |
| <b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>                       |                    |                    |
| Noncapital grants and contributions   | 14,781             | 90,816             |
| County tax receipts   | 731,693            | 702,302            |
| Net cash provided by noncapital financing activities                          | <u>746,474</u>     | <u>793,118</u>     |
| <b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>              |                    |                    |
| Purchase of property and equipment  | (9,149,079)        | (1,648,441)        |
| Proceeds from issuance of long-term debt                                      | 11,644,952         | --                 |
| Principal payments on long-term debt  | (98,578)           | (90,285)           |
| Interest payments   | (9,464)            | (9,634)            |
| Payments for bond issuance costs  | (331,697)          | (8,434)            |
| Capital grants and contributions  | 81,010             | 49,288             |
| Net cash provided by (used in) capital and related financing activities       | <u>2,137,144</u>   | <u>(1,707,506)</u> |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                  |                    |                    |
| Purchase of investments and assets limited as to use or restricted            | (4,905,147)        | (1,473,839)        |
| Withdrawals from investments and assets limited as to use or restricted       | 1,664,705          | 1,389,789          |
| Investment income   | 42,029             | 60,554             |
| Net cash used in investing activities   | <u>(3,198,413)</u> | <u>(23,496)</u>    |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS                          | (363,864)          | 497,669            |
| CASH AND CASH EQUIVALENTS, Beginning of year                                  | <u>1,246,422</u>   | <u>748,753</u>     |
| CASH AND CASH EQUIVALENTS, End of year  | <u>\$ 882,558</u>  | <u>1,246,422</u>   |
| <b>SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:</b> |                    |                    |
| Equipment acquired under capital lease obligations                            | <u>\$ 122,604</u>  | <u>36,427</u>      |
| Interest payments (expensed and capitalized)                                  | <u>\$ 154,229</u>  | <u>9,634</u>       |

*See notes to financial statements*

# Decatur County Hospital

## Statements of Cash Flows (Continued) For the Years Ended June 30, 2012 and 2011

|   | <u>2012</u>        | <u>2011</u>      |
|---|--------------------|------------------|
| RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:          |                    |                  |
| Operating loss  | \$ (1,526,206)     | (67,887)         |
| Adjustments to reconcile operating income to net cash provided by (used in) operating activities: |                    |                  |
| Depreciation and amortization   | 945,049            | 446,890          |
| Interest expense included in operating expenses   | 9,464              | 9,634            |
| (Gain) loss on disposal of property and equipment   | 962,140            | (10,855)         |
| (Increase) decrease in current assets -   |                    |                  |
| Receivables -   |                    |                  |
| Patients  | 94,141             | 99,734           |
| Other   | 13,867             | 5,213            |
| Inventories   | (13,980)           | (26,849)         |
| Prepaid expenses  | 6,192              | 20,223           |
| Estimated third-party payor settlements   | --                 | 370,639          |
| Increase (decrease) in current liabilities -  |                    |                  |
| Accounts payable - trade  | 28,797             | (20,148)         |
| Accrued salaries, vacation and benefits payable   | 10,675             | (7,027)          |
| Estimated third-party payor settlements   | <u>(579,208)</u>   | <u>615,986</u>   |
| Net cash provided by (used in) operating activities   | \$ <u>(49,069)</u> | <u>1,435,553</u> |

*See notes to financial statements*

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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

The following is a summary of reporting entity and significant accounting policies of Decatur County Hospital (Hospital). These policies are in accordance with accounting principles generally accepted in the United States of America. The Hospital is a Critical Access Hospital, operating with 25 acute-care beds. The Hospital also has related health care ancillary and outpatient services.

#### A. *Reporting Entity*

The financial statements of the Hospital are used to account for the provisions of acute hospital and physician clinic services to the residents of Decatur County and the surrounding area.

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

The Budget Reconciliation Act of 1997 (Act) contained many provisions impacting Medicare reimbursement for Health Services. The Act established the Medicare Rural Hospital Flexibility Program to assist states and rural communities to improve access to essential health care services through limited service hospitals and rural health networks. A Critical Access Hospital (CAH) is an acute care facility that provides emergency, outpatient and short-term inpatient services. Medicare reimburses CAH's on a reasonable cost basis.

The Hospital's application to become certified as a CAH was approved by the Iowa Department of Public Health and the certification was effective July 1, 2002.

#### B. *Industry Environment*

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

Management believes that the Hospital is in compliance with applicable government laws and regulations as they apply to the areas of fraud and abuse. While no regulatory inquiries have been made which are expected to have a material effect on the Hospital's financial statements, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

As a result of recently enacted federal healthcare reform legislation, substantial changes are anticipated in the United States healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement of healthcare providers and the legal obligations of health insurers, providers and employers. These provisions are currently slated to take effect at specified times over approximately the next decade.

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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### C. *Basis of Presentation*

The balance sheets display the Hospital's assets and liabilities, with the differences reported as net assets. Net assets are reported in the following categories:

Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including any restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted net assets - expendable – This component of net assets results when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of the preceding categories. Unrestricted net assets often have constraints on resources imposed by management which can be removed or modified.

### D. *Measurement Focus and Basis of Accounting*

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

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

Pursuant to Section 1600 of the Governmental Accounting Standards Board's (GASB) Codification of Governmental Accounting and Financial Reporting Standards, Health Services has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

### E. *Use of Estimates*

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

### F. *Cash and Cash Equivalents*

Cash and cash equivalents for purposes of the statements of cash flows include highly liquid investments with an original maturity of three months or less, excluding amounts limited as to use by the Board of Trustees, donor or debt agreement.

### G. *Patient Receivables, Net*

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

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

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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

### *H. Inventories*

Inventories are stated at the lower of cost, determined by the first-in, first-out method, or market.

### *I. 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. The succeeding year property tax receivable represents taxes certified by the Board of Supervisors to be collected in the next fiscal year for the purposes set out in the budget for that year. By statute, the Board of Supervisors is required to certify the budget in March of each year for the subsequent 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. Property tax revenue is reported as non-operating revenue when collected by the County Treasurer.

### *J. Assets Limited as to Use or Restricted*

By Board of Trustees – Periodically, the Hospital's Board of Trustees has set aside assets for future capital improvements and equipment. The Board retains control over these funds and may, at its discretion, subsequently use them for other purposes.

Under Debt Agreements - These funds are used for the payment of principal and interest on the Series 2011A and 2011B bonds and to provide funds for the construction of the replacement hospital facility. Debt service reserve fund requirement is \$794,166 and \$409,838 for the Series 2011A and 2011B bonds, respectively. Project fund requirement is \$50,001 and \$268,951 for the Series 2011A and 2011B bonds, respectively. Interest fund requires an amount equal to the interest becoming due on the next interest payment date.

By Donor - These funds consist of contributed assets that have been restricted by the donor for specific capital improvements or operating activities.

### *K. Short-Term Investments*

Short-term investments are assets available for operations without donor imposed restrictions. Short-term investments consist of certificates of deposit and accrued interest, which are recorded at fair value.

### *L. Capital Assets*

Capital assets acquisitions in excess of \$5,000 are capitalized and recorded at cost. Depreciation is computed using the straight-line method based upon useful lives set forth using general guidelines from the American Hospital Association Guide for Estimated Useful Lives of Depreciable Hospital Assets. 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 the depreciation and amortization in the financial statements.

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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Lives range by capital asset classification as follows:

|  |                |
|--|----------------|
| Land improvements                            | 10 to 25 years |
| Buildings and building improvements (Note 5) | 5 to 40 years  |
| Equipment, computers, and furniture          | 3 to 20 years  |

*M. Costs of Borrowing*

Except for capital assets acquired through gifts, contributions or capital grants, interest cost on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring these assets.

*N. Bond Financing Costs*

Bond financing costs related to the issuance of Series 2011A and 2011B bonds are being amortized over the life of the related bonds on a straight-line basis. Amortization expense of \$12,148 and \$0 for the years ended June 30, 2012 and 2011, respectively, is included in depreciation and amortization expense in the accompanying statements of revenue, expenses and changes in net assets.

