

Grundy County Memorial Hospital
Grundy Center, Iowa

**Basic Financial Statements and
Supplementary Information
June 30, 2012 and 2011**

Together with Independent Auditor's Report

Grundy County Memorial Hospital

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Grundy County Memorial Hospital

Officials
June 30, 2012

<u>Board of Commissioners</u>	<u>Title</u>	<u>Address</u>	<u>Term Expires</u>
Brenda Davis	Chair	Reinbeck, IA	July 2013
Dan Robertson	Vice Chair	Reinbeck, IA	July 2013
Barbara Smith	Secretary	Grundy Center, IA	July 2013
Todd Button	Treasurer	Conrad, IA	July 2014
David Harberts	Member	Dike, IA	July 2014
Dr. Jane Hasek	Member	Reinbeck, IA	July 2012
T.J. Johnsrud	Member	Conrad, IA	July 2014
Joel Meyer	Member	Wellsburg, IA	July 2014
Nancy Olson	Member	Conrad, IA	July 2013
Ron Saak	Member	Grundy Center, IA	July 2012
Mary Schmidt	Member	Grundy Center, IA	July 2013

<u>Hospital Officials</u>	<u>Title</u>
Pamela K. Delagardelle	Chief Executive Officer
Lisa A. Zinkula	Chief Financial Officer

Independent Auditor's Report

To the Board of Commissioners of
Grundy County Memorial Hospital
Grundy Center, Iowa:

We have audited the accompanying balance sheets of Grundy County Memorial Hospital (Hospital), as of and for the years ended June 30, 2012 and 2011 and the related statements of revenue, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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 Grundy County Memorial 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 September 18, 2012 on our consideration of the Hospital's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3-12 and 28 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 audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Hospital's financial statements. The accompanying supplementary information in Exhibits 1-7 and the schedule of expenditures of federal awards, as required by Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* are presented for purposes of additional analysis and are 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, Exhibits 1-7 and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the financial statements as a whole.

SEIM JOHNSON, LLP

Omaha, Nebraska,
September 18, 2012.

Grundy County Memorial Hospital

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

Our discussion and analysis of Grundy County Memorial Hospital's (Hospital's) financial performance provides an overview of the Hospital and its financial activities for the fiscal years ended June 30, 2012, 2011, and 2010. Please read it in conjunction with the Hospital's financial statements, which begin on page 14.

Using This Annual Report

The annual report consists of a series of financial statements and other information, as follows:

- Management's Discussion and Analysis introduces the Hospital and its basic financial statements while providing an analytical overview of the Hospital's financial activities.
- The Hospital's financial statements consist of three statements - Balance Sheets; Statements of Revenue, Expenses, and Changes in Net Assets; and Statements of Cash Flows. These financial statements and related notes provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by contributors, grantors, or enabling legislation.
- Notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

General Information

The Hospital

The Hospital is a 25-bed critical access hospital located in Grundy Center, Iowa. The Hospital also has a 55-bed long-term care unit. Grundy County Memorial Hospital is the only hospital in Grundy County and serves a population base of over 12,000 residents. The Hospital has an operating agreement with Allen Health System of Waterloo, Iowa and is an affiliate of the Iowa Health System.

History

The Hospital was a private hospital operated in a home at 1209 6th Street in Grundy Center from about 1900 to 1905, under the direction of Drs. McAlvin, Thielen and McDowell. After discontinuance as a hospital, the house moved to 708 7th Street for a residence and was razed in 1965.

From 1921 to 1927, Dr. Locke H. Carpenter supplied hospital beds in connection with his office in the Carpenter Building, 617 G Avenue. Dr. Henry L. Mol established hospital facilities in connection with his office over the Corner Drug Store from 1929 to 1935.

Through the efforts of Dr. Mol and community leaders, the present Grundy County Memorial Hospital opened July 1, 1952, at its current location at 201 East J Avenue in Grundy Center as a 38-bed full service facility.

By 1967, the technical facilities were fast becoming obsolete. Moreover, the long term care of elderly people had become a need in the community. Expansion and adjustment of the original space was necessary. A bond issue for \$750,000 to match identical federal funds went before voters of the county. The vote passed, and the design, funding, construction, furnishing, and moving of the technical and administrative spread over nearly two and a half years. When finished, the 89-bed facility contained the most modern supportive amenities. Fifty-five residents could be cared for in the long-term care unit, a number that remains the same today. An open house and formal dedication in 1971 introduced the renovated hospital to the county.

Thirty-five years ago the newly constructed hospital stood alone on the east edge of town. Today, a neighborhood and businesses completely surround the healthcare facility.

Financial and Operations History

From 1983-2000, the Hospital continued to provide care despite struggling with the harsh economics that became part of rural healthcare. In 1993, the County Board of Supervisors believed maintaining a hospital in the county was critical to the medical and economic health of the area. They provided a subsidy and approved a bond referendum to pay the Hospital's debt. The county has continued to subsidize the Hospital since that time.

Grundy County Memorial Hospital

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

A combination of factors helped heal the Hospital's finances. In 2000, Grundy County Memorial Hospital affiliated with Allen Hospital in Waterloo and reduced costs through resource sharing and joint purchasing. The Grundy County Memorial Hospital Board of Commissioners exercises joint authority for financial and long term planning, while Allen provides day-to-day operational management services. In addition, the Medicare Rural Hospital Flexibility Program allowed the Hospital to apply for status as a critical access hospital in order to receive full cost-based reimbursement for Medicare services. As a result, the Hospital began operating in the black, independent of the county subsidy.

With finances stabilized, the Hospital added and enhanced services to meet the most common and critical local needs. In the fall of 2005, a new financial and clinical software package, CPSI, was implemented to improve patient safety, clinical care & documentation, and support Hospital operations. The conversion also included updating and adding hardware throughout the facility.

Modernization Project, Phase I

Prior to the completion of the modernization project in May 2006, the Hospital was built strictly as an inpatient facility and it had completely outgrown its ability to allocate space to outpatient services. The building was in desperate need of updating. The GCMH Board of Commissioners prioritized the most urgent needs of the Hospital and approved a \$6 million modernization plan to maximize efficiency, quality and convenience. The Hospital implemented its plan the spring of 2004 to modernize the physical plant and continue to improve its technology to best serve the future healthcare needs of residents of Grundy County and the surrounding area.

Phase I of the Modernization Project included the following plant improvements:

- **Mechanical systems** replacements and upgrades that totaled \$1.8 million in heating, cooling, air handling and electrical systems
- **Specialty Clinics** with six new exam rooms, two specialty procedure rooms, physician's dictation area and nurses' station
- **Emergency Department** with two emergency bays, a designated trauma/cardiac room and waiting area
- **Outpatient Therapies Department** for growing Physical Therapy, Occupational Therapy, Speech Therapy and Cardiac Rehab programs
- **Ambulatory Surgery** with the addition of pre-admitting and recovery beds and recliners
- **Operating Room** remodeling that included new doors and ventilation systems to decrease infection control risks
- **Radiology Department** with a CT scanner, dexascan, mammography, sonography, and sleep studies equipment
- **Hospital Entry and Parking Area**
- **Healing Garden** adjacent to Long Term Care with cement walkways, a gazebo, a pergola, water fountains and over 1,000 trees, shrubs and perennials.

The Outpatient Therapy area was completed and occupied November 2004. The new addition, including Lab, Radiology, Specialty Clinic and Lobby, was completed June 2005. The Surgery, Recovery Room and Emergency Department remodel was completed April 2006. The parking lot re-pavement, expansion, and new signage were completed the fall of 2006. An Open House and Donor Appreciation Event for the public occurred May 11, 2006.

Modernization Project, Phase II

The GCMH Board of Commissioners approved moving forward with Phase II of the Modernization Project in October of 2008. The Hospital broke ground on the project late spring of 2009. The new addition included the following areas:

Grundy County Memorial Hospital

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

- **Inpatient Area** with 18 new beds; eight medical/surgical, two hospice, one bariatric, one pediatric and six orthopedic rooms; a physical therapy rehabilitation room; and an outpatient services room.
- **Emergency Department** with three private treatment bays and a large trauma room, ambulance garage, and decontamination room.
- **Ambulatory Surgery Unit** with nine private patient bays.

