

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM**

FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 2012 AND 2011

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
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YEARS ENDED JUNE 30, 2012 AND 2011**

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**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
BOARD OF TRUSTEES AND HEALTH SYSTEM OFFICIALS**

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
	<u>Board of Trustees</u>	
Kris Ausborn	Chair	December 31, 2014
Pat Joyce	Treasurer	December 31, 2012
Tammy Naig	Secretary	December 31, 2012
Dawn Schmidt	Trustee	December 31, 2016
James Hobart	Trustee	December 31, 2016
Mary Cooper	Trustee	December 31, 2012
	<u>Health System Officials</u>	
Desiree Einsweiler	Chief Executive Officer	
Renay Hauswirth	Director of Finance	
Coleen Ruddy	Director of Patient Billing	
Joann Higgins	Director of Nursing	



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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Palo Alto County Hospital
dba: Palo Alto County Health System
Emmetsburg, Iowa

We have audited the accompanying balance sheets of Palo Alto County Hospital, dba: Palo Alto County Health System (Health System), as of June 30, 2012, and its discretely presented component unit, Palo Alto County Health Care Foundation (Foundation), as of December 31, 2011, as listed in the table of contents, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Health System's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Palo Alto County Hospital, dba: Palo Alto County Health System were audited by other auditors whose report dated September 6, 2011, expressed an unqualified opinion on those statements.

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

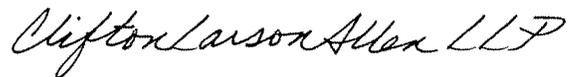
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Health System as of June 30, 2012, and the financial statements of its discretely presented component unit as of December 31, 2011, and the respective changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 17, 2012, on our consideration of the Health System's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Board of Trustees
Palo Alto County Hospital
dba: Palo Alto County Health System

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the 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, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 8 and the Budgetary Comparison Information on pages 34 and 34 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statement in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.



CliftonLarsonAllen LLP

Austin, Minnesota
August 17, 2012

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2012 AND 2011**

This discussion and analysis of the financial performance of Palo Alto County Hospital, dba: Palo Alto County Health System (Health System), provides an overall review of the Health System's financial activities and balances as of and for the years ended June 30, 2012, 2011, and 2010. The intent of this discussion is to provide further information on the Health System's performance as a whole. We encourage readers to consider the information presented here in conjunction with the Health System's financial statements, including the notes thereto, to enhance their understanding of the Health System's financial status.

Overview of the Financial Statements

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

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

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

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

Financial Highlights

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

- The Balance Sheet at June 30, 2012, indicates total assets of \$36,609,342, total liabilities of \$12,137,170 and net assets of \$24,472,172

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2012 AND 2011**

- The Statements of Revenues, Expenses and Changes in Net Assets indicate total net operating revenue of \$22,334,436 an increase of .9% over the previous fiscal year, total operating expenses of \$21,963,864 an increase 2.7% resulting in a gain from operations of \$370,572 or 1.7% compared to 3.4% from the previous year. The Health System had a non-operating gain of \$1,243,251.
- The Health System's current assets exceeded its current liabilities by \$9,602,377 at June 30, 2012, providing a 3.7 current ratio.
- The Health System recorded an excess of revenues over expenses for fiscal year ending June 30, 2012, amounting to \$1,613,823.
- Gross outpatient charges increased 2.6% during fiscal year 2012.
- Total operating expenses increased 2.7% from the previous fiscal year.
- Gross days in accounts receivable continue to be very favorable at 46 on June 30, 2012.
- Total acute patient days total 1,360 a 9.3% decrease from prior year
 - Skilled care days 885 (7.9% increase)
 - Long-term care days 7,814 (1.1% increase)
 - Surgeries 982 (9.4% decrease)
 - Physical Therapy visits 6,656 (1.6% increase)

Organization Highlights

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

- Implemented Dr. First in the clinics. This gives the Providers the ability to send prescriptions electronically directly to the patient's elected pharmacy.
- Installed computers in every exam room in all three clinics – West Bend, Graettinger and Emmetsburg.
- Hired a new Physical Therapist.
- Reduced workman's compensation rates enough to trigger a premium rebate.
- Implemented a new nuclear medicine machine with additional capabilities.
- Started offering new 3D/4D imaging.
- Implemented LEAN philosophy, including Hoshin Strategy Deployment focused on reducing accounts receivable days and improving patient satisfaction scores.
- Developing Medical Home techniques by training 4 Health Coaches.
- Emphasis on recruiting, resulting in the hiring of one new full time physician and one part time pediatrician. Additionally, a few department leader positions that had been on hold were recruited.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2012 AND 2011**

Condensed Financial Statements

Table 1: Assets, Liabilities, and Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>
ASSETS			
Current Assets	\$ 11,985,687	\$ 14,709,294	\$ 11,350,988
Noncurrent Cash and Investments	4,241,311	4,812,847	4,904,639
Capital Assets, Net	19,088,377	20,334,331	21,260,760
Succeeding Year Property Tax Receivable	1,145,423	1,165,193	1,112,548
Other Assets	148,544	280,008	295,428
Total Assets	<u>\$ 36,609,342</u>	<u>\$ 41,301,673</u>	<u>\$ 38,924,363</u>
LIABILITIES			
Current Liabilities	\$ 2,383,310	\$ 3,472,470	\$ 3,030,284
Long-Term Debt (Less Current Maturities)	8,575,912	13,828,705	14,107,186
Deferred Revenue from Succeeding Year Property Tax Receivable	1,145,423	1,165,193	1,112,548
Other Liabilities	32,525	30,367	28,606
Total Liabilities	<u>12,137,170</u>	<u>18,496,735</u>	<u>18,278,624</u>
NET ASSETS			
Invested in Capital Assets Net of Related Debt	10,571,009	6,495,634	7,174,002
Restricted - Expendable Under Bond Agreement	1,092,499	2,044,301	2,320,092
Unrestricted	12,808,664	14,265,003	11,151,645
Total Net Assets	<u>24,472,172</u>	<u>22,804,938</u>	<u>20,645,739</u>
Total Liabilities and Net Assets	<u>\$ 36,609,342</u>	<u>\$ 41,301,673</u>	<u>\$ 38,924,363</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2012 AND 2011**

Long-Term Debt

Palo Alto County Health System had \$90,000 and \$8,575,912 in short-term and long-term debt, respectively, for the year ended June 30, 2012, and \$290,000 and \$13,828,705 in short-term and long-term debt, respectively, for the year ended June 30, 2011. In 2012, the Revenue Bonds, Series 2003, were paid off in full.

Table 2: Statement of Revenues, Expenses and Changes in Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>
OPERATING REVENUES			
Net Patient Service Revenue	\$ 21,255,873	\$ 21,210,779	\$ 19,417,229
Apartment Revenue	419,591	405,195	379,651
Other Revenue	658,972	525,235	553,136
Total Operating Revenues	<u>22,334,436</u>	<u>22,141,209</u>	<u>20,350,016</u>
OPERATING EXPENSES			
Salaries and Wages	8,170,519	7,953,440	7,470,887
Employee Benefits	2,799,758	2,441,901	2,311,688
Supplies and Other Expenses	8,388,955	8,309,946	8,050,798
Depreciation and Amortization	1,863,393	1,934,759	1,762,441
Interest	741,239	739,757	728,754
Total Operating Expenses	<u>21,963,864</u>	<u>21,379,803</u>	<u>20,324,568</u>
OPERATING INCOME	370,572	761,406	25,448
Nonoperating Revenues, Net	<u>1,243,251</u>	<u>1,209,675</u>	<u>1,092,814</u>
EXCESS OF REVENUES AND GAINS OVER EXPENSES AND LOSSES	1,613,823	1,971,081	1,118,262
Capital Grants and Contributions	<u>53,411</u>	<u>188,118</u>	<u>852,500</u>
Increase in Net Assets	1,667,234	2,159,199	1,970,762
Net Assets, Beginning of Year	<u>22,804,938</u>	<u>20,645,739</u>	<u>18,674,977</u>
NET ASSETS, END OF YEAR	<u>\$ 24,472,172</u>	<u>\$ 22,804,938</u>	<u>\$ 20,645,739</u>

**PALO ALTO COUNTY HOSPITAL
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MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2012 AND 2011**

Economic and Other Factors and Next Year's Budget

The Health System's Board and management considered many factors when preparing the fiscal year 2013 budget. Of primary consideration in the 2013 budget are the unknowns of health care reform and the continued difficulty in the status of the economy.