*O. Compensated Absences*

Hospital employees accumulate a limited amount of earned but unused Paid Time Off (PTO) hours for subsequent use or for payment upon termination, death, or retirement and may be carried forward by an employee at a maximum amount of 240 hours. PTO expense is accrued as an expense and a liability as it is earned. Accrued PTO payable at June 30, 2012 and 2011 was \$202,890 and \$191,519 respectively.

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

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

*Q. Net Patient Service Revenue*

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates, reimbursed costs, and discounted charges. The Hospital has agreements with third-party payors who provide payment based on fee schedule amounts. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

*R. Grants and Contributions*

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

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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S. *Income Taxes*

Under the Code of Iowa, Chapter 347, the Hospital is an instrumentality of the County of Decatur, Iowa. As such, the Hospital is exempt from paying income taxes.

T. *Excess of Revenue Over (Under) Expenses*

The statements of revenue, expenses and changes in net assets include excess of revenue over (under) expense as a performance indicator. Changes in unrestricted net assets that are excluded from excess of revenue over (under) expenses, consistent with industry practice, include gifts, grants and bequests for purchase of property and equipment (including assets acquired using contributions, which by donor restriction were to be used for the purpose of acquiring such assets).

U. *Charity Care*

To fulfill its mission of community service, the Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of these amounts determined to qualify as charity care, they are not reported in the statements of revenue, expenses and changes in net assets. Charges excluded from revenue under the Hospital's charity care policy were \$49,882 and \$91,752 for 2012 and 2011, respectively.

V. *Risk Management*

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

W. *Reclassifications*

Certain amounts in the 2011 financial statements have been reclassified to conform to the 2012 reporting format.

X. *Subsequent Events*

The Hospital considered events occurring through October 26, 2012 for recognition or disclosure in the financial statements as subsequent events. That date is the date the financial statements were available to be issued.

**(2) Cash, Investments and Assets Limited as to Use or Restricted**

The Hospital's deposits in banks at June 30, 2012 and 2011 were entirely covered by federal depository insurance or the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Hospital is authorized by statute to invest public funds in obligations of the United States government, its agencies and 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.

Interest Rate Risk: The Hospital's investment policy does not limit investments on interest rate risk. The Hospital complies with State of Iowa statutes in regards to interest rate risk.

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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The composition of investments and assets limited as to use or restricted as of June 30, 2012 and 2011 is as follows:

|   | <u>2012</u>         | <u>2011</u>      |
|---|---------------------|------------------|
| Investments:  |                     |                  |
| Short-term investments -<br>Certificates of deposit | \$ <u>237,512</u>   | <u>1,887,697</u> |
| Assets Limited as to Use or Restricted:             |                     |                  |
| By the Board of Trustees for -                      |                     |                  |
| Capital improvements -                              |                     |                  |
| Cash and cash equivalents                           | \$ 144,506          | 84,742           |
| Certificates of deposit and accrued interest        | <u>1,810,318</u>    | <u>1,790,851</u> |
|   | <u>1,954,824</u>    | <u>1,875,593</u> |
| By bond agreements:                                 |                     |                  |
| Reserve fund -                                      |                     |                  |
| Certificates of deposit and accrued interest        | 1,218,274           | --               |
| Project fund -                                      |                     |                  |
| Cash and cash equivalents                           | 3,289,138           | --               |
| Interest fund -                                     |                     |                  |
| Cash and cash equivalents                           | <u>303,984</u>      | <u>--</u>        |
|   | <u>4,811,396</u>    | <u>--</u>        |
| Total assets limited as to use or restricted        | \$ <u>6,766,220</u> | <u>1,875,593</u> |

Investment return, including return on assets limited as to use or restricted, for the years ended June 30, 2012 and 2011 is summarized as follows:

|          | <u>2012</u>      | <u>2011</u>   |
|----------|------------------|---------------|
| Interest | \$ <u>42,029</u> | <u>60,554</u> |

### (3) Net Patient Service Revenue

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

**Medicare** - Inpatient acute care services rendered to Medicare program beneficiaries in a Critical Access Hospital are paid based on Medicare defined costs of providing the services. Inpatient nonacute services and certain outpatient services related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor. The Hospital's Medicare cost reports have been audited by the Medicare Administrative Contractor through June 30, 2010.

**Medicaid** - Inpatient acute services and outpatient services rendered to Medicaid program beneficiaries in a Critical Access Hospital are paid based on Medicaid defined costs of providing the services. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital.

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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

The Hospital reports net patient services revenue at estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period related services are rendered and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations.

Revenue from the Medicare and Medicaid programs accounted for approximately 51% and 10%, respectively, of the Hospital's net patient service revenue for the year ended June 30, 2012, and 52% and 10%, respectively, for the year ended June 30, 2011. The Hospital grants credit without collateral to their patients, most of who are local residents and are insured under third-party payor agreements. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The 2011 net patient service revenue increased approximately \$33,000, due to the 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, review and investigations.

A summary of patient service revenue and contractual adjustments for the years ended June 30, 2012 and 2011 are as follows:

|   | <u>2012</u>         | <u>2011</u>        |
|---|---------------------|--------------------|
| Gross patient service revenue:                            |                     |                    |
| Hospital -  |                     |                    |
| Inpatient   | \$ 1,606,229        | 1,860,110          |
| Outpatient  | 11,012,365          | 10,089,402         |
| Swingbed  | 805,208             | 854,854            |
| Surgery clinic  | <u>20,412</u>       | <u>39,945</u>      |
| Total gross patient service revenue                       | <u>13,444,214</u>   | <u>12,844,311</u>  |
| Contractual adjustments:                                  |                     |                    |
| Medicare  | (2,386,301)         | (2,375,772)        |
| Medicaid  | (710,970)           | (462,482)          |
| Other   | (1,292,624)         | (1,125,898)        |
| Charity care services                                     | <u>(49,882)</u>     | <u>(91,752)</u>    |
| Total contractual adjustments                             | <u>(4,439,777)</u>  | <u>(4,055,904)</u> |
| Net patient service revenue before provision for bad debt | <u>\$ 9,004,437</u> | <u>8,788,407</u>   |

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

### (4) Composition of Patient Receivables

Patient receivables as of June 30, 2012 and 2011 consist of the following:

|  | <u>2012</u>         | <u>2011</u>      |
|--|---------------------|------------------|
| Patient accounts                                   | \$ 1,658,586        | 1,576,727        |
| Less estimated third-party contractual adjustments | (465,000)           | (256,000)        |
| Less allowance for doubtful accounts               | <u>(175,000)</u>    | <u>(208,000)</u> |
|  | <u>\$ 1,018,586</u> | <u>1,112,727</u> |

The Hospital grants credits without collateral to its patients, most of whom are insured under third-party payor agreements. The mix of receivables from patients and third-party payors was as follows:

|                         | <u>2012</u>   | <u>2011</u>   |
|-------------------------|---------------|---------------|
| Medicare                | 35.0%         | 28.2%         |
| Medicaid                | 9.9           | 11.1          |
| Blue Cross              | 10.1          | 13.0          |
| Other third party payor | 19.9          | 18.3          |
| Private pay             | <u>25.1</u>   | <u>29.4</u>   |
|                         | <u>100.0%</u> | <u>100.0%</u> |