The Hospital Board of Commissioners and the Grundy County Board of Supervisors worked together to optimize the Hospital's borrowing potential by having the County issue general obligation bonds and enter into a loan agreement for these bonds with GCMH. The Emergency Department and Inpatient Area was completed and occupied June 2010. An Open House and Donor Appreciation Event for the public occurred June 9 and 10, 2010.

During FY 2011, the following construction projects were completed:

- **Dry storage & cooler/freezer** opened October 27, 2010
- **Surgery** pre- and post-operative areas opened November 4, 2010
- **Human Resources** area opened November 8, 2010
- **Patient Registration** opened January 13, 2011
- **East J Café** opened February 14, 2011
- **Surgery** clean/sterile area opened March 14, 2011

A Partner for Grundy County

GCMH Associates

The Hospital is a vital part of Grundy County. With a staff of 218, it is one of the county's largest employers. The total annual payroll and benefits for the Hospital reached \$9.6 million for the year ending June 30, 2012.

The growth, expansion and modernization of Grundy County Memorial Hospital has lead to the creation of over 100 jobs since 2003.

The Administrative Team and Hospital Board of Commissioners demonstrate their commitment to Hospital Associates by providing many opportunities for the professional development of their Associates as well as encouraging persons in lower skilled positions to train for higher skill level and professional positions within the organization.

Medical Staff

The Grundy County Memorial Hospital Medical Staff has grown from 22 physicians in 2003 to a total of 149 Providers (8 active and 141 Courtesy). The Medical Staff had 19 new providers apply for Medical Staff privileges during FY 2011-2012 and 11 relinquishments.

Economic Impact

According to Iowa Hospital Association statistics, Grundy County Memorial Hospital has an estimated economic impact of over \$10.1 million for the county each year. If the health sector increases or decreases in size, the medical health of the community, as well as the economic health of the community, are greatly affected. For the attraction of industrial firms, businesses, and retirees, it is crucial that the area have a quality health sector.

Community Partner

The Hospital also strives to be a good community partner. GCMH takes health education classes, health fairs and wellness opportunities out into its market area. GCMH collaborates with area schools to provide athletic trainer services for youth. The Hospital also offers immunization clinics, occupational health services, education and drug-screenings throughout the county, thereby touching many lives.

Grundy County Memorial Hospital

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

As a commitment to the organization's mission of "improving the health of the people in the communities we serve", hospital Associates are actively leading wellness committees in communities and at the county level. Numerous community outreach activities this year have been aimed at raising awareness about healthy living using a "Blue Zones" approach. Hospital leaders helped lead the application and registration process to be selected as an Iowa Blue Zone community. Although not selected in the first round, Associates continue to lead workplace initiatives, and develop and implement community strategies for encouraging healthy behaviors.

The Hospital is committed to addressing anticipated future workforce issues in healthcare. GCMH is actively partnering with area schools, Allen College, and Hawkeye Community College to organize activities for kindergarten through high school students, offer Certified Nursing Assistant (CNA) classes, and collaborate on entry level college classes that foster interest in the pursuit of healthcare careers. Hospital leadership is also participating in a regional task force with four market area high schools (Cedar Valley West) to implement clinical and non-clinical internships at the hospital for the purpose of career exploration. GCMH piloted the program last school year with 11 seniors from Gladbrook-Reinbeck and Grundy Center High Schools interning in Surgery, Inpatient, Lab, Radiology, Therapy Services, Long Term Care, Maintenance, Dietary, Wellness, Marketing, Foundation, Business Office and Long Term Care areas.

The Emergency Department Team has focused on providing continuing education for Emergency Medical Services (EMS) groups in the hospital's market area in 2012.

GCMH Administration and key staff are actively involved in the community-wide health needs assessment, planning and implementation strategies with public health, schools, businesses, community and county officials. The planning sessions focus on updating and resetting the vision for community health.

Vision for the Future

The mission of Grundy County Memorial Hospital, "to improve the health of the people in the communities we serve through healing, caring and teaching" and the vision of the Hospital is, "best outcome, every patient, every time".

The Strategic Initiatives for GCMH for FY 2011 – 2013 are:

- Elevate GCMH's high standards for clinical quality, patient safety, customer service and professionalism.
- Expand and seek greater alignment with the medical staff.
- Build a regional reputation for targeted services and develop new services.
- Partner in the development of a progressive aging retirement community.
- Increase market share and engage service area communities while creating greater support for GCMH.
- Further strengthen the GCMH board, medical staff, and leadership team.
- Improve and sustain financial performance.

Major Strategic Accomplishments for FY 2011-2012

- Awarded \$1.8M Broadband Technology Opportunities Program (BTOP) Grant through the US Dept. of Commerce to install telehealth equipment in hospitals, physician offices, schools, and EMS for the purpose of improving access to healthcare in the rural area
- Worked with Iowa Health Physicians to recruit two family practitioners, Dr. Eric Neverman (who will join the Grundy Family Medicine Clinic in 2015) and Dr. Ryan Arnevik (joining Fall, 2013) and a physician's assistant, Michael Knutsen (joining August, 2012).
- **2011 Press Ganey Summit Award for Patient Satisfaction in Emergency Services**
Presented to a hospital that sustains an overall rank above the 95th percentile for patient satisfaction in Emergency Department databases for three years in a row.
- **2011 IAHS Quality First Award**
Recognized by Iowa Association of Homes and Services for the Aging for significant strides in quality improvement in the areas of falls prevention and medication errors.

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

- **2011 *Modern Healthcare's* Top 100 Best Places to Work in Healthcare Award**
Recognized by *Modern Healthcare* for creating and retaining an engaged healthcare workforce.
- **2011 Cedar Valley Top 20 Employers of Choice Award**
Nominated by GCMH Associates as an Employer of Choice; the hospital was chosen as a 2011 Cedar Valley Top 20 Employer of Choice from over 200 businesses nominated.
- GCMH Board of Commissioners supported a recommendation by the Long Term Care Committee and CEO to remain in the Long Term Care business and continue collaborations with other partners to address the need for continuous care services for the elderly in Grundy Center.
- GCMH Board of Commissioners approved the implementation of Epic, a new electronic health record (EHR) that includes computerized physician order entry (CPOE), in FY2013 to meet meaningful use requirements.

Financial Highlights

- The Hospital's cash and cash equivalents increased \$1,092,788 from 2011 to 2012 due to an increase in cash received from patients and third-party payors due to volume increases. From 2010 to 2011 there was an increase of \$2,588,774.
- The Hospital's increase in net assets was \$907,811, 9.3% from June 30, 2011 to June 30, 2012 and \$2,458,787, 33.8% from June 30, 2010 to June 30, 2011.
- Net patient and service revenue before provision for bad debt increased \$1,298,524, 7.9% from 2011 to 2012 and \$2,754,316, 20.1% from 2010 to 2011.
- Operating expenses increased \$1,372,145, 8.5% from the year ending June 30, 2011 to June 30, 2012 and \$2,731,121, 20.3% from the year ending June 30, 2010 to June 30, 2011.

Financial Statements

The Balance Sheets and Statements of Revenue, Expenses, and Changes in Net Assets

The Balance Sheets and the Statements of Revenue, Expenses, and Changes in Net Assets report information about the Hospital's resources and its activities in a way that helps answer the question of whether the Hospital, as a whole, is better or worse off as a result of the year's activities. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenue and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net assets and changes in them. You can think of the Hospital's net assets - the difference between assets and liabilities - as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the Hospital's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the Hospital.

The Statements of Cash Flows

The Statements of Cash Flows reports cash receipts, cash payments, and net changes in cash and cash equivalents resulting from operations, investing, and financing activities. It shows where cash came from and what the cash was used for. It also provides the change in the cash balance during the reporting period.

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

Changes in the Hospital's Net Assets and Operating Results

The Hospital's Net Assets

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheets on page 14. The Hospital's net assets increased \$907,811, 9.3% from June 30, 2011 to June 30, 2012 and \$2,458,787, 33.8% from June 30, 2010 to June 30, 2011. (Refer to **Table 1**).