Items listed below were also considered:

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

Summary

The Health System's Board of Trustees and Administrative Team continue to be extremely proud of the excellent patient care, dedication, commitment and support each of our 285 employees provides to every person they serve. We would also like to thank each member of the Health System's Medical Staff for their dedication and support provided.

Contacting the Health System's Finance Department

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

Palo Alto County Health System
Attn: Renay Hauswirth, CFO
3201 1st Street
Emmetsburg, IA 50536

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
BALANCE SHEETS
JUNE 30, 2012 AND 2011**

	2012	2011
ASSETS		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 8,985,297	\$ 11,416,442
Restricted by Bond Agreement	-	337,445
Patient and Resident Receivables, Net of Allowance for Uncollectible Accounts (\$734,600 in 2012, \$715,900 in 2011)	2,109,542	2,446,850
Other Receivables	153,480	88,752
Estimated Third-Party Payor Settlements	357,890	-
Succeeding Year Property Tax Receivable	1,145,423	1,165,193
Supplies	291,249	302,411
Prepaid Expenses	88,229	117,394
Total Current Assets	13,131,110	15,874,487
NONCURRENT CASH AND INVESTMENTS		
Internally Designated for Capital Improvements	3,148,812	3,105,991
Restricted by Bond Agreement	1,092,499	1,706,856
Total Noncurrent Cash and Investments	4,241,311	4,812,847
BOND ISSUANCE COSTS, NET	148,544	280,008
CAPITAL ASSETS, NET	19,088,377	20,334,331
Total Assets	\$ 36,609,342	\$ 41,301,673

See accompanying Notes to Financial Statements.

LIABILITIES AND NET ASSETS	<u>2012</u>	<u>2011</u>
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 90,000	\$ 290,000
Accounts Payable	397,430	450,593
Payable to Affiliated Organization	245,591	236,488
Accrued Expenses:		
Salaries and Wages	157,461	477,488
Paid Time-off	619,596	592,144
Interest	185,831	296,636
Payroll Taxes and Benefits	332,401	154,121
Estimated Health Claims	355,000	285,000
Deferred Revenue - Succeeding Year Property Tax Receivable	1,145,423	1,165,193
Estimated Third-Party Payor Settlements	-	690,000
Total Current Liabilities	<u>3,528,733</u>	<u>4,637,663</u>
SECURITY DEPOSITS	32,525	30,367
LONG-TERM DEBT	<u>8,575,912</u>	<u>13,828,705</u>
Total Liabilities	12,137,170	18,496,735
COMMITMENTS AND CONTINGENCIES		
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	10,571,009	6,495,634
Restricted - Expendable Under Bond Agreement	1,092,499	2,044,301
Unrestricted	12,808,664	14,265,003
Total Net Assets	<u>24,472,172</u>	<u>22,804,938</u>
Total Liabilities and Net Assets	<u>\$ 36,609,342</u>	<u>\$ 41,301,673</u>

**PALO ALTO COUNTY HEALTH CARE FOUNDATION
BALANCE SHEETS
DECEMBER 31, 2011 AND 2010**

	2011	2010
ASSETS		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 532,631	\$ 183,769
Accrued Interest Receivable	3,536	6,834
Total Current Assets	536,167	190,603
NONCURRENT CASH AND INVESTMENTS		
	1,255,099	1,876,521
Total Assets	\$ 1,791,266	\$ 2,067,124
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Property Tax Payable	\$ -	\$ 965
Commitment to Health System	-	245,000
Total Current Liabilities	-	245,965
NET ASSETS		
Unrestricted	1,791,266	1,821,159
Total Liabilities and Net Assets	\$ 1,791,266	\$ 2,067,124

See accompanying Notes to Financial Statements.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2012 AND 2011**

	2012	2011
OPERATING REVENUES		
Net Patient and Resident Service Revenue (Net of Provision for Bad Debts of \$690,457 in 2012 and \$713,070 in 2011)	\$ 21,255,873	\$ 21,210,779
Apartment Revenue	419,591	405,195
Other Operating Revenue	658,972	525,235
Total Operating Revenues	22,334,436	22,141,209
EXPENSES		
Salaries and Wages	8,170,519	7,953,440
Employee Benefits	2,799,758	2,441,901
Supplies and Other Expenses	8,388,955	8,309,946
Depreciation	1,863,393	1,934,759
Interest and Amortization	741,239	739,757
Total Expenses	21,963,864	21,379,803
OPERATING INCOME	370,572	761,406
NONOPERATING REVENUE (EXPENSE)		
Investment Income	65,057	107,252
Tax Apportionments	1,164,039	1,114,606
Noncapital Contributions and Grants	11,905	13,033
Loss on Sale of Capital Assets	2,250	(25,216)
Nonoperating Gains, Net	1,243,251	1,209,675
EXCESS OF REVENUES OVER EXPENSES	1,613,823	1,971,081
CAPITAL GRANTS AND CONTRIBUTIONS	53,411	188,118
INCREASE IN NET ASSETS	1,667,234	2,159,199
Net Assets, Beginning of Year	22,804,938	20,645,739
NET ASSETS, END OF YEAR	\$ 24,472,172	\$ 22,804,938

See accompanying Notes to Financial Statements.

**PALO ALTO COUNTY HEALTH CARE FOUNDATION
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
REVENUES		
Investment Income	\$ 34,676	\$ 55,713
Rental Income	-	5,625
Contributions	22,673	73,872
Total Revenues	<u>57,349</u>	<u>135,210</u>
EXPENSES		
Property Taxes	-	1,930
Other Expenses	357	5,863
Contributions to Health System	86,885	27,418
Total Expenses	<u>87,242</u>	<u>35,211</u>
LOSS ON SALE OF CAPITAL ASSETS	<u>-</u>	<u>(12,633)</u>
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	(29,893)	87,366
Net Assets, Beginning of Year	<u>1,821,159</u>	<u>1,733,793</u>
NET ASSETS, END OF YEAR	<u><u>\$ 1,791,266</u></u>	<u><u>\$ 1,821,159</u></u>

See accompanying Notes to Financial Statements.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2012 AND 2011**