### (5) Capital Assets

Capital assets and the related accumulated depreciation are summarized as follows:

|  | <u>June 30,<br/>2011</u> | <u>Additions</u>  | <u>Transfers<br/>and Disposals</u> | <u>June 30,<br/>2012</u> |
|--|--------------------------|-------------------|------------------------------------|--------------------------|
| Capital assets, not being depreciated:       |                          |                   |                                    |                          |
| Land   | \$ 44,272                | 15,000            | --                                 | 59,272                   |
| Construction in progress                     | <u>1,228,225</u>         | <u>10,292,925</u> | <u>--</u>                          | <u>11,521,150</u>        |
| Total capital assets, not being depreciated  | <u>1,272,497</u>         | <u>10,307,925</u> | <u>--</u>                          | <u>11,580,422</u>        |
| Capital assets, being depreciated:           |                          |                   |                                    |                          |
| Land improvements                            | 136,779                  | --                | (95,113)                           | 41,666                   |
| Hospital buildings                           | 4,372,835                | --                | (1,548,220)                        | 2,824,615                |
| Major moveable equipment                     | <u>3,523,629</u>         | <u>296,398</u>    | <u>(25,769)</u>                    | <u>3,794,258</u>         |
| Total capital assets, being depreciated      | <u>8,033,243</u>         | <u>296,398</u>    | <u>(1,669,102)</u>                 | <u>6,660,539</u>         |
| Less accumulated depreciation:               |                          |                   |                                    |                          |
| Land improvements                            | 81,125                   | 4,273             | (62,221)                           | 23,177                   |
| Hospital buildings                           | 2,631,999                | 616,913           | (618,972)                          | 2,629,940                |
| Major moveable equipment                     | <u>2,691,235</u>         | <u>311,715</u>    | <u>(25,769)</u>                    | <u>2,977,181</u>         |
| Total accumulated depreciation               | <u>5,404,359</u>         | <u>932,901</u>    | <u>(706,962)</u>                   | <u>5,630,298</u>         |
| Total capital assets, being depreciated, net | <u>2,628,884</u>         | <u>(636,503)</u>  | <u>(962,140)</u>                   | <u>1,030,241</u>         |
| Total capital assets, net                    | <u>\$ 3,901,381</u>      | <u>9,671,422</u>  | <u>(962,140)</u>                   | <u>12,610,663</u>        |

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

|  | June 30,<br>2010    | Additions        | Transfers<br>and Disposals | June 30,<br>2011 |
|--|---------------------|------------------|----------------------------|------------------|
| Capital assets, not being depreciated:       |                     |                  |                            |                  |
| Land   | \$ 44,272           | --               | --                         | 44,272           |
| Construction in progress                     | 21,636              | 1,206,589        | --                         | 1,228,225        |
| Total capital assets, not being depreciated  | <u>65,908</u>       | <u>1,206,589</u> | <u>--</u>                  | <u>1,272,497</u> |
| Capital assets, being depreciated:           |                     |                  |                            |                  |
| Land improvements                            | 136,779             | --               | --                         | 136,779          |
| Hospital buildings                           | 4,290,824           | 82,011           | --                         | 4,372,835        |
| Major moveable equipment                     | 3,153,412           | 445,556          | (75,339)                   | 3,523,629        |
| Total capital assets, being depreciated      | <u>7,581,015</u>    | <u>527,567</u>   | <u>(75,339)</u>            | <u>8,033,243</u> |
| Less accumulated depreciation:               |                     |                  |                            |                  |
| Land improvements                            | 76,852              | 4,273            | --                         | 81,125           |
| Hospital buildings                           | 2,488,465           | 143,534          | --                         | 2,631,999        |
| Major moveable equipment                     | 2,461,492           | 299,083          | (69,340)                   | 2,691,235        |
| Total accumulated depreciation               | <u>5,026,809</u>    | <u>446,890</u>   | <u>(69,340)</u>            | <u>5,404,359</u> |
| Total capital assets, being depreciated, net | <u>2,554,206</u>    | <u>80,677</u>    | <u>(5,999)</u>             | <u>2,628,884</u> |
| Total capital assets, net                    | <u>\$ 2,620,114</u> | <u>1,287,266</u> | <u>(5,999)</u>             | <u>3,901,381</u> |

Total depreciation for the year ended June 30, 2012 and 2011, including depreciation on rental property owned by the Hospital, was \$932,901 and \$446,890 respectively.

Construction in progress at June 30, 2012 consists of costs related to the construction of a replacement hospital facility that began in July 2011 and is expected to be completed in November 2012. Funding for the estimated \$17.2 project will be provided through the Series 2011A and 2011B notes as seen in Note 6 with the remainder to be provided by operations. The Board of Trustees has approved the demolition of the existing hospital facility upon completion of the replacement hospital facility. A change in accounting estimate occurred during fiscal year 2012 as management has adjusted the estimated useful life of the existing facility to coincide with the expected demolition date. This change in estimated useful life resulted in additional, and expected, depreciation expense for the years ended June 30, 2012 and 2013 of approximately \$514,000 and \$134,000, respectively.

### (6) Long-Term Debt

Long-term debt activity of the Hospital for the years ended June 30, 2012 and 2011 is as follows:

|                               | June 30,<br>2011  | Borrowings        | Payments        | June 30,<br>2012  | Due Within<br>One Year |
|-------------------------------|-------------------|-------------------|-----------------|-------------------|------------------------|
| Capital Lease Obligations (A) | 112,418           | 122,604           | (98,578)        | 136,444           | 32,785                 |
| Series 2011A Bonds (B)        | --                | 9,962,000         | --              | 9,962,000         | --                     |
| Series 2011B Bonds (C)        | --                | 1,682,952         | --              | 1,682,952         | --                     |
|                               | <u>\$ 112,418</u> | <u>11,767,556</u> | <u>(98,578)</u> | <u>11,781,396</u> | <u>32,785</u>          |
|                               | June 30,<br>2010  | Borrowings        | Payments        | June 30,<br>2011  | Due Within<br>One Year |
| Capital Lease Obligations (A) | \$ 166,276        | 36,427            | (90,285)        | 112,418           | 76,441                 |
|                               | <u>\$ 166,276</u> | <u>36,427</u>     | <u>(90,285)</u> | <u>112,418</u>    | <u>76,441</u>          |

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

- (A) Capital lease obligations at varying rates of imputed interest from 7.0% to 7.2% maturing through 2016 and collateralized by leased equipment.
- (B) The Hospital issued \$9,962,000 of Hospital Revenue Bonds Series 2011A. The proceeds of these bonds are to be used to construct a replacement hospital facility. The Series 2011A bonds bear interest at rate of 4.3%, maturing in September 14, 2031. The interest rate on the bonds will be adjusted in September 2021 and shall be the greater of 4.3% or the interest rate on a 10 year U.S. Treasury note plus 4% multiplied by .64. Annual principal payments are due beginning in 2014 in amounts ranging from \$197,000 to \$767,000 through September 2031.
- (C) The City of Leon, Iowa issued \$5,141,000 of Hospital Revenue Bonds Series 2011B. Proceeds from the issuance were loaned to the Hospital under a loan agreement between the Hospital and the City of Leon, Iowa. Proceeds from the Series 2011B bonds will be provided to the Hospital in varying draw amounts through May 2013. The interest rate on the bonds will be adjusted in September 2021 and shall be the greater of 4.3% or the interest rate on a 10 year U.S. Treasury note plus 4% multiplied by .64. Annual principal payments are due beginning in 2014 in amounts ranging from \$102,000 to \$396,000 through September 2031.

The Series 2011 bonds grant a security interest in all revenue either accrued or received in connection with operations of the Hospital. The terms of the trust indenture require the Hospital to comply with certain covenants. The covenants provide for restrictions as to financial reporting, restrictions on the sale of the health care facilities and require the Hospital to maintain various reserve accounts.