Table 1: Assets, Liabilities, and Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Assets:			
Current assets	\$ 8,647,518	7,519,400	5,013,251
Capital assets, net	18,510,448	19,350,160	17,877,376
Other noncurrent assets	1,703,639	1,371,253	3,008,809
Total assets	<u>28,861,605</u>	<u>28,240,813</u>	<u>25,899,436</u>
Liabilities:			
Long-term debt outstanding	14,888,628	15,505,823	16,133,742
Other current and noncurrent liabilities	3,337,337	3,007,161	2,496,652
Total liabilities	<u>18,225,965</u>	<u>18,512,984</u>	<u>18,630,394</u>
Net assets:			
Invested in capital assets, net of related debt	3,621,820	3,919,379	3,427,644
Restricted for debt service	113,002	111,665	109,150
Unrestricted	6,900,818	5,696,785	3,732,248
Total net assets	<u>\$ 10,635,640</u>	<u>9,727,829</u>	<u>7,269,042</u>

Year Ending June 30, 2011 to June 30, 2012:

The Hospital's total assets increased \$620,792. This increase is a result of an increase in cash and cash equivalents \$1,092,788, a decrease of \$839,712 in capital assets, net due to disposals relating to finishing the modernization project and retirement of assets replaced, and an increase in patient and resident receivable of \$162,335, while other noncurrent assets increased as a result of an increase in assets limited as to use or restricted of \$342,779 primarily related to funds available for the modernization project.

Year Ending June 30, 2010 to June 30, 2011:

The Hospital's total assets increased \$2,341,377. This increase is a result of an increase in cash and cash equivalents \$2,588,774, an increase of \$1,472,784 in capital assets, net due to increased costs incurred associated with the modernization project, and an increase in patient and resident receivable of \$707,656, while other noncurrent assets decrease is a result of a decrease in assets limited as to use or restricted of \$2,193,179 primarily related to funds available for the modernization project.

Grundy County Memorial Hospital

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

Operating Results

In 2012, the Hospital's net assets increased by \$907,811, 9.3% while in 2011 the increase was \$2,458,787, 33.8%. (Refer to **Table 2**). These increases include an excess of revenue over expenses before capital grants and contributions of \$268,834 for June 30, 2012, \$303,763 for June 30, 2011, and \$285,412 for June 30, 2010.

Table 2: Condensed Statements of Revenue, Expenses and Changes in Net Assets

	<u>2012</u>	<u>2011</u>	<u>2009</u>
Operating Revenue:			
Net patient service revenue	\$ 17,777,256	16,478,732	13,724,416
Provision for bad debt	(590,012)	(400,786)	(298,600)
Other operating revenue	458,885	263,297	157,187
Total operating revenue	17,646,129	16,341,243	13,583,003
Operating Expenses:			
Salaries and benefits	9,603,944	8,816,239	7,919,268
Purchased services and other	5,129,406	4,783,902	4,154,126
Depreciation and amortization	2,172,594	1,960,417	1,329,217
Interest	682,040	655,281	82,107
Total operating expenses	17,587,984	16,215,839	13,484,718
Operating income	58,145	125,404	98,285
Nonoperating Revenue and Expenses:			
County subsidy	163,000	163,000	150,000
Investment income	43,669	39,330	41,372
Other nonoperating revenue and expenses, net	4,020	(23,971)	(4,245)
Total nonoperating revenue (expenses), net	210,689	178,359	187,127
Excess of revenue over expenses before capital grants and contributions	268,834	303,763	285,412
Capital grants and contributions	638,977	2,155,024	170,336
Increase in net assets	\$ 907,811	2,458,787	455,748

Operating Income

The first component of the overall change in the Hospital's net assets is its operating income - the difference between net patient service revenue and the expenses incurred to perform those services. For the year ending June 30, 2010, the Hospital reported operating income of \$98,285; for the year ending June 30, 2011, the Hospital reported operating income of \$125,404; and for the year ending June 30, 2012, the Hospital reported operating income of \$58,145.

Grundy County Memorial Hospital

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

Year Ending June 30, 2011 to June 30, 2012:

The primary components of the operating income of \$58,145 are:

- Inpatient and swing bed revenue decreased \$130,211, 4.5% from June 30, 2011 to June 30, 2012 due to a decrease in patient days and change in the mix of days which was offset by a room rate increase. Acute days increased 4.2%, Skilled days decreased 21.6%, and Hospitality days increased 512.5% between the years. The Acute and Skilled days were positively impacted by 24 total knee surgeries and 9 total hip surgeries.
- Outpatient revenue increased \$4,028,414, 29.4% from 2011 to 2012. This increase is primarily due to:
 - Emergency Room visits increased from 2,755 visits to 3,414, an increase of 659 visits, 23.9%.
 - Lab procedures increased by 12,309, 15.7% from 2011 to 2012.
 - Operating room revenue increased \$639,947, 39.8% from 2011 to 2012.
 - Radiology revenue increased \$785,415, 30.0% from 2011 to 2012. This increase relates to increases in all of the modalities in Radiology (X-ray, Mammography, CT, MRI, Ultrasound, Dexa, ECG and C-Arm).
 - Therapy visits increase from 6,324 visits to 7,213, an increase of 889 visits, 14.1%.
- Long Term Care revenue increased \$93,982, 3.4%. This increase reflects an increase in days of 27, 1.5% and an increase in rates effective July 1, 2011.
- Increases in salary and benefit costs for the Hospital's Associates of \$743,200, 10.8%. FTEs increased from 138.32 for 2011 to 143.73 for 2011, an increase of 3.9%
- Purchased services and professional fees increased \$209,450, 12.3% from 2011 to 2012. This increase is a result of the use of contracted Emergency Department physicians vs. employed providers.
- Increases in supplies and other expenses of \$419,495, 5.5%. This increase is a result of the increase in outpatient volume and surgical procedures.

Year Ending June 30, 2010 to June 30, 2011:

The primary components of the operating income of \$125,404 are:

- Inpatient and swing bed revenue increased \$1,684,503, 45.8% from June 30, 2010 to June 30, 2011 due to an increase in patient days and a change in the mix of day along with a room rate increase. Acute days increased 18.6%, Skilled days increased 35.4%, and Hospitality days decreased 66.7% between the years. The Acute and Skilled days were positively impacted by 34 total knee surgeries and 9 total hip surgeries.
- Outpatient revenue increased \$2,488,551, 22.2% from 2010 to 2011. This increase is primarily due to:
 - Emergency Room visits increased from 2,403 visits to 2,755, an increase of 352 visits, 14.6%.
 - Lab revenue increased \$114,703, 6.4% from 2010 to 2011, as a result of an increase in rates effective July 1, 2010 to offset rising cost of supplies.
 - Operating room revenue increased \$170,867, 12.1% from 2010 to 2011 due to more complex surgeries being performed.
 - Radiology revenue increased \$606,139, 24.1% from 2010 to 2011. This increase primarily relates to the increased CT, MRI, and C-Arm volume.
 - Cardiac Rehab revenue increased \$65,456, 30.2% from 2010 to 2011.
 - Grundy County Memorial Hospital Orthopedic Hospital Clinic services began September 1, 2010, resulting in revenue of \$789,697.

Grundy County Memorial Hospital

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

- Long Term Care revenue increased \$258,383. This increase reflects an increase in days of 752, 4.3% and an increase in rates effective July 1, 2010.
- Increases in salary and benefit costs for the Hospital's Associates of \$816,637, 13.5%. FTEs increased from 128.27 for 2010 to 138.32 for 2011, an increase of 7.8%
- Purchased services and professional fees increased \$133,912, 8.5% from 2010 to 2011. This increase is a result of the physician fees relating to the opening of the GCMH clinic.
- Increases in supplies and other expenses of \$433,969, 19.8%. This increase is a result of the increase in outpatient volume and surgical procedures (34 total knee, 9 total hip replacements, and 144 cataract surgeries).

Nonoperating Revenue and Expenses

Nonoperating revenue and expenses consist primarily of the county subsidy, investment income, noncapital grants and contributions, and the gain (loss) on disposal of capital assets.

Capital Asset and Debt Administration

Capital Assets

As of June 30, 2012, the Hospital had \$18,510,448 invested in capital assets, net of accumulated depreciation, as detailed in Note 6 to the financial statements. For the year ending June 30, 2012, the Hospital purchased capital assets costing \$1,319,434. Capital asset additions for the year ending June 30, 2011 were \$3,425,165 and for the year ending June 30, 2010 were \$11,326,288.