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash Received from Patients, Residents and Third-Party Payors	\$ 20,964,882	\$ 22,018,574
Cash Paid to Employees	(11,125,377)	(7,840,235)
Cash Paid to Suppliers and Contractors	(8,530,243)	(10,798,659)
Other Receipts and Payments, Net	594,244	744,932
Net Cash Provided by Operating Activities	1,903,506	4,124,612
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Non-Capital Grants and Contributions	11,905	13,033
County Tax Revenue Received	1,164,039	1,112,006
Net Cash Provided by Non-Capital Financing Activities	1,175,944	1,125,039
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Principal Payments on Long-Term Debt	(5,575,000)	(275,000)
Purchase of Capital Assets	(479,884)	(1,034,397)
Proceeds from the Sale of Capital Assets	2,250	850
Interest Payments on Long-term Debt	(487,568)	(717,281)
Decrease in Construction Payable	-	(363,255)
Net Security Deposits Received (Paid)	2,158	1,762
Capital Grants and Contributions	53,411	188,118
Net Cash Used by Capital and Related Financing Activities	(6,484,633)	(2,199,203)
CASH FLOWS FROM INVESTING ACTIVITIES		
Sales and Transfers of Investments	908,981	214,658
Investment Income	65,057	107,252
Net Cash Provided by Investing Activities	974,038	321,910
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2,431,145)	3,372,358
Cash and Cash Equivalents - Beginning	11,416,442	8,044,084
CASH AND CASH EQUIVALENTS - ENDING	\$ 8,985,297	\$ 11,416,442

See accompanying Notes to Financial Statements.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
STATEMENTS OF CASH FLOWS (CONTINUED)
YEARS ENDED JUNE 30, 2012 AND 2011**

	2012	2011
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating Income	\$ 370,572	\$ 761,406
Adjustments to Reconcile Adjusted Operating Income to Net Cash Provided by Operating Activities:		
Depreciation	1,863,393	1,934,759
Amortization	253,671	26,939
Interest Expense Considered Capital and Related Financing Activity	487,568	712,818
Provision for Bad Debts	690,457	713,070
(Increase) Decrease in:		
Patient and Resident Receivables	(353,149)	(983,835)
Other Receivables	(64,728)	219,697
Supplies	11,162	(17,852)
Prepaid Expenses	29,165	(37,294)
Increase (Decrease) in:		
Accounts Payable - Trade and Affiliated	(181,615)	60,360
Accrued Expenses	(155,100)	61,179
Estimated Third-Party Payor Settlements	(1,047,890)	673,365
Net Cash Provided by Operating Activities	\$ 1,903,506	\$ 4,124,612
NONCASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Assets included in Accounts Payable	\$ 157,355	\$ -

See accompanying Notes to Financial Statements.

**PALO ALTO COUNTY HEALTH CARE FOUNDATION
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase (Decrease) In Unrestricted Net Assets	\$ (29,893)	\$ 87,366
Adjustments to Reconcile Excess of Operating Revenues over Operating Expenses to Net Cash Provided by Operating Activities:		
Amortization of Premiums on Investments	1,219	1,787
Loss on Sale of Capital Assets	-	12,633
Changes in Assets and Liabilities:		
Accrued Interest Receivable	3,298	3,628
Property Tax Payable	(965)	133
Commitment to Health System	(245,000)	(600,000)
Net Cash Used by Operating Activities	(271,341)	(494,453)
CASH FLOWS FROM CAPITAL AND FINANCING ACTIVITIES		
Proceeds from Sale of Capital Assets	-	22,519
Net Cash Provided by Financing Activities	-	22,519
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Investments	(500,000)	(700,000)
Sale of Investments	1,133,210	1,250,000
Interest Received	-	22,775
Interest Capitalized to Certificates of Deposit	(13,007)	-
Net Cash Provided by Investing Activities	620,203	572,775
NET INCREASE IN CASH AND CASH EQUIVALENTS	348,862	100,841
Cash and Cash Equivalents - Beginning	183,769	82,928
CASH AND CASH EQUIVALENTS - ENDING	\$ 532,631	\$ 183,769

See accompanying Notes to Financial Statements.

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**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization

Palo Alto County Hospital, dba: Palo Alto County Health System (Health System), consists of a 25-bed acute care hospital and a 22-bed skilled nursing/long-term care facility, located in Emmetsburg, Iowa. It is organized under Chapter 347 of the Code of Iowa. The Health System provides health care services in accordance with a Master Affiliation Agreement discussed further in Note 9. Services are provided to residents of Palo Alto County and surrounding counties in Iowa.

Tax Exempt Status

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

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

Reporting Entity

For financial reporting purposes, the Health System has included all funds, organizations, agencies, boards, commissions, and authorities. The Health System has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Health System are such that exclusion would cause the Health System's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Health System to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Health System.

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

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation

The balance sheets display the Health System's assets and liabilities, with the difference reported as net assets. Net assets are reported in the following categories/components:

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

Restricted Net Assets

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

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

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

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

Measurement Focus and Basis of Accounting

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

The Health System's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The accompanying financial statements have been prepared on the accrual basis of accounting. Revenues are recognized when earned and expenses are recorded when the liability is incurred.

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

Use of Estimates

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

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents

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

Patient and Resident Receivables

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

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

The carrying amount of patient and resident receivables is reduced by a valuation allowance that reflects management's estimate of amounts that will not be collected from patients, residents, and third-party payors. Management reviews patient and resident 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 and residents due to bad debts. Management considers historical write off and recovery information in determining the estimated bad debt provision. Management also reviews accounts to determine if classification as charity care is appropriate.

Property Tax Receivable

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

Deferred Revenue

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

Supplies

Supplies are stated at lower of average cost or market.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Assets Limited as to Use or Restricted

Assets limited as to use or restricted include assets set aside by the Board of Trustees for future capital improvements, over which the Board retains control and may at its discretion subsequently use for other purposes; and assets which are restricted by bond agreements. Assets limited as to use or restricted that are available for obligations classified as current liabilities are reported in current assets.

Restricted funds are used to differentiate resources, the use of which is restricted by donors or grantors, from resources of general funds on which donors or grantors place no restriction or which arise as a result of the operations of the Health System for its stated purposes. Resources set aside for board designated purposes are not considered to be restricted. Contributions are reported in nonoperating revenue. Grants restricted for specific operating purposes are reported as other operating revenues.

Capital Assets

Capital asset acquisitions in excess of \$5,000 are capitalized and are recorded at cost. Capital assets donated for the Health System's operations are recorded as additions to net assets at fair value at the date of receipt. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. The estimated useful lives of capital assets are as follows:

Land Improvements	8-20 Years
Buildings and Fixed Equipment	5-56 Years
Major Movable Equipment	3-25 Years

Unamortized Bond Issuance Costs and Expense

Bond issuance costs of \$191,736 from the Series 2006 Hospital Revenue Bonds are being amortized over the life of the bonds using the straight-line method. As of June 30, 2012 and 2011, accumulated amortization was \$43,192 and \$35,039, respectively. Bond issuances costs of \$180,011 from the Series 2003 Hospital Revenue Bonds were being amortized over the life of the bonds using the straight-line method. The 2003 Hospital Revenue Bonds were paid in full during 2012 and the amortization has been accelerated accordingly. As of June 30, 2012 and 2011, accumulated amortization was \$180,011 and \$56,700, respectively. Total amortization expense of the bond issuance costs was \$131,464 and \$15,419 for the years ended June 30, 2012 and 2011, respectively.

Compensated Absences

Health System employees accumulate a limited amount of earned but unused paid time-off for subsequent use or for payment upon termination, death, or retirement. The cost of projected paid time-off payouts is recorded as a current liability on the balance sheet based on rates that are in effect at June 30, 2012 and 2011.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Operating Revenues and Expenses

The Health System's statements of revenues, expenses, and changes in net assets distinguish between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Health System's principal activity. Nonexchange revenues, including interest income, taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, including interest expense.