Assets recorded under capital leases consist of fixed and major moveable equipment items and building components with totals as follows:

|                                | <u>2012</u>       | <u>2011</u>      |
|--------------------------------|-------------------|------------------|
| Cost                           | \$ 634,958        | 512,354          |
| Less: Accumulated amortization | <u>(507,230)</u>  | <u>(431,978)</u> |
| Net book value                 | <u>\$ 127,728</u> | <u>80,376</u>    |

A summary of the Hospital's future principal and interest payments as of June 30, 2012 is as follows:

| <u>Year</u> | <u>Principal</u>     | <u>Interest</u>  | <u>Total</u>      |
|-------------|----------------------|------------------|-------------------|
| 2013        | \$ 32,785            | 604,488          | 637,273           |
| 2014        | 503,412              | 654,733          | 1,158,145         |
| 2015        | 622,121              | 628,904          | 1,251,025         |
| 2016        | 643,124              | 618,641          | 1,261,765         |
| 2017        | 636,000              | 576,354          | 1,212,354         |
| 2018 - 2022 | 3,291,954            | 2,110,245        | 5,402,199         |
| 2023 - 2026 | 2,970,000            | 1,028,375        | 3,998,375         |
| 2027 - 2032 | 3,082,000            | 321,234          | 3,403,234         |
|             | <u>\$ 11,781,396</u> | <u>6,542,974</u> | <u>18,324,370</u> |

The Hospital's policy is to capitalize interest cost on the construction in progress. For the year ended June 30, 2012, the Hospital capitalized \$182,400 of interest costs associated with the Series 2011 bonds.

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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### (7) Net Asset Balances

Restricted, expendable net assets are restricted for the following at June 30, 2012 and 2011:

|                              | <u>2012</u>      | <u>2011</u> |
|------------------------------|------------------|-------------|
| By donors for capital assets | \$ <u>85,530</u> | <u>--</u>   |

### (8) Designated Net Asset

Of the \$5,618,992 and \$5,369,403 of unrestricted net assets reported in 2012 and 2011, respectively \$1,954,824 and \$1,875,593 has been designated by the Hospital's Board of Trustees for capital acquisitions. Designated funds remain under control of the Board of Trustees, which may as its discretion later use the funds for other purposes.

### (9) Pension and Retirement Benefits

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

Plan members are required to contribute 5.38% of their annual salary and the Hospital is required to contribute 8.07% of annual covered payroll. Contribution requirements are established by State statute. The Hospital's contribution to IPERS for the years ended June 30, 2012, 2011 and 2010 were \$281,843, \$243,069, and \$243,106, respectively.

### (10) Management Contract

The Hospital has a contractual arrangement with Mercy Medical Center – Des Moines (Mercy), under which Mercy provides management and other services to the Hospital. The arrangement does not alter the authority of responsibility of the Board of Trustees of the Hospital. The amount paid to Mercy for services during the years ended June 30, 2012 and 2011 were \$375,751 and \$346,433, respectively.

### (11) Professional Liability Insurance

The Hospital carries a professional liability policy (including malpractice) providing coverage of \$1,000,000 for injuries per occurrence and \$3,000,000 aggregate coverage. In addition, the Hospital carries an umbrella policy which also provides \$3,000,000 aggregate coverage. These policies provide coverage on a per occurrence basis covering those claims which have occurred during the coverage period.

Accounting principles generally accepted in the United States of America require a healthcare provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claims experience, no such accrual has been made.

### (12) Commitments and Contingencies

#### Operating Leases

The Hospital leases certain equipment under an operating lease expiring in July 2016. Total rental expense in 2012 and 2011 for this equipment was \$53,496 and \$220,056, respectively.

# Decatur County Hospital

## Notes to Financial Statements June 30, 2012 and 2011

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The following is a schedule by year of future minimum lease payments under operating leases as of June 30, 2012, that have initial lease terms in excess of one year:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2013        | \$ 27,288     |
| 2014        | 20,538        |
| 2015        | 19,278        |
| 2016        | 10,637        |

### (13) Subsequent Events

As seen in Note 6, the proceeds from the Series 2011B bonds will be provided to the Hospital in varying draw amounts through May 2013. The Hospital has drawn an additional \$2,034,000 since June 30, 2012.

## Decatur County Hospital

### Budgetary Comparison Schedule of Revenue, Expenses and Changes in Net Assets Budget and Actual (Cash Basis) For the Year Ended June 30, 2012

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This budgetary comparison is presented as required supplementary information in accordance with Governmental Accounting Standards Board Statement No. 41 for governments with significant budgetary prospective differences resulting from Decatur County Hospital 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 Hospital on the cash basis following required public notice and hearing in accordance with Chapters 24 and 347 of the Code of Iowa. The Board of Trustees certifies the approved budget to the appropriate county auditors. The budget may be amended during the year utilizing similar statutorily prescribed procedures. Formal and legal budgetary control is based on total expenditures.

For the year ended June 30, 2012, the Hospital's expenditures exceeded amounts budgeted.

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

|   | Actual<br>Accrual<br>Basis | Accrual<br>Adjustments | Actual<br>Cash<br>Basis | Budgeted<br>Amounts | Variance<br>Favorable<br>(Unfavorable) |
|---|----------------------------|------------------------|-------------------------|---------------------|--|
| Estimated amount to be raised by taxation | \$ 731,693                 | --                     | 731,693                 | 711,319             | 20,374                                 |
| Estimated other revenues / receipts       | <u>7,924,679</u>           | <u>12,119,824</u>      | <u>20,044,503</u>       | <u>9,331,033</u>    | <u>10,713,470</u>                      |
|   | 8,656,372                  | 12,119,824             | 20,776,196              | 10,042,352          | 10,733,844                             |
| Expenses / Disbursements                  | <u>9,296,997</u>           | <u>8,602,621</u>       | <u>17,899,618</u>       | <u>9,008,510</u>    | <u>(8,891,108)</u>                     |
| Net                                       | (640,625)                  | 3,517,203              | 2,876,578               | <u>\$ 1,033,842</u> | <u>1,842,736</u>                       |
| Balance beginning of year                 | <u>9,158,366</u>           | <u>(3,342,950)</u>     | <u>5,815,416</u>        |                     |  |
| Balance end of year                       | <u>\$ 8,517,741</u>        | <u>174,253</u>         | <u>8,691,994</u>        |                     |  |