Capital asset additions for 2012 relates to the purchase of an anesthesia machine, telehealth equipment (cart systems, laptops, etc.), elevator upgrades, FUJI flat panel detector, generator, access control system, steam line upgrade, steamer for Dietary, Surgery instruments, ultrasound machine, LTC dining room, resident room and solarium remodel.

Capital asset additions for 2011 relates to the construction costs associated with the Phase II Modernization Project, parking lot expansion, call light system and technology for the new area, phone system and network equipment & lines associated, an access control system, utensils and equipment for East J Café, shelving units, steam sterilizer, surgical instruments, infusion pumps, cardiac monitoring equipment, coagulation analyzer, dexta machine, telehealth equipment (cameras, televisions, laptops, etc), exterior and interior signage and CPSI server.

Capital asset additions for 2010 relates to the construction costs associated with the Phase II Modernization Project, furniture/equipment (beds, recliners, chairs, pumps, lifts, shelving systems, etc), call light system and technology for the new areas, phone system and network equipment & lines associated, an access control system, general x-ray machine, CT injector, defibrillators, surgical instruments including a colonoscope, hip fracture instruments & total joint instruments, cardiac monitoring equipment, exercise equipment for the new therapy services and cardiac rehab departments, computers, laptops, bar code scanners and servers for various areas of the hospital, along with office furniture.

Debt

On August 26, 2005, the Hospital entered in to a loan agreement with Grundy National Bank of Grundy Center, Iowa for \$650,000 to finance the costs of the acquisition and installation of clinical and financial equipment and software. The Board of Commissioners adopted a resolution approving and authorizing the loan agreement. The Series 2005 Subordinate Hospital Revenue Note is payable solely from the net revenue of the Hospital but is subordinate to the Hospital's obligations to make payment under the Series 2004 Bonds. This loan was paid in full September 2010.

On December 27, 2005, the Hospital entered in to a loan agreement with the Grundy County Rural Electric Cooperative of Grundy Center, Iowa for \$290,000. The Grundy County Rural Electric Cooperative filed an application and supporting material with the Rural Utilities Services requesting the loan for promoting rural economic development. This loan is an interest free loan over ten years. The loan was used to finance the modernization and

Grundy County Memorial Hospital

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

expansion project of the Hospital. The Series 2005, Second Subordinate Hospital Revenue Note is payable solely from the net revenue of the Hospital but is subordinate to the Hospital's obligations to make payment under the Series 2004 Bonds and the Series 2005 Subordinate Hospital Revenue Note. This loan is payable monthly through December 2015.

The Hospital has entered into a construction commitment for the Modernization Project, Phase II. To finance the project, on July 28, 2009, the Hospital entered into a loan agreement with Grundy County, Iowa through an issuance of General Obligation Urban Renewal Notes, Series 2009, in the amount of \$16,020,000. The proceeds of the notes were also used to refund the existing Series 2004 Hospital Revenue Bonds. The Hospital has pledged future net revenues of the Hospital to pay for this loan. Interest is paid semi-annually with a varying rate between 4.25% and 4.75%. The first interest payment was June 2010 and the first principal payment was June 2011.

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 demonstrate the Hospital's accountability. If you have questions about this report or need additional financial information, contact the Hospital Administration Office, at 201 East J Avenue, Grundy Center, IA 50638.

Grundy County Memorial Hospital

Balance Sheets June 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 5,651,455	4,558,667
Assets limited as to use or restricted	113,002	186,707
Receivables -		
Patient and resident, net of allowance for doubtful accounts of \$363,315 in 2012 and \$431,244 in 2011	2,225,808	2,063,473
Succeeding year County subsidy receivable	263,000	263,000
Other	62,645	107,039
Inventories	223,119	225,842
Prepaid expenses	108,489	114,672
	<u>8,647,518</u>	<u>7,519,400</u>
Total current assets	8,647,518	7,519,400
Assets limited as to use or restricted - less amounts required for current obligations	1,600,078	1,257,299
Capital assets, net	18,510,448	19,350,160
Other assets, net	103,561	113,954
	<u>28,861,605</u>	<u>28,240,813</u>
Total assets	\$ 28,861,605	28,240,813
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current maturities of long-term debt	646,250	626,250
Accounts payable -		
Trade	514,901	588,513
Capital related	139,334	299,050
Accrued expenses -		
Accrued salaries, wages and vacation payable	883,830	1,018,691
Payroll taxes	44,529	59,514
Interest	54,888	56,578
Deferred revenue	154,544	147,629
Deferred revenue for succeeding year County subsidy receivable	263,000	263,000
Estimated third-party payor settlements	1,282,311	574,186
	<u>3,983,587</u>	<u>3,633,411</u>
Total current liabilities	3,983,587	3,633,411
Long-term debt, net of unamortized discount and current maturities	14,242,378	14,879,573
	<u>18,225,965</u>	<u>18,512,984</u>
Total liabilities	18,225,965	18,512,984
Net assets:		
Invested in capital assets, net of related debt	3,621,820	3,919,379
Restricted for debt service	113,002	111,665
Unrestricted	6,900,818	5,696,785
	<u>10,635,640</u>	<u>9,727,829</u>
Total net assets	10,635,640	9,727,829
Total liabilities and net assets	\$ 28,861,605	28,240,813

See notes to the financial statements

Grundy County Memorial 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 and resident service revenue before provision for bad debt	\$ 17,777,256	16,478,732
Provision for bad debts	<u>(590,012)</u>	<u>(400,786)</u>
Net patient and resident service revenue	17,187,244	16,077,946
Other operating revenue	<u>458,885</u>	<u>263,297</u>
Total operating revenue	<u>17,646,129</u>	<u>16,341,243</u>
OPERATING EXPENSES:		
Salaries	7,622,476	6,879,276
Employee benefits	1,981,468	1,936,963
Purchased services and professional fees	1,912,131	1,702,681
Utilities	338,682	355,662
Supplies and other expenses	2,767,060	2,624,679
Depreciation and amortization	2,172,594	1,960,417
Insurance	111,533	100,880
Interest	<u>682,040</u>	<u>655,281</u>
Total operating expenses	<u>17,587,984</u>	<u>16,215,839</u>
OPERATING INCOME	<u>58,145</u>	<u>125,404</u>
NONOPERATING REVENUE (EXPENSES), NET:		
Investment income	43,669	39,330
County subsidy	163,000	163,000
Gain (loss) on disposal of capital assets	<u>4,020</u>	<u>(23,971)</u>
Nonoperating revenue, net	<u>210,689</u>	<u>178,359</u>
EXCESS OF REVENUE OVER EXPENSES BEFORE CAPITAL GRANTS AND CONTRIBUTIONS	268,834	303,763
CAPITAL GRANTS AND CONTRIBUTIONS	<u>638,977</u>	<u>2,155,024</u>
INCREASE IN NET ASSETS	907,811	2,458,787
NET ASSETS, Beginning of year	<u>9,727,829</u>	<u>7,269,042</u>
NET ASSETS, End of year	<u>\$ 10,635,640</u>	<u>9,727,829</u>

See notes to financial statements

Grundy County Memorial Hospital

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

	<u>2012</u>	<u>2011</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from patients and third-party payors	\$ 17,739,949	16,314,035
Cash paid for employee salaries and benefits	(9,753,790)	(8,699,955)
Cash paid to suppliers and contractors	(5,194,112)	(4,683,324)
Other receipts and payments, net	<u>503,279</u>	<u>184,423</u>
Net cash provided by operating activities	<u>3,295,326</u>	<u>3,115,179</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
County subsidy received	<u>163,000</u>	<u>163,000</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of capital assets	(1,479,358)	(3,733,490)
Proceeds from sale of capital assets	10,000	--
County subsidy received for capital acquisitions	100,000	100,000
Capital grants and contributions	538,977	2,055,024
Payments on long term debt	(626,250)	(647,477)
Interest paid on debt	<u>(683,730)</u>	<u>(715,138)</u>
Net cash used in capital and related financing activities	<u>(2,140,361)</u>	<u>(2,941,081)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
(Deposits to) withdrawals from assets limited as to use, net	(269,074)	2,193,179
Investment income, net	<u>43,897</u>	<u>58,497</u>
Net cash provided by (used in) investing activities	<u>(225,177)</u>	<u>2,251,676</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,092,788	2,588,774
CASH AND CASH EQUIVALENTS - Beginning of year	<u>4,558,667</u>	<u>1,969,893</u>
CASH AND CASH EQUIVALENTS - End of year	<u>\$ 5,651,455</u>	<u>4,558,667</u>