Net Patient and Resident Service Revenue

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

Patient and resident service revenue is reported at the estimated net realizable amounts from patients, residents, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors and a provision for uncollectible accounts. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Investment Income

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

Contributions and Grants

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

Asset Retirement Obligation

The Health System would recognize an asset retirement obligation in the period in which it incurs a legal obligation associated with the retirement of a tangible long-lived asset, including leased premises, resulting from the acquisition, construction, development, and/or normal use of the asset. The fair value of the asset retirement cost would be capitalized as part of the carrying value of the related long-lived asset and is depreciated over the life of the asset. The liability may be changed to reflect the passage of time and changes in the fair value assessment of the retirement obligation.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Charity Care

To fulfill its mission of community service, the Health System provides care to patients and residents who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Revenue from services to these patients and residents is automatically recorded in the accounting system at the established rates, but the Health System does not pursue collection of the amounts. The resulting adjustments are recorded as adjustments to patient and resident service revenue, depending on the timing of the charity determination.

Electronic Health Record Incentive Payments

As discussed in Note 4, the Health System received funds under the Electronic Health Records (EHR) Incentive Program during 2012. The Health System recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured the Hospital will meet all meaningful use objectives and any other specific grant requirements that are applicable, *e.g.*, electronic transmission of quality measures to CMS in the second and subsequent payment years.

Advertising Costs

The Health System expenses advertising costs as incurred.

County Tax Revenue

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

Subsequent Events

The Health System has evaluated subsequent events through August 17, 2012, the date which the financial statements were available to be issued.

NOTE 2 CHARITY CARE AND COMMUNITY BENEFITS

The Health System maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy. The amounts of charges foregone were \$263,950 and \$264,400 for the years ended June 30, 2012 and 2011, respectively. The estimated costs of the charges foregone, based upon an overall cost-to-charge ratio calculation, for the years ended June 30, 2012 and 2011 were \$172,000 and \$167,000, respectively.

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

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

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 3 NET PATIENT AND RESIDENT SERVICE REVENUE

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

Medicare

The Health System is licensed as a Critical Access Hospital (CAH). The Health System is reimbursed for most inpatient and outpatient services at cost with final settlement determined after submission of annual cost reports by the Health System and are subject to audits thereof by the Medicare fiscal intermediary. The Health System's Medicare cost reports have been settled by the Medicare fiscal intermediary through the year ended June 30, 2010.

Medicaid

Hospital

Inpatient and outpatient services rendered to Medicaid program beneficiaries are paid based on a cost reimbursement methodology. The Health System is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Health System and audits thereof by the Medicaid fiscal intermediary. The Health System's Medicaid cost reports have been processed by the Medicaid fiscal intermediary through June 30, 2009.

Nursing Home

Routine services rendered to nursing home residents who are beneficiaries of the Medicaid program are paid according to a schedule of prospectively determined daily rates.

Other Payors

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

Revenue from the Medicare and Medicaid programs accounted for approximately 47% and 11%, respectively, of the Health System's net patient and resident service revenue for the year ended June 30, 2012, and 45% and 11%, respectively, of the Health System's net patient and resident service revenue for the year ended June 30, 2011. The 2012 and 2011 net patient and resident service revenue increased approximately, \$51,000 and \$336,000, respectively, due to the removal of allowances previously estimated that are no longer necessary as a result of final settlements, adjustments in excess of amounts previously estimated, and years that are no longer subject to audits, reviews, and investigations.

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

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 3 NET PATIENT AND RESIDENT SERVICE REVENUE (CONTINUED)

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

A summary of patient and resident service revenue, contractual adjustments, and provision for bad debts for the years ended June 30, 2012 and 2011 is as follows:

	2012	2011
Total Patient and Resident Service Revenue	\$ 32,683,061	\$ 32,163,008
Revenue Adjustments:		
Medicare	(4,991,017)	(5,311,901)
Medicaid	(892,119)	(740,620)
Provision for Bad Debt	(690,457)	(713,070)
Commercial and Other	(4,853,595)	(4,186,638)
Total Contractual Adjustments and Bad Debts	(11,427,188)	(10,952,229)
Net Patient and Resident Service Revenue	\$ 21,255,873	\$ 21,210,779

NOTE 4 ELECTRONIC HEALTH RECORD INCENTIVE PROGRAM

The Electronic Health Record (EHR) incentive program was enacted as part of the American Recovery and Reinvestment Act of 2009 (ARRA) and the Health Information Technology for Economic and Clinical Health (HITECH) Act. These Acts provided for incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified EHR technology. The incentive payments are made based on a statutory formula and are contingent on the Organization continuing to meet the escalating meaningful use criteria. For the first payment year, the Health Center must attest, subject to an audit, that it met the meaningful use criteria for a continuous 90-day period. For the subsequent payment year, the Health Center must demonstrate meaningful use for the entire year. The incentive payments are generally made over a four year period. For hospitals that do not start receiving meaningful use payments until federal fiscal year 2014 or 2015, the base payment amount will reduce in subsequent years by ¼, ½, and ¾.

The Health System demonstrated meaningful use to the 90-day period ended September 1, 2011, and received the first tentative incentive payment of \$28,044 in March 2012. This amount is recognized as other operating revenue in the statements of revenues, expenses, and changes in net assets. The final amount of this payment will be determined based on information from the Health Centers' Medicare cost report. Events could occur that would cause the final payment to differ materially upon final settlement.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 5 DEPOSITS AND INVESTMENTS

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

At June 30, 2012 and 2011, the Health System's carrying amounts of deposits and investments are as follows:

	<u>2012</u>	<u>2011</u>
Checking and Savings Accounts	\$ 8,985,297	\$ 11,416,442
Certificates of Deposit	3,148,812	3,444,790
Money Market Accounts	1,092,499	1,705,502
Total Deposits	<u>\$ 13,226,608</u>	<u>\$ 16,566,734</u>
Included in the Following Balance Sheet Captions:		
Cash and Cash Equivalents	\$ 8,985,297	\$ 11,416,442
Restricted Under Bond Agreement - Current	-	337,445
Assets Limited as to Use or Restricted	4,241,311	4,812,847
	<u>\$ 13,226,608</u>	<u>\$ 16,566,734</u>

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

At December 31, 2011 and 2010, the Foundation's carrying amounts of deposits and investments are as follows:

	<u>2011</u>	<u>2010</u>
Certificates of Deposit	<u>\$ 1,255,099</u>	<u>\$ 1,876,521</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 6 CAPITAL ASSETS

Capital assets activity for the years ended June 30, 2012 and 2011 was as follows:

	July 1, 2011	Additions	(Retirements)	Transfers	June 30, 2012
Capital Assets Not Being Depreciated					
Land	\$ 140,365	\$ -	\$ -	\$ -	\$ 140,365
Construction in Progress	-	6,922	-	-	6,922
Total Capital Assets Not Being Depreciated	140,365	6,922	-	-	147,287
Capital Assets Being Depreciated					
Land Improvements	301,978	-	-	-	301,978
Buildings	23,225,227	133,347	-	-	23,358,574
Fixed Equipment	2,060,888	-	-	-	2,060,888
Major Movable Equipment	7,210,101	503,872	(162,099)	-	7,551,874
Total Capital Assets Being Depreciated	32,798,194	637,219	(162,099)	-	33,273,314
Accumulated Depreciation					
Land Improvements	202,455	14,662	-	-	217,117
Buildings	6,314,516	1,012,551	-	-	7,327,067
Fixed Equipment	1,482,571	79,764	-	-	1,562,335
Major Movable Equipment	4,604,686	756,416	(135,397)	-	5,225,705
Total Accumulated Depreciated	12,604,228	1,863,393	(135,397)	-	14,332,224
Total Capital Assets Being Depreciated, Net	20,193,966	(1,226,174)	(26,702)	-	18,941,090
Total Capital Assets, Net	<u>\$ 20,334,331</u>	<u>\$ (1,219,252)</u>	<u>\$ (26,702)</u>	<u>\$ -</u>	<u>\$ 19,088,377</u>
	July 1, 2010	Additions	(Retirements)	Transfers	June 30, 2011
Capital Assets Not Being Depreciated					
Land	\$ 140,365	\$ -	\$ -	\$ -	\$ 140,365
Construction in Progress	6,600	-	-	(6,600)	-
Total Capital Assets Not Being Depreciated	146,965	-	-	(6,600)	140,365
Capital Assets Being Depreciated					
Land Improvements	276,577	40,901	(15,500)	-	301,978
Buildings	23,206,741	38,343	(19,857)	-	23,225,227
Fixed Equipment	2,068,798	123,847	(131,757)	-	2,060,888
Major Movable Equipment	6,574,808	831,306	(202,613)	6,600	7,210,101
Total Capital Assets Being Depreciated	32,126,924	1,034,397	(369,727)	6,600	32,798,194
Accumulated Depreciation					
Land Improvements	191,541	10,914	-	-	202,455
Buildings	5,326,054	1,006,547	(18,085)	-	6,314,516
Fixed Equipment	1,530,444	78,843	(126,716)	-	1,482,571
Major Movable Equipment	3,965,090	838,457	(198,861)	-	4,604,686
Total Accumulated Depreciated	11,013,129	1,934,761	(343,662)	-	12,604,228
Total Capital Assets Being Depreciated, Net	21,113,795	(900,364)	(26,065)	6,600	20,193,966
Total Capital Assets, Net	<u>\$ 21,260,760</u>	<u>\$ (900,364)</u>	<u>\$ (26,065)</u>	<u>\$ -</u>	<u>\$ 20,334,331</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 7 LONG-TERM DEBT

A schedule of changes in long-term debt for 2012 and 2011 is as follows:

	Balance July 1, 2011	Additions	(Payments) & (Amortization)	Balance June 30, 2012	Amounts Due Within One Year
Hospital Revenue Bonds, Series 2003	\$ 5,485,000	\$ -	\$ (5,485,000)	\$ -	\$ -
Hospital Revenue Bonds, Series 2006	8,840,000	-	(90,000)	8,750,000	90,000
	14,325,000	-	(5,575,000)	8,750,000	90,000
Bond Discount	(15,956)	-	15,956	-	-
Deferred Loss on Bond Refinancing	(101,636)	-	101,636	-	-
Bond OID Less Premium 2006	(88,703)	-	4,615	(84,088)	-
	<u>\$ 14,118,705</u>	<u>\$ -</u>	<u>\$ (5,452,793)</u>	8,665,912	<u>\$ 90,000</u>
Total Long-Term Debt				(90,000)	
Less Current Maturates				<u>\$ 8,575,912</u>	

	Balance July 1, 2010	Additions	(Payments) & (Amortization)	Balance June 30, 2011	Amounts Due Within One Year
Hospital Revenue Bonds, Series 2003	\$ 5,680,000	\$ -	\$ (195,000)	\$ 5,485,000	\$ 200,000
Hospital Revenue Bonds, Series 2006	8,920,000	-	(80,000)	8,840,000	90,000
	14,600,000	-	(275,000)	14,325,000	290,000
Bond Discount	(16,888)	-	932	(15,956)	-
Deferred Loss on Bond Refinancing	(107,570)	-	5,934	(101,636)	-
Bond OID Less Premium 2006	(93,356)	-	4,653	(88,703)	-
	<u>\$ 14,382,186</u>	<u>\$ -</u>	<u>\$ (263,481)</u>	14,118,705	<u>\$ 290,000</u>
Total Long-Term Debt				(290,000)	
Less Current Maturates				<u>\$ 13,828,705</u>	

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

Years Ending June 30,	Long-Term Debt		
	Principal	Interest	Total
2013	\$ 90,000	\$ 447,963	\$ 537,963
2014	95,000	443,969	538,969
2015	100,000	439,806	539,806
2016	100,000	435,356	535,356
2017	105,000	425,850	530,850
2018-2022	625,000	2,042,779	2,667,779
2023-2027	805,000	1,858,813	2,663,813
2028-2032	2,515,000	1,509,697	4,024,697
2033-2037	4,315,000	574,640	4,889,640
	<u>\$ 8,750,000</u>	<u>\$ 8,178,873</u>	<u>\$ 16,928,873</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 7 LONG-TERM DEBT (CONTINUED)

The Hospital Revenue Bonds, Series 2003 were issued in the amount of \$6,735,000 on August 1, 2003. Payments of interest at rates from 1.7% to 5.4% were payable semi-annually on February 1 and August 1, and principal payments were due annually on August 1. In fiscal 2012, the Health System paid the Hospital Revenue Bonds, Series 2003, in full.

The Hospital Revenue Bonds, Series 2006 were issued in the amount of \$9,000,000 on August 1, 2006. Payments of interest at rates from 4.125% to 5.250% are payable semi-annually on February 1 and August 1, and principal payments are due annually on August 1 through 2036. The bonds are collateralized by the patient and resident revenues of the Health System.

The Health System is subject to certain covenants under the bond agreement regarding the funding of debt service reserve and sinking fund accounts. The Health System was in compliance with these covenants for the years ended June 30, 2012 and 2011.

The bond resolution of the Series 2003 bonds required the establishment of the following "Funds":

Sinking Fund – into which the Health System was required to deposit a monthly sum equal to at least one-sixth of the interest coming due on the bonds on the next interest payment date. In addition, the Health System was required to deposit a monthly sum equal to at least one-twelfth of the principal coming due on the bonds on the next principal date.

Debt Service Reserve Fund – into which the Health System was required to deposit an amount equal to the lesser of (i) 100% of the maximum principal and interest due in any fiscal year with respect to the bonds, (ii) 125% of the average annual debt service payment with respect to the bonds, (iii) 10% of the original principal amount of the bonds.

The bond resolution of the Series 2006 bonds requires the establishment of the following "Funds":

Sinking Fund – into which the Health System is required to deposit a monthly sum equal to at least one-sixth of the interest coming due on the bonds on the next interest payment date. In addition, the Health System is required to deposit a monthly sum equal to at least one-twelfth of the principal coming due on the bonds on the next principal date.

Debt Service Reserve Fund – into which the Health System was required to deposit an amount equal to the sum of \$821,323, to fund final debt payment on August 1, 2036.

NOTE 8 PENSION AND RETIREMENT BENEFITS

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

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 8 PENSION AND RETIREMENT BENEFITS (CONTINUED)

Plan members are required to contribute 5.38% of their annual covered salary, and the Health System is required to contribute 8.07% of annual covered payroll for the year ended June 30, 2012. Plan members were required to contribute 4.50% and 4.30% of their annual covered salary, and the Health System was required to contribute 6.95% and 6.65% of annual covered payroll for the years ended June 30, 2010 and 2009, respectively. Contribution requirements are established by state statute. The Health System's contributions to IPERS for the years ended June 30, 2012, 2011, and 2010, were \$659,042, \$563,323, and \$500,694, respectively, equal to the required contributions for each year.