*See accompanying independent auditor's report*

**Decatur County Hospital**

**Exhibit 1**

**Net Patient Service Revenue  
For the Years Ended June 30, 2012 and 2011**

|  | 2012                       |                          |                       |                            | 2011                    |                          |                       |                            |
|--|----------------------------|--------------------------|-----------------------|----------------------------|-------------------------|--------------------------|-----------------------|----------------------------|
|  | Inpatient                  | Outpatient               | Swing Bed             | Total                      | Inpatient               | Outpatient               | Swing Bed             | Total                      |
| <b>NURSING SERVICES:</b>   |                            |                          |                       |                            |                         |                          |                       |                            |
| Medical, surgical and obstetrics   | \$ 592,065                 | 452,426                  | --                    | 1,044,491                  | 622,984                 | 362,800                  | --                    | 985,784                    |
| Skilled nursing  | --                         | --                       | 254,526               | 254,526                    | --                      | --                       | 278,637               | 278,637                    |
| Respite  | --                         | --                       | 16,472                | 16,472                     | --                      | --                       | 30,814                | 30,814                     |
| Observation  | --                         | 336,163                  | --                    | 336,163                    | --                      | 254,382                  | --                    | 254,382                    |
|  | <u>592,065</u>             | <u>788,589</u>           | <u>270,998</u>        | <u>1,651,652</u>           | <u>622,984</u>          | <u>617,182</u>           | <u>309,451</u>        | <u>1,549,617</u>           |
| <b>OTHER PROFESSIONAL SERVICES:</b>  |                            |                          |                       |                            |                         |                          |                       |                            |
| Operating and recovery rooms   | 61,187                     | 932,602                  | --                    | 993,789                    | 135,847                 | 980,641                  | 4,623                 | 1,121,111                  |
| Laboratory   | 150,415                    | 2,028,214                | 35,370                | 2,213,999                  | 180,230                 | 1,840,631                | 53,411                | 2,074,272                  |
| Central services and supply  | 25,186                     | 124,352                  | 1,363                 | 150,901                    | 53,330                  | 118,597                  | 4,334                 | 176,261                    |
| Emergency and outpatient service   | 11,733                     | 1,137,648                | --                    | 1,149,381                  | 11,196                  | 1,046,446                | --                    | 1,057,642                  |
| Ambulance  | 27,197                     | 915,493                  | --                    | 942,690                    | 17,455                  | 757,336                  | --                    | 774,791                    |
| Electrocardiology  | 6,956                      | 96,792                   | 592                   | 104,340                    | 7,992                   | 87,172                   | 444                   | 95,608                     |
| Radiology  | 49,682                     | 1,161,195                | 10,899                | 1,221,776                  | 57,655                  | 1,168,461                | 13,713                | 1,239,829                  |
| CT scanner   | 64,467                     | 829,196                  | --                    | 893,663                    | 68,591                  | 697,109                  | --                    | 765,700                    |
| Vascular imaging   | 23,911                     | 289,832                  | --                    | 313,743                    | 9,729                   | 254,922                  | 1,069                 | 265,720                    |
| Cardiac rehab  | --                         | 79,156                   | 4,620                 | 83,776                     | --                      | 158,466                  | 3,080                 | 161,546                    |
| Pharmacy   | 395,236                    | 1,462,168                | 245,701               | 2,103,105                  | 441,207                 | 1,238,268                | 202,118               | 1,881,593                  |
| Anesthesiology   | 24,216                     | 385,400                  | --                    | 409,616                    | 42,694                  | 394,373                  | --                    | 437,067                    |
| Respiratory therapy  | 159,685                    | 213,453                  | 82,326                | 455,464                    | 190,814                 | 212,659                  | 87,243                | 490,716                    |
| Physical therapy   | 11,385                     | 490,679                  | 80,843                | 582,907                    | 16,603                  | 426,381                  | 94,387                | 537,371                    |
| Occupational therapy   | 1,693                      | 67,655                   | 67,718                | 137,066                    | 2,411                   | 81,974                   | 74,580                | 158,965                    |
| Speech therapy   | 1,215                      | 5,801                    | 4,778                 | 11,794                     | 1,372                   | 1,301                    | 6,401                 | 9,074                      |
| Clinics  | --                         | 20,412                   | --                    | 20,412                     | --                      | 39,945                   | --                    | 39,945                     |
| Diabetic education   | --                         | 4,140                    | --                    | 4,140                      | --                      | 7,483                    | --                    | 7,483                      |
|  | <u>1,014,164</u>           | <u>10,244,188</u>        | <u>534,210</u>        | <u>11,792,562</u>          | <u>1,237,126</u>        | <u>9,512,165</u>         | <u>545,403</u>        | <u>11,294,694</u>          |
| <b>GROSS PATIENT SERVICE REVENUE</b>   | <b>\$ <u>1,606,229</u></b> | <b><u>11,032,777</u></b> | <b><u>805,208</u></b> | <b>13,444,214</b>          | <b><u>1,860,110</u></b> | <b><u>10,129,347</u></b> | <b><u>854,854</u></b> | <b>12,844,311</b>          |
| <b>LESS:</b>   |                            |                          |                       |                            |                         |                          |                       |                            |
| Contractual allowances and other deductions, primarily Medicare and Medicaid |                            |                          |                       | (4,389,895)                |                         |                          |                       | (3,964,152)                |
| Charity care services and other discounts, based on charges forgone          |                            |                          |                       | (49,882)                   |                         |                          |                       | (91,752)                   |
| <b>NET PATIENT SERVICE REVENUE BEFORE PROVISION FOR BAD DEBT</b>             |                            |                          |                       | <b>9,004,437</b>           |                         |                          |                       | <b>8,788,407</b>           |
| <b>PROVISION FOR BAD DEBT</b>  |                            |                          |                       | <b>(414,330)</b>           |                         |                          |                       | <b>(411,322)</b>           |
| <b>NET PATIENT SERVICE REVENUE</b>   |                            |                          |                       | <b>\$ <u>8,590,107</u></b> |                         |                          |                       | <b>\$ <u>8,377,085</u></b> |

See accompanying independent auditor's report

**Other Operating Revenue**  
**For the Years Ended June 30, 2012 and 2011**

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|                                       | <u>2012</u>       | <u>2011</u>    |
|---------------------------------------|-------------------|----------------|
| Meals sold                            | \$ 41,798         | 43,855         |
| Laundry                               | 3,158             | 1,337          |
| Medical records transcriptions        | 25,242            | 31,395         |
| Outsourcing of occupational therapist | --                | 26,024         |
| Other                                 | <u>72,626</u>     | <u>95,309</u>  |
|                                       | <u>\$ 142,824</u> | <u>197,920</u> |

*See accompanying independent auditor's report*

**Departmental Expenses  
For the Years Ended June 30, 2012 and 2011**

|                                     | 2012                  |  |                           |                  | 2011                  |  |                           |                  |
|-------------------------------------|-----------------------|--|---------------------------|------------------|-----------------------|--|---------------------------|------------------|
|                                     | Salaries<br>and Wages | Professional Fees<br>and Purchased<br>Services | Supplies<br>and All Other | Total            | Salaries<br>and Wages | Professional Fees<br>and Purchased<br>Services | Supplies<br>and All Other | Total            |
| <b>NURSING SERVICES:</b>            |                       |  |                           |                  |                       |  |                           |                  |
| Medical and surgical                | \$ 74,504             | --   | 1,058                     | 75,562           | 60,251                | --   | 1,973                     | 62,224           |
| Administration                      | 794,457               | 1,215  | 52,911                    | 848,583          | 766,913               | 3,796  | 59,585                    | 830,294          |
|                                     | <u>868,961</u>        | <u>1,215</u>                                   | <u>53,969</u>             | <u>924,145</u>   | <u>827,164</u>        | <u>3,796</u>                                   | <u>61,558</u>             | <u>892,518</u>   |
| <b>OTHER PROFESSIONAL SERVICES:</b> |                       |  |                           |                  |                       |  |                           |                  |
| Operating and recovery room         | 200,734               | 109  | 39,102                    | 239,945          | 212,637               | --   | 52,957                    | 265,594          |
| Central services and supply         | --                    | --   | 66,825                    | 66,825           | --                    | --   | 83,372                    | 83,372           |
| Emergency room                      | 252,098               | 503,720  | 20,733                    | 776,551          | 247,022               | 481,408  | 8,895                     | 737,325          |
| Radiology                           | 202,331               | 293,308  | 158,016                   | 653,655          | 188,656               | 304,487  | 271,018                   | 764,161          |
| Ambulance                           | 212,484               | --   | 36,088                    | 248,572          | 194,931               | --   | 38,998                    | 233,929          |
| Ultrasound                          | --                    | --   | 25,915                    | 25,915           | --                    | --   | 33,308                    | 33,308           |
| Cardiac rehab                       | 62,023                | 134,861  | 6,030                     | 202,914          | 71,923                | 114,880  | 5,392                     | 192,195          |
| Laboratory                          | 182,452               | 2,890  | 348,247                   | 533,589          | 180,709               | 3,415  | 294,169                   | 478,293          |
| Pharmacy                            | 39,306                | 134,420  | 373,611                   | 547,337          | 38,868                | 106,146  | 278,984                   | 423,998          |
| Social services                     | 17,589                | --   | --                        | 17,589           | 12,107                | --   | 44                        | 12,151           |
| Home health                         | 16,552                | 463  | 3,572                     | 20,587           | 31,274                | 2,368  | 4,663                     | 38,305           |
| Anesthesiology                      | --                    | 156,060  | 1,450                     | 157,510          | --                    | 147,437  | 3,516                     | 150,953          |
| Respiratory therapy                 | 71,045                | 36,156   | 26,654                    | 133,855          | 69,417                | 28,900   | 27,168                    | 125,485          |
| Physical therapy                    | 152,298               | 33,202   | 13,996                    | 199,496          | 148,338               | 3,467  | 17,448                    | 169,253          |
| Occupational therapy                | 35,888                | 27,872   | 7,153                     | 70,913           | 53,504                | 23,239   | 8,043                     | 84,786           |
| Speech therapy                      | --                    | --   | 2,618                     | 2,618            | --                    | --   | 1,350                     | 1,350            |
| Clinics                             | 37,807                | --   | 2,749                     | 40,556           | 34,606                | --   | 3,515                     | 38,121           |
| Medical records                     | 142,182               | --   | 18,476                    | 160,658          | 148,150               | 162  | 19,735                    | 168,047          |
| Quality assurance                   | 2,002                 | --   | 281                       | 2,283            | --                    | --   | 444                       | 25,107           |
|                                     | <u>1,626,791</u>      | <u>1,323,061</u>                               | <u>1,151,516</u>          | <u>4,101,368</u> | <u>1,656,805</u>      | <u>1,215,909</u>                               | <u>1,153,019</u>          | <u>4,025,733</u> |
| <b>GENERAL SERVICES:</b>            |                       |  |                           |                  |                       |  |                           |                  |
| Plant operation and maintenance     | 130,057               | 3,012  | 330,573                   | 463,642          | 126,803               | 120  | 390,111                   | 517,034          |
| Laundry and linen                   | 11,262                | 41,685   | 1,912                     | 54,859           | 10,706                | 26,248   | 4,530                     | 41,484           |
| Dietary                             | 169,292               | 38,228   | 75,803                    | 283,323          | 175,602               | 38,553   | 68,716                    | 282,871          |
| Housekeeping                        | 96,144                | 6,581  | 11,995                    | 114,720          | 92,035                | 15,863   | 10,722                    | 118,620          |
|                                     | <u>406,755</u>        | <u>89,506</u>                                  | <u>420,283</u>            | <u>916,544</u>   | <u>405,146</u>        | <u>80,784</u>                                  | <u>474,079</u>            | <u>960,009</u>   |
| <b>ADMINISTRATIVE SERVICES</b>      | <b>534,723</b>        | <b>275,206</b>                                 | <b>298,145</b>            | <b>1,108,074</b> | <b>503,492</b>        | <b>255,141</b>                                 | <b>310,299</b>            | <b>1,068,932</b> |
| <b>NONDEPARTMENTAL:</b>             |                       |  |                           |                  |                       |  |                           |                  |
| Employee benefits                   | --                    | --   | 1,223,149                 | 1,223,149        | --                    | --   | 1,186,991                 | 1,186,991        |
| Depreciation and amortization       | --                    | --   | 945,049                   | 945,049          | --                    | --   | 446,890                   | 446,890          |
| Interest                            | --                    | --   | 9,464                     | 9,464            | --                    | --   | 9,634                     | 9,634            |
| Insurance                           | --                    | --   | 69,204                    | 69,204           | --                    | --   | 63,040                    | 63,040           |
|                                     | <u>--</u>             | <u>--</u>                                      | <u>2,246,866</u>          | <u>2,246,866</u> | <u>--</u>             | <u>--</u>                                      | <u>1,706,555</u>          | <u>1,706,555</u> |
| <b>TOTAL EXPENSES</b>               | <b>\$ 3,437,230</b>   | <b>1,688,988</b>                               | <b>4,170,779</b>          | <b>9,296,997</b> | <b>3,392,607</b>      | <b>1,555,630</b>                               | <b>3,705,510</b>          | <b>8,653,747</b> |