See notes to financial statements

Grundy County Memorial Hospital

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

	<u>2012</u>	<u>2011</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Operating income	\$ 58,145	125,404
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	2,172,594	1,960,417
Interest expense included in operating expenses	682,040	655,281
(Increase) decrease in current assets -		
Receivables -		
Patients	(162,335)	(707,656)
Other	44,394	(78,874)
Inventories	2,723	19,111
Prepaid expenses	6,183	(96,445)
Estimated third-party payor settlements - Medicare and Medicaid	--	375,000
Increase (decrease) in current liabilities -		
Accounts payable	(73,612)	177,912
Accrued salaries, wages and vacation payable	(134,861)	102,218
Payroll taxes	(14,985)	14,066
Deferred revenue	6,915	(5,441)
Estimated third-party payor settlements - Medicare and Medicaid	708,125	574,186
Net cash provided by operating activities	<u>\$ 3,295,326</u>	<u>3,115,179</u>

See notes to financial statements

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

(1) Organization and Summary of Significant Accounting Policies

The Hospital is a 25-bed public hospital with an attached 55-bed nursing home located in Grundy Center, Iowa, organized under Chapter 37 of the Iowa Code and governed by an 11 member Board of Commissioners elected for alternating terms of three years.

The following is a summary of significant accounting policies of Grundy County Memorial Hospital (Hospital). These policies are in accordance with accounting principles generally accepted in the United States of America.

A. *Reporting Entity*

For financial reporting purposes, Grundy County Memorial Hospital has included all the funds of the Hospital and Nursing Home, specifically all assets, liabilities, revenue and expenses over which the Hospital's governing board exercises oversight responsibility. 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. Grundy County Memorial Hospital has no component units required to be reported in accordance with the Governmental Accounting Standards Board criteria.

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 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.

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 three categories:

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

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

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

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

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

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 are recognized when earned and expenses are recorded when the liability is incurred.

In reporting its financial activity, the Hospital applies all applicable GASB pronouncements for proprietary funds as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

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 include highly liquid investments with an original maturity of three months or less.

G. *Patient and Resident Receivables*

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

Payments of patient and resident receivables are allocated to the specific claim 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 best 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.

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

H. *County Subsidy Receivable*

County subsidy receivable is recognized on the budget approval date, which is the date that the budget is certified by the County Board of Supervisors. The succeeding year county subsidy receivable represents subsidies certified by the Board of Supervisors to be granted in the next fiscal year for the purposes set out in the budget for the next fiscal year. By statute, the Board of Supervisors is required to certify the budget in March of each year for the subsequent fiscal year.

However, by statute, the budget certification for the following fiscal year becomes effective on the first day of that year. Although the succeeding year county subsidy receivable has been recorded, the related revenue is deferred and will not be recognized as revenue until the year for which it is granted.

I. *Assets Limited as to Use or Restricted*

By Board of Commissioners - Periodically, the Hospital's Board of Commissioners 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 Loan Agreement - These funds are used for the payment of principal and interest on the notes and to provide funds for the construction of additions to and remodeling of the existing Hospital facilities.

J. *Capital Assets*

Capital asset acquisitions in excess of \$5,000 are capitalized and recorded at cost. Capital assets donated for Hospital operations are recorded at their estimated fair value at the date of receipt. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method.

Useful lives are determined using guidelines from the American Hospital Association Guide for Estimated Useful Lives of Depreciable Hospital Assets. Lives range by capital asset classification as follows:

Land improvements	10 to 50 years
Buildings and building improvements	10 to 50 years
Equipment, computers, and furniture	3 to 25 years

Gifts of capital assets with explicit restrictions that specify how the assets are to be used and gifts of cash that must be used to acquire capital assets are reported as capital grants and contributions.

K. *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.

L. *Deferred Debt Financing Costs*

Deferred debt financing costs included in other assets on the accompanying balance sheets are being amortized over the life of the related notes using the effective interest method. Amortization expense applicable to these notes amounted to \$19,448 and \$33,977 for the years ended June 30, 2012 and 2011, respectively. These amounts are included in depreciation and amortization expense in the accompanying statements of revenue, expenses and changes in net assets.

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

M. Compensated Absences

Hospital associates accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, death, or retirement. The cost of vacation is recorded as a current liability on the balance sheet. The compensated absences liability has been computed based on rates of pay in effect at June 30, 2012 and 2011.

N. 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 year. 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 year or expected to be collected soon enough thereafter to be used to pay liabilities of the current year. Deferred revenue consists of succeeding year County subsidy receivable and advance billings of nursing home revenue.

O. Statements of Revenue, Expenses and Changes in Net Assets

For purposes of display, transactions deemed by management to be ongoing, major or central to the provision of health care services are reported as operating revenue and expenses. County subsidies granted to finance the current year is included in non-operating revenue and peripheral or incidental transactions are reported as non-operating revenue and expenses.

P. Net Patient and Resident 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. Net 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.

Q. Charity Care

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

R. Grants and Contributions

From time to time, the Hospital receives contributions from Grundy County Memorial Hospital Foundation, as well as grants and 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 or that are restricted to a specific operating purpose are reported as nonoperating revenue. Amounts restricted to capital acquisitions are reported after nonoperating revenue and expenses.

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

S. *Investment Income*

Investment income consists entirely of interest on cash and deposits and is included in nonoperating revenue and expenses.

(2) **Deposits and Investments**

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 Commissioners; 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.

Credit Risk: The Hospital's investments are categorized to give an indication of the level of risk assumed by the Hospital at year end. The Hospital's investments are all category 1 which means that the investments are insured or registered or the securities are held by the Hospital or its agent in the Hospital's name. The Hospital had no investments as defined by Government Accounting Standards Board Statement No. 3 at June 30, 2012 and 2011.

Interest Rate Risk: The Hospital's investment policy allows for the investment of funds with varying maturities as a means of managing its exposure to fair value losses arising from changes in interest rates, so long as the maturities are consistent with the needs and uses of the Hospital's funds.

Investment return, including return on assets limited as to use or restricted, for the years ended June 30, 2012 and 2011 is included in investment income on the statements of revenue, expenses and changes in net assets.

(3) **Net Patient and 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 fiscal intermediary

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. Long-term care services are reimbursed at a prospectively determined rate per day of care. These rates vary accordingly to a patient classification system. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital.

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.

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

Revenue from the Medicare and Medicaid programs accounted for approximately 44% and 11%, respectively, of the Hospital's net patient revenue for the year ended June 30, 2012, and 37% and 9%, respectively, of the Hospital's net patient revenue for the year ended June 30, 2011. 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 2012 and 2011 net patient service revenue increased approximately \$17,000 and \$102,000, respectively, due to removal of allowances that are no longer necessary as a result of final settlements and years that are no longer subject to audits, reviews or investigations.

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

	<u>2012</u>	<u>2011</u>
Gross patient and resident service revenue:		
Hospital -		
Inpatient	\$ 2,752,801	2,883,012
Outpatient	17,714,690	13,686,276
Swingbed	2,134,496	2,484,207
Nursing Home	<u>2,839,154</u>	<u>2,745,172</u>
	25,441,141	21,798,667
Contractual adjustments:		
Medicare	(3,743,366)	(2,689,050)
Medicaid	(545,887)	(381,611)
Other	(3,241,688)	(2,169,871)
Charity care services	<u>(132,944)</u>	<u>(79,403)</u>
Total contractual adjustments	<u>(7,663,885)</u>	<u>(5,319,935)</u>
Net patient and resident service revenue before provision for bad debt	<u>\$ 17,777,256</u>	<u>16,478,732</u>

(4) Assets Limited as to Use or Restricted

By Board

Cash deposits and investments designated by the Board for future capital improvements, as of June 30, 2012 and 2011, are summarized as follows:

	<u>2012</u>	<u>2011</u>
Money market accounts	\$ 860,150	853,538
Certificates of deposit	<u>739,928</u>	<u>403,761</u>
	<u>\$ 1,600,078</u>	<u>1,257,299</u>

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

Under Loan Agreement

In connection with the loan agreement relating to the issuance the General Obligation Urban Renewal Capital Loan Notes, Series 2009, the Hospital is required to maintain the following funds:

Sinking Fund – Established for the monthly deposit by the Hospital of 1/12th of the next annual principal payment and 1/6th of the next semi-annual interest payment.