NOTE 9 RELATED ORGANIZATIONS

Master Affiliation Agreement

The Health System has a Master Affiliation Agreement with Mercy Medical Center – North Iowa (MMC-NI) to provide hospital, physician, and other health care services in Palo Alto County and surrounding counties in central Iowa. As a part of this Master Affiliation Agreement, the Health System entered into a Professional Service Agreement with MMC-NI whereby MMC-NI provides professional medical services for the Health System. Amounts paid to MMC-NI for the provision of these services amounted to \$2,405,811 and \$2,375,546 for the years ended June 30, 2012 and 2011, respectively.

Management Services Agreement

The Health System has a contractual arrangement with MMC-NI under which MMC-NI provides administrative staff, management consultation, and other services to the Health System. The arrangement does not alter the authority or responsibility of the Board of Trustees of the Health System. Expenses for the administrative and management services for the years ended June 30, 2012 and 2011 were \$708,811 and \$702,659, respectively.

Due to Affiliated Organization

As of June 30, 2012 and 2011, the Health System's records reflect an amount due to MMC-NI of \$245,591 and \$236,488, respectively, for the various services and distributions related to these agreements.

NOTE 10 CONTINGENCIES

Malpractice Insurance

The Health System has insurance coverage to provide protection for professional liability losses on a claims-made basis subject to a limit of \$1 million per claim and an aggregate limit of \$3 million. The Health System also has directors' and officers' insurance coverage to provide protection for losses on a claims-made basis subject to a limit of \$2 million per claim and an aggregate limit of \$2 million. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term, but reported subsequently, will be uninsured.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 10 CONTINGENCIES (CONTINUED)

Excess Liability Umbrella Insurance

The Health System also has excess liability umbrella coverage on a claims-made basis subject to a limit of \$5 million per occurrence and an annual aggregate limit of \$5 million. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term, but reported subsequently, will be uninsured.

Self-Funded Employee Health Insurance Plan

The Health System has a self-funded employee health insurance plan covering substantially all employees. The plan is responsible to pay all administration expenses and benefits up to the reinsurance limits. A liability of \$355,000 and \$285,000 has been established to record the incurred but not reported claims outstanding at June 30, 2012 and 2011.

Health Care Legislation and Regulation

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient and resident services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violation of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient and resident services previously billed.

NOTE 11 RISK MANAGEMENT

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

NOTE 12 CONCENTRATION OF CREDIT RISK

The Health System grants credit without collateral to its patients and residents, most of whom are insured under third-party payor agreements. The mix of receivables from third-party payors, patients, and residents at June 30, 2012 and 2011 was as follows:

	2012	2011
Medicare	34%	31%
Medicaid	8%	6%
Blue Cross	17%	22%
Other Third-Party Payors, Patients and Residents	41%	41%
	<u>100%</u>	<u>100%</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 13 FOUNDATION COMMITMENT

The Palo Alto County Health Care Foundation committed \$845,000 to the Health System's construction and renovation project in fiscal year 2009. During the year ended June 30, 2010, the Foundation paid \$600,000 of the pledged balance to the Health System. The remaining pledged balance of \$245,000 was paid to the Health System during March 2011.

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REQUIRED SUPPLEMENTARY INFORMATION

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**PALO ALTO COUNTY HOSPITAL
 DBA: PALO ALTO COUNTY HEALTH SYSTEM
 BUDGETARY COMPARISON SCHEDULE OF REVENUES, EXPENSES, AND
 CHANGES IN NET ASSETS – BUDGET AND ACTUAL (CASH BASIS)
 REQUIRED SUPPLEMENTARY INFORMATION
 YEAR ENDED JUNE 30, 2012**

	General Fund	Accrual Adjustments	Cash Basis	Original Budget	Final to Actual Cash Basis Variance
Estimated Amount to be Raised by Taxation	\$ 1,164,039	\$ -	\$ 1,164,039	\$ 1,165,192	\$ (1,153)
Estimated Other Revenues/Receipts	<u>22,467,059</u>	<u>135,829</u>	<u>22,602,888</u>	<u>23,897,931</u>	<u>(1,295,043)</u>
	23,631,098	135,829	23,766,927	25,063,123	(1,296,196)
Expenses/Disbursements	<u>21,963,864</u>	<u>4,234,208</u>	<u>26,198,072</u>	<u>22,951,051</u>	<u>(3,247,021)</u>
Net	1,667,234	(4,098,379)	(2,431,145)	2,112,072	(4,543,217)
Balance Beginning of Year	<u>22,804,938</u>	<u>(11,388,496)</u>	<u>11,416,442</u>	<u>9,375,636</u>	<u>2,040,806</u>
Balance End of Year	<u><u>\$ 24,472,172</u></u>	<u><u>\$ (15,486,875)</u></u>	<u><u>\$ 8,985,297</u></u>	<u><u>\$ 11,487,708</u></u>	<u><u>\$ (2,502,411)</u></u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING
YEAR ENDED JUNE 30, 2012**

This budgetary comparison is presented as Required Supplementary Information in accordance with Governmental Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from the Health System preparing a budget on the cash basis of accounting.

The Board of Trustees annually prepares and adopts a budget designating the amount necessary for the improvement and maintenance of the Health System on the cash basis following required public notice and hearing in accordance with Chapters 24 and 347 of the Code of Iowa. The Board of Trustees certifies the approved budget to the appropriate county auditors. The budget may be amended during the year utilizing similar statutorily prescribed procedures. Formal and legal budgetary control is based on total expenditures. The Health System did not amend its original budget during the year ended June 30, 2011.

For the year ended June 30, 2012, the Health System's expenditures exceeded the amount budgeted.

OTHER SUPPLEMENTARY INFORMATION

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULES OF NET PATIENT AND RESIDENT SERVICE REVENUE
YEARS ENDED JUNE 30, 2012 AND 2011**

	Total	
	2012	2011
PATIENT AND RESIDENT SERVICE REVENUE		
Medical and Surgical	\$ 1,262,072	\$ 1,324,483
Nursery	166,831	147,245
Long-Term Care	1,201,828	1,149,029
Total Patient and Resident Service Revenue	<u>2,630,731</u>	<u>2,620,757</u>
OTHER PROFESSIONAL SERVICE REVENUE		
Operating Room	2,984,871	3,003,101
Emergency Room	2,648,604	2,647,962
Labor and Delivery Room	95,336	92,582
Obstetric Services	379,461	365,885
Anesthesiology	724,756	768,797
Radiology and Ultrasound	5,027,574	4,692,031
Laboratory	3,560,267	3,312,493
Respiratory Therapy	1,110,535	1,142,580
Physical Therapy	992,505	1,005,913
Occupational Therapy	148,808	138,496
Speech Therapy	22,220	39,931
Electrocardiology	579,076	592,215
Medical and Surgical Supplies	552,566	563,881
Pharmacy	3,561,136	3,533,215
Ambulance	890,799	946,661
Home Health	602,985	634,831
Hospice	762,726	454,969
Cardiac Rehabilitation	70,827	144,120
Pulmonary Rehabilitation	39,289	44,560
Graettinger Clinic	463,773	451,040
Emmetsburg Clinic	4,212,454	4,320,358
West Bend Clinic	885,712	911,030
Total Other Professional Service Revenue	<u>30,316,280</u>	<u>29,806,651</u>
Gross Patient and Resident Charges	32,947,011	32,427,408
Charity Care	<u>(263,950)</u>	<u>(264,400)</u>
Total Patient Service Revenues	32,683,061	32,163,008
CONTRACTUAL ADJUSTMENTS		
Medicare	(4,991,017)	(5,311,901)
Medicaid	(892,119)	(740,620)
Commercial and Other	(4,853,595)	(4,186,638)
Total Contractual Adjustments	<u>(10,736,731)</u>	<u>(10,239,159)</u>
Patient and Resident Service Revenues, Net of Contractual Adjustments	21,946,330	21,923,849
Provision for Bad Debts	<u>(690,457)</u>	<u>(713,070)</u>
Net Patient and Resident Service Revenues	<u>\$ 21,255,873</u>	<u>\$ 21,210,779</u>