See accompanying independent auditor's report

**Patient Receivables and Allowance for Doubtful Accounts  
For the Years Ended June 30, 2012 and 2011**

## ANALYSIS OF AGING:

| Days Since Discharge                  | 2012                |                  | 2011             |                  |
|---------------------------------------|---------------------|------------------|------------------|------------------|
|                                       | Amount              | Percent of Total | Amount           | Percent of Total |
| 0 - 30                                | \$ 1,067,994        | 64.39 %          | 908,814          | 57.63 %          |
| 31 - 60                               | 263,526             | 15.89            | 247,702          | 15.71            |
| 61 - 90                               | 106,298             | 6.41             | 153,232          | 9.72             |
| 91 - 120                              | 56,699              | 3.42             | 82,732           | 5.25             |
| 121 and over                          | 164,069             | 9.89             | 184,247          | 11.69            |
|                                       | <u>1,658,586</u>    | <u>100.00 %</u>  | <u>1,576,727</u> | <u>100.00 %</u>  |
| Less:                                 |                     |                  |                  |                  |
| Allowance for doubtful accounts       | (175,000)           |                  | (208,000)        |                  |
| Allowance for contractual adjustments | <u>(465,000)</u>    |                  | <u>(256,000)</u> |                  |
|                                       | <u>\$ 1,018,586</u> |                  | <u>1,112,727</u> |                  |

|   | 2012              | 2011             |
|---|-------------------|------------------|
| ALLOWANCE FOR DOUBTFUL ACCOUNTS:              |                   |                  |
| Balance, beginning of year                    | \$ 208,000        | 224,000          |
| Provision of uncollectible accounts           | 414,330           | 411,322          |
| Recoveries of accounts previously written off | 186,656           | 137,029          |
| Accounts written off                          | <u>(633,986)</u>  | <u>(564,351)</u> |
| Balance, end of year                          | <u>\$ 175,000</u> | <u>208,000</u>   |

*See accompanying independent auditor's report*

**Inventories / Prepaid Expenses**  
**For the Years Ended June 30, 2012 and 2011**


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|                                  | <u>2012</u>       | <u>2011</u>    |
|----------------------------------|-------------------|----------------|
| INVENTORIES:                     |                   |                |
| Laboratory                       | \$ 39,881         | 46,390         |
| Plant operations and maintenance | 88,951            | 81,343         |
| Dietary                          | 8,719             | 6,572          |
| Operating room                   | 15,832            | 19,286         |
| Pharmacy                         | 64,445            | 50,056         |
| Laundry                          | 9,962             | 10,148         |
| CT scan                          | 131               | 131            |
| Ambulance                        | 171               | 324            |
| Physical therapy                 | 542               | 404            |
|                                  | <u>\$ 228,634</u> | <u>214,654</u> |
| PREPAID EXPENSES:                |                   |                |
| Insurance                        | \$ 104,443        | 70,785         |
| Maintenance contracts            | 41,519            | 81,369         |
|                                  | <u>\$ 145,962</u> | <u>152,154</u> |

*See accompanying independent auditor's report*

**Financial Statistical Highlights  
For the Years Ended June 30, 2012 and 2011**


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|   | <u>2012</u>         | <u>2011</u>         |
|---|---------------------|---------------------|
| Patient days:                               |                     |                     |
| Adult and pediatric-                        |                     |                     |
| Medicare                                    | 549                 | 556                 |
| Other                                       | <u>222</u>          | <u>261</u>          |
|   | 771                 | 817                 |
| Swing bed - Skilled                         | 719                 | 787                 |
| Respite                                     | <u>122</u>          | <u>210</u>          |
| Total                                       | <u><u>1,612</u></u> | <u><u>1,814</u></u> |
| Patient discharges:                         |                     |                     |
| Adult and pediatric-                        |                     |                     |
| Medicare                                    | 170                 | 154                 |
| Other                                       | <u>91</u>           | <u>99</u>           |
|   | 261                 | 253                 |
| Swing bed - Skilled                         | 75                  | 65                  |
| Respite                                     | <u>17</u>           | <u>11</u>           |
| Total                                       | <u><u>353</u></u>   | <u><u>329</u></u>   |
| Average length of stay:                     |                     |                     |
| Adult and pediatric-                        |                     |                     |
| Medicare                                    | 3.23 days           | 3.61 days           |
| Other                                       | 1.82 days           | 2.64 days           |
| Swing bed - Skilled                         | 9.59 days           | 12.11 days          |
| Respite                                     | 7.17 days           | 19.09 days          |
| Surgical procedures                         | 321                 | 344                 |
| Emergency room visits                       | 2,550               | 2,538               |
| Number of employees - full-time equivalents | 81.99               | 82.21               |

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

To the Board of Trustees of  
Decatur County Hospital  
Leon, Iowa:

We have audited the financial statements of Decatur County Hospital (Hospital), as of and for the year ended June 30, 2012 and 2011, and have issued our report thereon, dated October 26, 2012. 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*

Management of the Hospital is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Hospital'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 an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weakness and a deficiency that we consider to be a significant deficiency.