Project Fund – Established for the deposit of the loan proceeds used to pay for the Facility Modernization Project.

The amounts segregated as of June 30, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Sinking Fund, cash and money market accounts	\$ 113,002	111,665
Project Fund – Cash and money market accounts	--	75,042
	113,002	186,707
Less amounts required for current obligations	<u>(113,002)</u>	<u>(186,707)</u>
	\$ <u> --</u>	<u> --</u>

(5) **Composition of Patient Receivables**

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

	<u>2012</u>	<u>2011</u>
Patient and resident accounts	\$ 3,493,201	3,185,618
Less allowance for doubtful accounts	(363,315)	(431,244)
Less estimated third-party contractual adjustments	<u>(904,078)</u>	<u>(690,901)</u>
	\$ <u>2,225,808</u>	<u>2,063,473</u>

The Hospital grants credits without collateral to its patients and residents, 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	41%	32%
Medicaid	6	5
Commercial insurance	41	49
Patients and residents	<u>12</u>	<u>14</u>
	<u>100%</u>	<u>100%</u>

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

(6) Capital Assets

Capital assets and the related accumulated depreciation for the years ending June 30, 2012 and 2011 is summarized as follows:

	June 30, 2011	Additions	Transfers and Disposals	June 30, 2012
Capital assets, not being depreciated:				
Land	\$ 338,506	39,845	--	378,351
Construction in progress	34,850	132,112	(29,358)	137,604
Total capital assets, not being depreciated	<u>373,356</u>	<u>171,957</u>	<u>(29,358)</u>	<u>515,955</u>
Capital assets, being depreciated:				
Land improvements	183,979	--	--	183,979
Buildings	19,184,740	335,239	6,732	19,526,711
Major moveable equipment, including equipment under capital lease	7,954,415	812,238	(1,349)	8,765,304
Vehicles	15,765	--	--	15,765
Total capital assets, being depreciated	<u>27,338,899</u>	<u>1,147,477</u>	<u>5,383</u>	<u>28,491,759</u>
Less accumulated depreciation:				
Land improvements	105,755	17,498	--	123,253
Buildings	5,272,355	1,191,345	--	6,463,700
Major moveable equipment, including equipment under capital lease	2,968,220	944,303	(17,975)	3,894,548
Vehicles	15,765	--	--	15,765
Total accumulated depreciation	<u>8,362,095</u>	<u>2,153,146</u>	<u>(17,975)</u>	<u>10,497,266</u>
Total capital assets, being depreciated, net	<u>18,976,804</u>	<u>(1,005,669)</u>	<u>23,358</u>	<u>17,994,493</u>
Total capital assets, net	<u>\$ 19,350,160</u>	<u>(833,712)</u>	<u>(6,000)</u>	<u>18,510,448</u>

	June 30, 2010	Additions	Transfers and Disposals	June 30, 2011
Capital assets, not being depreciated:				
Land	\$ 307,587	30,919	--	338,506
Construction in progress	756,679	1,707,258	(2,429,087)	34,850
Total capital assets, not being depreciated	<u>1,064,266</u>	<u>1,738,177</u>	<u>(2,429,087)</u>	<u>373,356</u>
Capital assets, being depreciated:				
Land improvements	189,981	--	(6,002)	183,979
Buildings	16,847,801	--	2,336,939	19,184,740
Major moveable equipment, including equipment under capital lease	6,609,901	1,686,988	(342,474)	7,954,415
Vehicles	15,765	--	--	15,765
Total capital assets, being depreciated	<u>23,663,448</u>	<u>1,686,988</u>	<u>1,988,463</u>	<u>27,338,899</u>
Less accumulated depreciation:				
Land improvements	94,259	17,498	(6,002)	105,755
Buildings	4,239,275	1,109,287	(76,207)	5,272,355
Major moveable equipment, including equipment under capital lease	2,501,039	799,655	(332,474)	2,968,220
Vehicles	15,765	--	--	15,765
Total accumulated depreciation	<u>6,850,338</u>	<u>1,926,440</u>	<u>(414,683)</u>	<u>8,362,095</u>
Total capital assets, being depreciated, net	<u>16,813,110</u>	<u>(239,452)</u>	<u>2,403,146</u>	<u>18,976,804</u>
Total capital assets, net	<u>\$ 17,877,376</u>	<u>1,498,725</u>	<u>(25,941)</u>	<u>19,350,160</u>

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

(7) Long-Term Debt

Long-term debt activity of the Hospital as of and for the years ending June 30, 2012 and 2011 consisted of the following:

	<u>June 30, 2011</u>	<u>Borrowings</u>	<u>Payments / Amortization</u>	<u>June 30, 2012</u>	<u>Due Within One Year</u>
Notes Payable (B)	\$ 160,104	--	(36,250)	123,854	36,250
Urban Renewal Capital Loan Notes (C)	15,445,000	--	(590,000)	14,855,000	610,000
Discount on Urban Renewal Capital Loan Notes (C)	<u>(99,281)</u>	<u>--</u>	<u>9,055</u>	<u>(90,226)</u>	<u>--</u>
Net	<u>\$ 15,505,823</u>	<u>--</u>	<u>(617,195)</u>	<u>14,888,628</u>	<u>646,250</u>

	<u>June 30, 2010</u>	<u>Borrowings</u>	<u>Payments / Amortization</u>	<u>June 30, 2011</u>	<u>Due Within One Year</u>
Subordinate Hospital Revenue Note (A)	\$ 36,227	--	(36,227)	--	--
Notes Payable (B)	196,354	--	(36,250)	160,104	36,250
Urban Renewal Capital Loan Notes (C)	16,020,000	--	(575,000)	15,445,000	590,000
Discount on Urban Renewal Capital Loan Notes (C)	<u>(118,839)</u>	<u>--</u>	<u>19,558</u>	<u>(99,281)</u>	<u>--</u>
Net	<u>\$ 16,133,742</u>	<u>--</u>	<u>(627,919)</u>	<u>15,505,823</u>	<u>626,250</u>

- (A) On August 26, 2005, the Hospital entered into a loan agreement with Grundy National Bank in the amount of \$650,000 to finance the implementation of new clinical and financial software. The Hospital has pledged future net revenues to repay the loan. The loan is payable in monthly installments of \$12,148, including interest at 4.57%. The loan was paid in full on September 1, 2011.
- (B) On December 27, 2005, the Hospital entered into a rural development loan agreement with Grundy County Rural Electric Cooperative in the amount of \$290,000 to provide additional funds for the construction of additions to and remodeling of the existing Hospital facilities. The Hospital has pledged future net revenues to repay the loan. The loan is payable in monthly installments of \$3,021, without interest, beginning December 2007 through December 2015.
- (C) On July 28, 2009, the Hospital entered into a loan agreement with Grundy County, Iowa relating to an issuance of General Obligation Urban Renewal Capital Loan Notes, Series 2009, in the amount of \$16,020,000. The proceeds of the notes, net of discount of \$127,097, were used to refund the existing Series 2004 Hospital Revenue Bonds and provide funds for the construction of additions to and remodeling of the existing Hospital facilities. The Hospital has pledged future net revenues to repay the loan. Interest is paid semi-annually with a varying rate between 4.25% and 4.75%.

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

Annual debt service requirements related to the long-term debt are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 646,250	658,655	1,304,905
2014	661,250	632,730	1,293,980
2015	686,250	606,168	1,292,418
2016	690,104	578,543	1,268,647
2017	700,000	549,855	1,249,855
2018-2022	4,010,000	2,275,400	6,285,400
2023-2027	5,125,000	1,310,180	6,435,180
2028-2030	2,460,000	176,340	2,636,340
	<u>\$ 14,978,854</u>	<u>6,787,871</u>	<u>21,766,725</u>

Under the terms of the Loan Agreement and Hospital Revenue Bonds, the Hospital is required to maintain certain funds which are included in the assets limited as to use or restricted in the accompanying financial statements.