Inpatient		Outpatient	
2012	2011	2012	2011
\$ 1,262,072	\$ 1,324,483	\$ -	\$ -
166,831	147,245	-	-
1,201,828	1,149,029	-	-
<u>2,630,731</u>	<u>2,620,757</u>	-	-
338,004	332,915	2,646,867	2,670,186
142,225	161,750	2,506,379	2,486,212
95,336	92,582	-	-
290,934	252,957	88,527	112,928
53,953	70,194	670,803	698,603
216,499	271,309	4,811,075	4,420,722
380,817	377,527	3,179,450	2,934,966
654,642	705,005	455,893	437,575
165,379	163,263	827,126	842,650
59,121	50,282	89,687	88,214
3,026	5,207	19,194	34,724
43,513	36,253	535,563	555,962
75,746	93,849	476,820	470,032
829,670	859,290	2,731,466	2,673,925
-	-	890,799	946,661
-	-	602,985	634,831
20,896	48,690	741,830	406,279
-	-	70,827	144,120
-	-	39,289	44,560
-	-	463,773	451,040
-	-	4,212,454	4,320,358
-	-	885,712	911,030
<u>3,369,761</u>	<u>3,521,073</u>	<u>26,946,519</u>	<u>26,285,578</u>
<u>\$ 6,000,492</u>	<u>\$ 6,141,830</u>	<u>\$ 26,946,519</u>	<u>\$ 26,285,578</u>

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**PALO ALTO COUNTY HOSPITAL
 DBA: PALO ALTO COUNTY HEALTH SYSTEM
 SCHEDULES OF OTHER OPERATING REVENUES
 YEARS ENDED JUNE 30, 2012 AND 2011**

	2012	2011
OTHER OPERATING REVENUES		
Home Health Support	\$ 301,982	\$ 285,006
Business Health	121,492	80,029
Meals Sold	65,289	64,292
Lifeline	46,734	49,871
Specialty Clinic	33,060	34,930
Willow Ridge	4,120	3,822
Miscellaneous	86,295	7,285
Total Other Operating Revenues	\$ 658,972	\$ 525,235

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULES OF OPERATING EXPENSES
YEARS ENDED JUNE 30, 2012 AND 2011**

	Total	
	2012	2011
Medical and Surgical	\$ 869,429	\$ 901,571
Nursery	45,708	46,413
Long-Term Care	717,871	718,453
Operating Room	655,755	646,691
Emergency Room	1,033,512	973,096
Labor and Delivery Room	13,518	11,236
Obstetric Services	236,473	182,263
Anesthesiology	277,402	297,133
Radiology and Ultrasound	803,309	804,572
Laboratory	791,503	751,577
Respiratory Therapy	86,492	77,274
Physical Therapy	268,761	286,227
Occupational Therapy	49,220	47,927
Speech Pathology	18,641	29,959
Electrocardiology	90,782	81,345
Pharmacy	785,190	807,317
Ambulance	328,636	313,702
Home Health	576,451	610,089
Hospice	146,096	116,624
Cardiac Rehab	93,419	87,894
Pulmonary Rehab	22,456	24,146
Specialty Clinic	9,797	14,139
Graettinger Clinic	334,302	341,220
Emmetsburg Clinic	2,901,625	2,778,899
West Bend Clinic	515,308	498,684
Apartments	112,913	111,281
Business Health	126,651	115,781
Diabetic Education	23,945	22,508
Administrative and General	2,449,754	2,377,770
Operation of Plant	614,542	670,742
Housekeeping, Laundry and Linen	253,865	238,909
Dietary	514,647	488,571
Nursing Administration	186,841	225,151
Medical Records	270,976	264,665
Blood	44,745	41,106
Central Supply	288,939	258,451
Employee Benefits	2,799,758	2,441,901
Depreciation Expense	1,863,393	1,934,759
Amortization Expense	253,671	26,939
Interest Expense	487,568	712,818
TOTAL	\$ 21,963,864	\$ 21,379,803

Salaries and Wages		Other	
2012	2011	2012	2011
\$ 784,394	\$ 779,191	\$ 85,035	\$ 122,380
40,004	39,736	5,704	6,677
640,178	640,805	77,693	77,648
478,178	444,519	177,577	202,172
293,511	291,785	740,001	681,311
1,995	3,677	11,523	7,559
224,030	169,743	12,443	12,520
-	-	277,402	297,133
318,404	349,162	484,905	455,410
409,561	401,223	381,942	350,354
33,562	27,755	52,930	49,519
239,347	249,310	29,414	36,917
46,268	42,875	2,952	5,052
-	-	18,641	29,959
6,356	4,526	84,426	76,819
-	-	785,190	807,317
250,063	240,226	78,573	73,476
480,773	468,814	95,678	141,275
95,335	80,601	50,761	36,023
83,861	81,413	9,558	6,481
21,004	19,653	1,452	4,493
8,700	10,575	1,097	3,564
224,377	227,980	109,925	113,240
980,331	925,035	1,921,294	1,853,864
296,261	288,913	219,047	209,771
54,471	53,735	58,442	57,546
91,239	91,526	35,412	24,255
19,479	14,772	4,466	7,736
868,008	792,648	1,581,746	1,585,122
211,041	248,679	403,501	422,063
217,995	202,906	35,870	36,003
326,072	310,229	188,575	178,342
177,045	211,789	9,796	13,362
230,389	222,633	40,587	42,032
939	92	43,806	41,014
17,348	16,914	271,591	241,537
-	-	2,799,758	2,441,901
-	-	1,863,393	1,934,759
-	-	253,671	26,939
-	-	487,568	712,818
<u>\$ 8,170,519</u>	<u>\$ 7,953,440</u>	<u>\$ 13,793,345</u>	<u>\$ 13,426,363</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULES OF PATIENT AND RESIDENT RECEIVABLES,
ALLOWANCE FOR DOUBTFUL ACCOUNTS, AND COLLECTION STATISTICS (UNAUDITED)
YEARS ENDED JUNE 30, 2012 AND 2011**

Analysis of Aging

Age of Accounts (by Date of Discharge)	June 30, 2012		June 30, 2011	
	Amount	Percent	Amount	Percent
30 Days or Less	\$ 2,492,547	60.09 %	\$ 2,822,626	66.07 %
31-60 Days	597,412	14.40 %	490,590	11.48 %
61-90 Days	264,586	6.38 %	204,304	4.78 %
91 Days and Over	793,465	19.13 %	754,842	17.67 %
Total Accounts Receivable	4,148,010	100.00 %	4,272,362	100.00 %
Less: Allowances				
Allowance for Contractual Adjustments	1,303,900		1,109,595	
Allowance for Doubtful Accounts	734,568		715,917	
Net Accounts Receivable	<u>\$ 2,109,542</u>		<u>\$ 2,446,850</u>	

Analysis of Allowance for Doubtful Accounts for the Years Ended June 30, 2012 and 2011:

	2012	2011
Beginning Balance	\$ 715,917	\$ 599,669
Add:		
Provision for Doubtful Accounts	690,457	713,070
Recoveries Previously Written-Off	261,051	468,937
	<u>951,508</u>	<u>1,182,007</u>
Less:		
Accounts Written-Off	<u>(932,857)</u>	<u>(1,065,759)</u>
Ending Balance	<u>\$ 734,568</u>	<u>\$ 715,917</u>