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 Hospital's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings and Questioned costs as Item II-A-12 to be a material weakness.

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. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings and Questioned Costs as Item II-B-12 to be a significant deficiency.

*Compliance and Other Matters*

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

Comments involving statutory and other legal matters about the Hospital's operations for the year ended June 30, 2012, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Hospital. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

We noted certain matters that we reported to management of the Hospital in a separate letter dated October 26, 2012.

This Hospital's responses to findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the Hospital'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 Decatur County Hospital, and other parties to whom Decatur County Hospital may report. This report is not intended to and should not be used by anyone other than those specified parties.

Seim Johnson, LLP

Omaha, Nebraska,  
October 26, 2012.

# Decatur County Hospital

## Schedule of Findings and Questioned Costs For the Year Ended June 30, 2012

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

- a. An unqualified opinion was issued on the financial statements.
- b. One material weakness and one significant deficiency in internal control over financial reporting were disclosed by the audit of the financial statements.
- c. The audit did not disclose any non-compliance which is material to the financial statements.

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

#### Instances of Non-Compliance

No matters were reported.

#### Material Weakness

##### II-A-12

|                        |  |
|------------------------|--|
| <i>Criteria:</i>       | The design or operation of the Hospital's internal controls should allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements in the financial statements on a timely basis. |
| <i>Condition:</i>      | We identified misstatements in the financial statements during the audit that were not initially identified by the Hospital's internal controls.   |
| <i>Effect:</i>         | Audit entries were required to adjust capital assets, accounts payable, depreciation and amortization, long-term debt and other accounts associated with the Hospital replacement facility project and related debt issuance.                    |
| <i>Cause:</i>          | Management did not identify these required transactions as the transactions are not a normal / recurring transaction for the Hospital.   |
| <i>Recommendation:</i> | The Hospital should review and revise its process over its reconciliation process. The Hospital should also consult professional advice related to abnormal transactions related to the construction project.                                    |
| <i>Response:</i>       | The Hospital concurs with the recommendation.  |
| <i>Conclusion:</i>     | Response accepted.   |

#### Significant Deficiency

##### II-B-12

|                        |   |
|------------------------|---|
| <i>Criteria:</i>       | Proper segregation of duties ensures an adequate internal control structure.  |
| <i>Condition:</i>      | We identified instances where a lack of segregation of duties exists.   |
| <i>Effect:</i>         | Without proper segregation of duties, a greater risk of fraud and defalcation may exist.  |
| <i>Cause:</i>          | Due to a limited number of administrative personnel, a lack of segregation of duties exists.  |
| <i>Recommendation:</i> | We recommend the Hospital continue to monitor and improve its segregation of duties.  |
| <i>Response:</i>       | Management is aware of this control deficiency and believes it is economically not feasible for the Hospital to employ additional personnel for the purpose of greater segregation of duties. The Hospital will continue to maintain and improve its segregation of duties. |
| <i>Conclusion:</i>     | Response accepted.  |

# Decatur County Hospital

## Schedule of Findings and Questioned Costs For the Year Ended June 30, 2012

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

#### III-A-12

Official Depositories: A resolution naming official depositories has been adopted by the Board. The maximum deposit amounts stated in the resolution was exceeded during the year ended June 30, 2012.

Recommendation – Management should review its depository resolution on a regular basis and obtain board approved adjustments when necessary.

Response – The Board of Trustees approved an adjusted depository resolution subsequent to fiscal year end that meets the depository requirements.

Conclusion – Response accepted.

#### III-B-12

Certified Budget: Hospital disbursements during the year ended June 30, 2012 exceeded amounts budgeted.

Recommendation – Management should review its budgeted amounts on a regular basis and make adjustments when necessary in compliance the Code of Iowa..

Response – Management will review its processes and procedures of the establishment and review of budgets.

Conclusion – Response accepted.

#### III-C-12

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

#### III-D-12

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

#### III-E-12

Business Transactions: No business transactions between the Hospital and Hospital officials and/or employees were noted to violate Chapter 347.9A(2)(a) of the Code of Iowa which limits a trustee's pecuniary interest in the purchase or sale of any commodities or supplies procured for or disposed of by said Hospital to \$1,500 without publicly invited and opened written competitive bids.

#### III-F-12

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

#### III-G-12

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

#### III-H-12

Publication of Bills Allowed and Salaries: Chapter 347.13(11) of the Code of Iowa states in part, "There shall be published quarterly in each of the official newspapers of the county as selected by the board of supervisors pursuant to Section 349.1 the schedule of bills allowed and there shall be published annually in such newspaper the schedule of salaries paid by job classification and category..." We noted no instances of noncompliance with the publication of bills allowed and salaries. The Hospital publishes a list of expenditures quarterly which are summarized by major classification and vendor. They also publish a schedule of salaries annually by category.

# Decatur County Hospital

## Summary Schedule of Prior Year Audit Findings For the Year Ended June 30, 2012

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| <u>Finding</u> | <u>Finding title</u>  | <u>Status</u>  | <u>If not corrected, corrective action plan or other explanation</u>   |
|----------------|---|----------------|--|
| II-A-11        | Allowance estimation and review process and pledges receivable reporting. | Corrected.     |  |
| II-B-11        | Segregation of duties in the accounting and data processing areas.        | Not corrected. | Management is aware of this deficiency in internal control and believes it is economically not feasible for the Hospital to employ additional personnel for the purpose of greater segregation of duties. The Hospital will continue to maintain and improve its segregation of duties. Similar finding reported at II-B-12. |

# **Decatur County Hospital**

## **Audit Staff**

**For the Year Ended June 30, 2012**

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### **This audit was performed by:**

- Randy D. Hoffman, CPA, FHFMA, Partner
- Jeremy Behrens, CPA, CHFP, Senior Manager
- Marc D. Behrens, CPA, Staff Auditor

October 26, 2012

To the Board of Trustees  
Decatur County Hospital  
Leon, Iowa:

In planning and performing our audit of the financial statements of Decatur County Hospital (Hospital), as of and for the year ended June 30, 2012, in accordance with auditing standards generally accepted in the United States of America, we considered the Hospital's internal control over financial reporting (internal control) 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 an opinion on the effectiveness of the Hospital's internal control. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified a certain deficiency in internal control that we consider to be a material weakness and a deficiency that we consider to be a significant deficiency.

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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected on a timely basis. We consider the following deficiency in the Hospital's internal control to be a material weakness:

#### **Audit Adjustment**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimations and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements.

As part of the audit, we reviewed the estimates made by management concerning depreciation and the impairment of assets related to the construction project. We noted the useful life of the existing Hospital facility was not reviewed and updated despite management's intention to demolish the facility during fiscal year 2013. A material journal entry was recommended to depreciate the remaining book value of the existing facility over management's intended future useful life. We recommend management review their estimation process for impaired assets and determine if procedures can be added to enhance the estimation process.

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A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charge with governance. We consider the following deficiency in the Hospital's internal control to be a significant deficiency:

#### **Segregation of Duties Over Financial Reporting**

One important aspect of internal control over financial reporting is segregation of duties among employees to prevent an individual employee the ability to circumvent the system of internal controls. In reviewing the financial reporting preparation process and controls, due to a limited number of administrative personnel, a lack of segregation of duties exists. Proper segregation of duties ensures an adequate internal control structure and, without this segregation, a greater risk of fraud and defalcation may exist. We recommend management continue to monitor and improve its segregation of duties.

Management is aware of this deficiency in internal controls and believes it is economically not feasible for the Hospital to employ additional personnel for the purpose of greater segregation of duties. The Hospital will continue to maintain and improve its segregation of duties.