(8) Pension and Retirement Benefits

The Hospital's associates are leased employees of Allen Health System. As a result, the associates participate in Allen Health System's defined contribution pension plan. Participants may make pre-tax contributions from 1% to 20% of eligible salaries. The Hospital contributes 2% of participants' eligible salaries and matches up to 50% of the first 4% of participants' contributions. Effective February 2011, the Hospital matches up to 50% on the first 6% of participants' contributions. Pension plan expense for the years ended June 30, 2012 and 2011 was \$294,690 and \$275,819, respectively.

(9) Operating Subsidy

Effective January 1, 1998, the Hospital entered into an operating agreement with Iowa Health System (Allen Health System). Under this agreement, the Board of Commissioners of Grundy County Memorial Hospital (Hospital Commission) and Allen Health System will jointly exercise certain powers of the Hospital Commission to operate the Hospital and share in the risk and benefits of operation. Included in the statements of revenue, expenses and changes in net assets as a result of this agreement are amounts due to Allen Health System as of June 30, 2012 and 2011 of \$58,145 and \$125,401, respectively.

(10) Commitments under Noncancellable Operating Leases

The Hospital leases certain office space and equipment under noncancellable operating lease agreements. Total lease expense for the years ended June 30, 2012 and 2011 for all operating leases was \$258,679 and \$273,329, respectively.

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

<u>Year Ending June 30,</u>	<u>Amount</u>
2013	\$ 259,756
2014	216,426
2015	202,087
2016	173,247
2017	152,647
2018-2020	457,942

Grundy County Memorial Hospital

Notes to Financial Statements For the Years Ended June 30, 2012 and 2011

(11) Hospital Risk Management

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

The Hospital's leased employees participate in Allen Health System's Self-Funded Health Plan (Plan). The Plan's members include all employees of Allen Health System. The Hospital contributes monthly to the Plan. The Hospital's contributions to the Plan during the years ended June 30, 2012 and 2011 were \$1,141,351 and \$1,104,516, respectively. Stop-loss coverage is provided through a commercial insurance company.

The Hospital also participates in Allen Health System's Self-Funded Worker's Compensation Plan. The Worker's Compensation Plan also has stop-loss coverage through a commercial insurance company.

(12) 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 \$1,000,000 per occurrence and aggregate coverage. These policies provide coverage on a claims-made basis covering only those claims which have occurred and are reported to the insurance company while the coverage is in force. In the event the Hospital should elect not to purchase insurance from the present carrier or the carrier should elect not to renew the policy, any unreported claims which occurred during the policy year may not be recoverable from the carrier.

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.

(13) Foundation

Grundy County Memorial Hospital Foundation (Foundation) was established to raise funds exclusively for the benefit of the Hospital. All funds raised, except funds required for the operations of the Foundation, will be distributed to or be held for the benefit of the Hospital as required to comply with the purposes specified by donors. Management has determined that the economic resources received from or held by the Foundation are not significant to the Hospital. Therefore the Foundation is not reported with the Hospital under GASB Statement 39.

A summary of the Foundation's assets, liabilities and net assets as of June 30, 2012 and 2011 follows:

	<u>(Unaudited)</u>	
	<u>2012</u>	<u>2011</u>
Assets	\$ <u>771,080</u>	<u>759,798</u>
Net assets	\$ <u>771,080</u>	<u>759,798</u>

The Hospital received \$156,760 and \$1,635,285 from the Foundation during the years ended June 30, 2012 and 2011, respectively, for the purchase of property and equipment related to the Hospital's Facility Modernization Project. As of June 30, 2012, the Foundation has approximately \$74,000 of pledges receivable related to the Hospital's Facility Modernization Project.

Grundy County Memorial Hospital

Budgetary Comparison Schedule of Revenue, Expenses and Changes in Net Assets Budget and Actual (Cash Basis) Required Supplementary Information June 30, 2012 and 2011

	<u>Accrual Basis</u>			<u>Budget</u>	<u>Variance Favorable (Unfavorable)</u>
	<u>General</u>	<u>Accrual Adjustments</u>	<u>Cash Basis</u>		
Estimated amount to be raised by taxation	\$ 263,000	--	263,000	263,000	--
Estimated other revenues / receipts	<u>18,232,795</u>	<u>603,307</u>	<u>18,836,102</u>	<u>19,915,710</u>	<u>(1,079,608)</u>
	<u>18,495,795</u>	<u>603,307</u>	<u>19,099,102</u>	<u>20,178,710</u>	<u>(1,079,608)</u>
Expenses / Disbursements	<u>17,587,984</u>	<u>149,256</u>	<u>17,737,240</u>	<u>21,016,200</u>	<u>3,278,960</u>
Net	907,811	454,051	1,361,862	(837,490)	\$ <u>2,199,352</u>
Balance beginning of year	<u>9,727,829</u>	<u>(3,725,156)</u>	<u>6,002,673</u>	<u>6,002,673</u>	
Balance end of year	\$ <u>10,635,640</u>	<u>(3,271,105)</u>	<u>7,364,535</u>	<u>5,165,183</u>	

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

The Board of Commissioners 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 Commissioners 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 did not exceed the amount budgeted.

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

	2012				2011			
	Inpatient	Outpatient	Swing Bed	Total	Inpatient	Outpatient	Swing Bed	Total
NURSING SERVICES:								
Long term care	\$ 2,839,154	--	--	2,839,154	2,745,172	--	--	2,745,172
Swing bed	--	--	1,050,161	1,050,161	--	--	1,215,213	1,215,213
Adult and pediatric	698,643	--	--	698,643	569,155	--	--	569,155
Observation	5,718	137,142	--	142,860	--	79,726	--	79,726
Hospitality	26,141	--	--	26,141	4,232	--	--	4,232
	<u>3,569,656</u>	<u>137,142</u>	<u>1,050,161</u>	<u>4,756,959</u>	<u>3,318,559</u>	<u>79,726</u>	<u>1,215,213</u>	<u>4,613,498</u>
OTHER PROFESSIONAL SERVICES:								
Operating and recovery rooms	847,337	2,249,035	--	3,096,372	1,122,233	1,609,088	--	2,731,321
Radiology	89,605	3,405,709	11,355	3,506,669	66,449	2,620,294	11,171	2,697,914
Laboratory	140,178	2,405,264	98,698	2,644,140	119,438	1,926,970	142,599	2,189,007
Emergency and outpatient service	39,031	4,327,614	991	4,367,636	31,676	2,771,855	2,681	2,806,212
Pharmacy	227,912	1,060,647	353,794	1,642,353	228,359	1,027,219	495,471	1,751,049
Physical therapy	56,119	1,261,130	289,696	1,606,945	56,803	1,058,622	342,196	1,457,621
Anesthesiology	212,215	707,848	--	920,063	229,738	551,862	--	781,600
Mobile services	2,555	629,616	--	632,171	3,080	506,076	1,203	510,359
Occupational therapy	34,931	143,150	184,642	362,723	21,458	190,819	162,508	374,785
Cardiac rehab	--	285,326	385	285,711	547	282,234	--	282,781
Sleep lab	--	289,652	--	289,652	--	242,370	--	242,370
Electrocardiology	6,240	232,290	1,530	240,060	6,081	183,838	2,712	192,631
Respiratory therapy	93,316	11,523	121,890	226,729	75,408	6,080	80,012	161,500
GCMH clinic	269,421	426,593	110	696,124	346,443	443,019	235	789,697
Wound clinic	1,420	104,908	--	106,328	696	123,217	918	124,831
Speech therapy	2,019	19,333	18,046	39,398	1,216	36,576	22,964	60,756
Diabetic education	--	10,355	--	10,355	--	15,316	--	15,316
Ambulance	--	1,412	3,198	4,610	--	485	4,324	4,809
Nutrition education	--	6,105	--	6,105	--	10,117	--	10,117
Central services and supply	--	38	--	38	--	493	--	493
	<u>2,022,299</u>	<u>17,577,548</u>	<u>1,084,335</u>	<u>20,684,182</u>	<u>2,309,625</u>	<u>13,606,550</u>	<u>1,268,994</u>	<u>17,185,169</u>
GROSS PATIENT AND RESIDENT SERVICE REVENUE	\$ 5,591,955	17,714,690	2,134,496	25,441,141	5,628,184	13,686,276	2,484,207	21,798,667
LESS:								
Contractual allowances and other deductions, primarily Medicare and Medicaid				(7,530,941)				(5,240,532)
Provision for bad debts				(590,012)				(400,786)
Charity care services and other discounts, based on charges forgone				(132,944)				(79,403)
NET PATIENT AND RESIDENT SERVICE REVENUE				\$ 17,187,244				\$ 16,077,946