Collection Statistics

	2012	2011
Patient and Resident Receivables, Net	\$ 2,109,542	\$ 2,446,850
Number of Days Charges Outstanding (1)	24	41
Uncollectable Accounts (2)	983,408	995,734
Percentage of Uncollectable Accounts to Total Charges	3.0%	3.1%

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

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

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULES OF SUPPLIES AND PREPAID EXPENSES
JUNE 30, 2012 AND 2011**

Supplies:	<u>2012</u>	<u>2011</u>
Pharmacy	\$ 117,765	\$ 125,237
Central Supply	60,723	43,223
Dietary	7,888	12,110
Other	104,873	121,841
Total Supplies	<u>\$ 291,249</u>	<u>\$ 302,411</u>
 Prepaid Expenses:	 <u>2012</u>	 <u>2011</u>
Dues and Other	<u>\$ 88,229</u>	<u>\$ 117,394</u>

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULES OF COMPARATIVE STATISTICS (UNAUDITED)
JUNE 30, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
Patient Days		
Acute	1,360	1,499
Swing-Bed	885	820
Long-Term Care	7,814	7,728
Nursery	263	246
	<u>10,322</u>	<u>10,293</u>
Admissions		
Acute	415	468
Swing-Bed	97	102
Long-Term Care	11	13
	<u>523</u>	<u>583</u>
Discharges		
Acute	417	468
Swing-Bed	94	102
Long-Term Care	11	13
	<u>522</u>	<u>583</u>
Acute Average Length of Stay	<u>3.70</u>	<u>3.20</u>
Swing-Bed Average Length of Stay	<u>2.40</u>	<u>8.00</u>
Acute Beds	<u>25</u>	<u>25</u>
Long-Term Care Beds	<u>22</u>	<u>22</u>
Percentage of Occupancy:		
Acute and Swing-Bed (Based on 25 Beds)	24.6%	25.4%
Long-Term Care (Based on 22 Beds)	<u>97.3%</u>	<u>96.2%</u>
Outpatient Visits	<u>22,088</u>	<u>22,771</u>
Clinic Visits:		
Graettinger	<u>2,988</u>	<u>2,898</u>
Emmetsburg	<u>22,837</u>	<u>23,678</u>
West Bend	<u>4,534</u>	<u>4,586</u>



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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

Board of Trustees
Palo Alto County Hospital
dba: Palo Alto County Health System
Emmetsburg, Iowa

We have audited the accompanying balance sheet of Palo Alto County Hospital, dba: Palo Alto County Health System (Health System), as of June 30, 2012, and its discretely presented component unit, Palo Alto County Health Care Foundation, as of December 31, 2011, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended and have issued our report thereon dated August 17, 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

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 weaknesses.

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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs listed as items 2012-1 and 2012-2 to be material weaknesses.

Board of Trustees
Palo Alto County Hospital
dba: Palo Alto County Health System

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements of Palo Alto County Hospital, dba: Palo Alto County Health System, 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 noncompliance or other matters that are described in Part II of the accompanying Schedule of Finding and Responses.

Comments involving statutory and other legal matters about the Health System'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 Health System. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

The Health System's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Responses. While we have expressed our conclusions on the Health System's responses, we did not audit the Health System'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 Palo Alto County Hospital, dba: Palo Alto County Health System, and other parties to whom the Health System may report. This report is not intended to be and should not be used by anyone other than these specified parties.



CliftonLarsonAllen LLP

Austin, Minnesota
August 17, 2012

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULE OF FINDINGS AND RESPONSES
YEAR ENDED JUNE 30, 2012**

Part I: Findings Related to the Financial Statements:

Significant Deficiencies:

2012-1 Segregation of Duties

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

Condition: Certain employees perform duties that are incompatible.

Cause: A limited number of office personnel prevents a proper segregation of accounting functions necessary to assure optimal internal control. This is not an unusual condition in organizations of your size.

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

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

Response: Management agrees with the finding and has reviewed the operating procedures of Palo Alto County Hospital dba: Palo Alto County Health System. Due to the limited number of office employees, management will continue to monitor the Health System's operations and procedures. Furthermore, we will continually review the assignment of duties to obtain the maximum internal control possible under the circumstances.

Conclusion: Response accepted.

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
YEAR ENDED JUNE 30, 2012**

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

2012-2 Preparation of Financial Statements

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

Condition: Palo Alto County Hospital dba: Palo Alto County Health System does not have an internal control system designed to provide for the preparation of the financial statements, including the accompanying footnotes and statements of cash flows, as required by GAAP. As auditors, we were requested to draft the financial statements and accompanying notes to the financial statements. The outsourcing of these services is not unusual in an organization of your size.

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

Effect: The effect of this condition is that the year-end financial reporting is prepared by a party outside of the Health System. The outside party does not have the constant contact with ongoing financial transactions that internal staff have. Furthermore, it is possible that new standards may not be adopted and applied timely to the interim financial reporting. It is the responsibility of Health System management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

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

Response: This finding and recommendation is not a result of any change in the Health System's procedures, rather it is due to an auditing standard implemented by the American Institute of Certified Public Accountants. Management feels that committing the resources necessary to remain current on GAAP and GASB reporting requirements and corresponding footnote disclosures would lack benefit in relation to the cost, but will continue evaluating on a going forward basis.

Conclusion: Response accepted

**PALO ALTO COUNTY HOSPITAL
DBA: PALO ALTO COUNTY HEALTH SYSTEM
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
YEAR ENDED JUNE 30, 2012**

Part II: Other Findings Related to Required Statutory Reporting:

II-A-12 **Certified Budget:** Disbursements during the year ended June 30, 2012 exceeded the amounts budgeted in the general government and business type activities functions due to additional expenditures for the early extinguishment of long-term debt. Chapter 384.20 of the Code of Iowa states, in part, "Public monies may not be expended or encumbered except under an annual or continuing appropriation."

Recommendation: The budget should have been amended in accordance with Chapter 384.18 of the Code of Iowa before disbursements were allowed to exceed the budget.

Response: Budgeted expenditures were exceeded in 2012 due to the early extinguishment of outstanding bonds. In the absence of this early extinguishment, the Health System did not exceed expenditures as budgeted. The budget will be amended in the future, if applicable.

Conclusion: Response accepted.

II-B-12 **Questionable Expenditures:** We noted no expenditures that we believe would be in conflict with the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

II-C-12 **Travel Expense:** No expenditures of Health System money for travel expenses of spouses of Health System officials and/or employees were noted.

II-D-12 **Business Transactions:** We noted no material business transactions between the Health System and Health System officials and/or employees.

II-E-12 **Board Minutes:** No transactions were found that we believe should have been approved in the Board minutes but were not.

II-F-12 **Deposits and Investments:** The Health System exceeded limits within its depository resolution at certain times during the year ended June 30, 2012.

Recommendation: It is recommended that the Health System increase its depository resolution limits to not exceed allowable amounts in the future.

Response: Subsequent to year end, the Health System transferred funds from the bank in order to comply with their depository resolution.

Conclusion: Response accepted.

II-G-12 **Publication of Bills Allowed and Salaries:** Chapter 347.13(11) of the Code of Iowa states "There shall be published quarterly in each of the official newspapers of the county as selected by the board of supervisors pursuant to section 349.1 the schedule of bills allowed and there shall be published annually in such newspapers the schedule of salaries paid by job classification and category..." The Health System published a schedule of bills allowed and a schedule of salaries paid as required by the Code of Iowa.