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The following is a description of the identified control deficiencies that we determined do not constitute significant deficiencies or material weaknesses:

#### **Accounts Payable / Construction in Process**

During our audit procedures over accounts payable and construction in process we noted that the "retainage" portion of several invoices relating to construction project were not included in accounts payable and construction in process at year end. As a result, an audit adjustment was made to increase accounts payable and construction in process. We recommend that management evaluate all invoices for completeness and proper cutoff.

#### **Allowance Estimates**

During our audit, we reviewed management's estimation process for third party payor settlements and the allowance for doubtful accounts. We noted management had not estimated the settlement with Medicaid, which resulted in an audit journal entry, but did note that management performed an extensive estimate over the settlement with Medicare. We recommend that management incorporate the results of the Medicare estimate process to develop a Medicaid estimate process. We also noted that management performed an estimation over the allowance for doubtful accounts. During our review of the estimate an audit journal entry was recommended to adjust for inconsistencies in coverage between years. We recommend management continue to monitor and improve its estimate process over the allowance for doubtful accounts.

#### **Bond Issuance**

Series 2011A and Series 2011B revenue bonds were issued during fiscal year 2012 to finance the construction project. During the audit we reviewed transactions related to the bond issuances which resulted in audit journal entries to amortize bond issuance costs and to record accrued interest income related to debt service reserve funds. We recommend that management develop policies and procedures to reconcile and monitor these transactions.

#### **Capital Lease**

As part of the audit we review new leases and management's process to determine if the lease is a capital lease or operating lease. During this review, we noted that a new operating lease met the criteria of a capital lease which resulted in an audit journal entry. We recommend that management review the criteria for capital lease reporting and develop policies and procedures to review all leases for proper reporting.

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The following are offered as constructive suggestions to be considered part of the ongoing process of modifying and improving the Hospital's policies and procedures:

#### **Health Information Technology Incentives**

The Health Information Technology for Economic and Clinical Health Act contains specific financial incentives designed to accelerate the adoption of electronic health record (EHR) systems among health care providers. To qualify for the financial incentive payments, the Hospital must attest it met specific criteria set by the Centers for Medicare and Medicaid Services. That attestation is subject to audit by the federal government or its designee. The EHR incentive payment will be earned and received through various payments through 2015.

The incentive amount is partially based on the value of un-depreciated assets required to implement the EHR system as of the first day the Hospital begins its attestation period. The amount that the Hospital would receive in traditional cost based reimbursement as a critical access hospital for the depreciation on the associated EHR system assets should be deferred and recognized as other operating income over the life of the EHR system assets. The remaining incentive amount should be recognized as other operating income in the Hospital's fiscal year beginning in the federal fiscal year that the attestation is met.

In addition to the federal incentive, the Iowa Department of Health and Human Services provides EHR incentive payments that will be earned and received through various payments for a period of three years. These incentive amounts are recognized as other operating income in the period in which they are received.

#### **340B Drug Discount Program**

The 340B program is a Federal drug discount program that was established in 1992 and was eligible to certain qualifying providers. The *Patient Protection and Affordable Care Act* and the *Health Care and Education Reconciliation Act of 2010* updated the qualifying criteria resulting in automatic eligibility of all critical access hospitals. The program allows the

Hospital to buy outpatient drugs at reduced prices and benefit from the cost savings. The program allows outpatient drugs to be sold by the Hospital and allows the Hospital to contract with local pharmacies to act as its agent. Under the second arrangement, the Hospital is required to purchase the pharmaceuticals and the vendor provides all pharmacy services.

Under the program, the Hospital would be required to:

- Maintain separate records for inpatient and outpatient drugs
- Sell covered outpatient drugs to qualifying patients only
- Ensure covered outpatient drug costs are not subsequently reimbursed by Medicare and Medicaid

We recommend that management review the provisions of the 340B drug discount program and review the potential benefits.

### **Medicare Cost Report Changes**

The Centers for Medicare and Medicaid Services finalized revisions to the Medicare cost report forms. These are the first major changes to the cost report since 1996. The changes modify the cost report to incorporate additional information/revisions for:

- Electronic Health Record (EHR)
- Hospital Uncompensated Care
- Medical Supplies and Implantable Devices
- Incorporation of the 339 Questionnaire

We recommend management review the new cost report forms and instructions to become familiar with the reporting changes. A copy of the new forms and instructions can be downloaded from the CMS website at the following address: <http://www.cms.gov/paperworkreductionactof1995/pral/list.asp>.

### **Accounting for Leases**

The International Accounting Standards Board (IASB), the body responsible for setting International Financial Reporting Standards (IFRS), and the Financial Accounting Standards Board (FASB), the body responsible for setting generally accepted accounting principles, issued a Proposed Accounting Standards Update on August 17, 2010 to Topic 840, *Leases* in response to concerns raised by users of financial statements regarding the treatment of leases. Existing lease accounting treatment has been criticized for its complexity on the basis that it has proved difficult to define the dividing line between capital and operating leases, as the current standards require the application of subjective judgments.

This proposal would apply a right-of-use model in accounting for all leases with a few exceptions. For leases within the scope of the standard, the following guidance would apply to lessees:

- A lessee would recognize an asset representing its right to use the leased asset for the lease term and a liability to make lease payments
- A lessor would recognize an asset representing its right to receive lease payments and, depending on its exposure to risks and benefits, would either:
  - Recognize a liability while continuing to recognize the underlying asset; or
  - Derecognize the asset and continue to recognize a residual asset representing rights to the asset at the end of the lease term

The lease term would be determined assuming the longest possible lease term that is more likely than not to occur. The measurement basis would use an expected outcome technique to reflect lease payments, including contingent rentals and expected payments under term option penalties and residual value guarantees. Those measurement bases would be 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. Leases with terms of 12 months or less would be subject to simplified requirements.

Recently, there have been indications that the IASB and the FASB have acknowledged that not all leases are equal and therefore it may be appropriate to have two separate methods of accounting. An updated proposal has not yet been released. However, they have agreed to consider an approach in which "finance leases" would be treated similarly to a

capital lease and "other-than-finance" leases would appear on the balance sheet but would flow through the income statement similar to operating leases. Further discussion is expected to occur regarding indicators to distinguish between the two types and how the transactions should be recorded.

The original proposal does not include a proposed effective date as the update would be issued in light of other joint projects between the IASB and the FASB. Although these provisions will most likely not be adopted in the near future, it would be prudent for businesses to plan ahead on the basis that the current accounting rules are expected to change, especially when they are negotiating long-term leases or loan facilities with financial covenants that could be impacted by these changes.

### Revenue Cycle Disclosures

In July 2011, the Financial Accounting Standards Board (FASB) issued an Accounting Standards Update to Topic 954, *Health Care Entities* effective for the first annual period ending after December 15, 2012. The proposed update, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities (a consensus of the FASB Emerging Issues Task Force)*, increases required disclosures and requires a change to the statement of operations. Certain health care entities will be required to classify bad debt as a deduction from revenue on the statement of operations, rather than as an operating expense as previously required. Enhanced disclosures include the organization's policy for assessing the timing and amount of uncollectible patient service revenue by major payor source. Major payor sources of revenue shall be identified by the entity and be consistent with how the entity manages its business. Additionally, disclosures will be required to include qualitative and quantitative information about significant changes in the allowance for doubtful accounts related to patient accounts receivable such as significant changes in estimates and underlying assumptions, the amount of self-pay write-offs, the amount of third-party payor write-offs, and other unusual transactions impacting the allowance for doubtful accounts. We recommend that management evaluate their ability to track the required information for each payor class.

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This communication is intended solely for the information and use of the Board of Trustees, management, others within the organization and is not intended to be and should not be used by anyone other than these specified parties. We would be pleased to answer any questions you may have regarding the comments and suggestions contained in the preceding paragraphs.

Sincerely,

SEIM JOHNSON, LLP



Randy D. Hoffman