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

	<u>2012</u>	<u>2011</u>
Grants	\$ 263,691	137,772
Cafeteria and vending	107,237	68,088
Clinic rent and other	55,892	41,990
Medical records transcriptions	1,342	1,552
Miscellaneous	<u>30,723</u>	<u>13,895</u>
	<u>\$ 458,885</u>	<u>263,297</u>

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

	2012				2011			
	Salaries and Wages	Professional Fees and Purchased Services	Supplies and Other	Total	Salaries and Wages	Professional Fees and Purchased Services	Supplies and Other	Total
NURSING SERVICES:								
Long term care	\$ 1,265,752	62,315	70,996	1,399,063	1,269,669	27,088	65,232	1,361,989
Adult and pediatric	839,876	24,519	62,985	927,380	476,777	25,550	67,510	569,837
Swing bed	--	604	3,348	3,952	327,907	6,242	4,154	338,303
Hospitality	--	19	--	19	7,158	25	--	7,183
	<u>2,105,628</u>	<u>87,457</u>	<u>137,329</u>	<u>2,330,414</u>	<u>2,081,511</u>	<u>58,905</u>	<u>136,896</u>	<u>2,277,312</u>
OTHER PROFESSIONAL SERVICES:								
Emergency room	1,060,318	296,341	61,540	1,418,199	1,105,359	94,603	54,954	1,254,916
Operating and recovery room	346,730	142,292	688,725	1,177,747	310,089	137,327	820,847	1,268,263
Physical therapy	434,282	1,807	166,293	602,382	392,109	6,241	160,745	559,095
Laboratory	235,669	98,378	237,675	571,722	211,382	102,614	185,653	499,649
Radiology	307,226	115,929	143,938	567,093	266,921	113,530	90,316	470,767
Pharmacy	86,889	53,378	356,121	496,388	77,602	51,347	354,747	483,696
GCMH clinic	57,100	238,126	1,663	296,889	35,174	280,960	2,155	318,289
Anesthesiology	1,388	219,915	5,965	227,268	--	208,053	2,669	210,722
Medical records	69,191	25,547	19,274	114,012	64,014	23,152	18,773	105,939
Cardiac rehab	67,609	2,740	4,217	74,566	56,163	2,740	8,867	67,770
Sleep lab	--	72,930	--	72,930	--	65,315	34	65,349
Central services and supply	62,334	5,772	(3,878)	64,228	59,511	6,415	2,741	68,667
Specialty clinic	39,239	--	2,450	41,689	10,044	--	6,140	16,184
Social services	36,078	--	736	36,814	35,898	--	442	36,340
Senior Life	21,460	--	8,297	29,757	8,123	--	2,889	11,012
Wound clinic	10,984	--	11,795	22,779	9,972	--	16,891	26,863
Speech therapy	--	22,277	--	22,277	--	33,983	117	34,100
Respiratory therapy	--	--	21,519	21,519	--	--	18,501	18,501
Diabetic education	11,874	--	1,688	13,562	14,312	--	2,380	16,692
Electrocardiology	--	10,695	2,349	13,044	--	8,799	2,116	10,915
	<u>2,848,371</u>	<u>1,306,127</u>	<u>1,730,367</u>	<u>5,884,865</u>	<u>2,656,673</u>	<u>1,135,079</u>	<u>1,751,977</u>	<u>5,543,729</u>
GENERAL SERVICES:								
Plant operation and maintenance	253,187	85,217	437,399	775,803	220,476	71,572	427,728	719,776
Dietary	483,379	--	268,162	751,541	404,517	750	232,161	637,428
Housekeeping	179,433	11,360	34,724	225,517	171,832	13,364	37,535	222,731
Laundry and linen	35,782	114,598	18,080	168,460	35,038	105,432	5,362	145,832
	<u>951,781</u>	<u>211,175</u>	<u>758,365</u>	<u>1,921,321</u>	<u>831,863</u>	<u>191,118</u>	<u>702,786</u>	<u>1,725,767</u>
ADMINISTRATIVE SERVICES	<u>1,716,696</u>	<u>307,372</u>	<u>479,681</u>	<u>2,503,749</u>	<u>1,309,229</u>	<u>317,579</u>	<u>388,682</u>	<u>2,015,490</u>
NONDEPARTMENTAL								
Employee benefits	--	--	1,981,468	1,981,468	--	--	1,936,963	1,936,963
Depreciation and amortization	--	--	2,172,594	2,172,594	--	--	1,960,417	1,960,417
Insurance	--	--	111,533	111,533	--	--	100,880	100,880
Interest	--	--	682,040	682,040	--	--	655,281	655,281
	<u>--</u>	<u>--</u>	<u>4,947,635</u>	<u>4,947,635</u>	<u>--</u>	<u>--</u>	<u>4,653,541</u>	<u>4,653,541</u>
\$	<u><u>7,622,476</u></u>	<u><u>1,912,131</u></u>	<u><u>8,053,377</u></u>	<u><u>17,587,984</u></u>	<u><u>6,879,276</u></u>	<u><u>1,702,681</u></u>	<u><u>7,633,882</u></u>	<u><u>16,215,839</u></u>

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

ANALYSIS OF AGING:

Days Since Discharge	<u>2012</u>		<u>2011</u>	
	<u>Amount</u>	<u>Percent of Total</u>	<u>Amount</u>	<u>Percent of Total</u>
0 - 30	\$ 2,152,139	61.61 %	2,051,061	64.37
31 - 60	699,563	20.03	525,520	16.50
61 - 90	206,207	5.90	133,480	4.19
91 - 120	121,537	3.48	105,645	3.32
120 - 180	133,927	3.83	143,881	4.52
> 180	<u>179,828</u>	<u>5.15</u>	<u>226,031</u>	<u>7.10</u>
	3,493,201	100.00 %	3,185,618	100.00
Less:				
Allowance for doubtful accounts	(363,315)		(431,244)	
Allowance for contractual adjustments	<u>(904,078)</u>		<u>(690,901)</u>	
	<u>\$ 2,225,808</u>		<u>\$ 2,063,473</u>	

	<u>2012</u>	<u>2011</u>
NET DAYS REVENUE IN PATIENT ACCOUNTS RECEIVABLE	47.40 days	46.84 days

ALLOWANCE FOR DOUBTFUL ACCOUNTS:

Balance, beginning of year	\$ 431,244	306,941
Provision of uncollectible accounts	590,012	400,786
Recoveries of accounts previously written off	92,175	65,554
Accounts written off	<u>(750,116)</u>	<u>(342,037)</u>
Balance, end of year	<u>\$ 363,315</u>	<u>431,244</u>

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

	<u>2012</u>	<u>2011</u>
INVENTORY:		
Pharmacy	\$ 122,855	128,956
Central supply	40,705	40,401
Laboratory	36,702	36,171
Dietary	19,337	16,647
Radiology	<u>3,520</u>	<u>3,667</u>
	<u>\$ 223,119</u>	<u>225,842</u>
PREPAID EXPENSES:		
Maintenance contracts	\$ 84,513	89,967
Insurance	<u>23,976</u>	<u>24,705</u>
	<u>\$ 108,489</u>	<u>114,672</u>

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

	<u>2012</u>	<u>2011</u>
Patient and Resident Days:		
Hospital -		
Adult and pediatric -		
Medicare	334	273
All other	238	276
Swing bed - skilled	1,444	1,843
Hospitality	<u>95</u>	<u>16</u>
	<u>2,111</u>	<u>2,408</u>
 Nursing Home	 <u>18,567</u>	 <u>18,540</u>
 Discharges:		
Hospital adult and pediatric -		
Medicare	121	94
All other	<u>88</u>	<u>91</u>
	<u>209</u>	<u>185</u>
 Average length of stay:		
Hospital adult and pediatric -		
Medicare	2.76 days	2.90 days
All other	2.70 days	3.03 days
 Observation equivalent days	 132	 84
 Surgical procedures	 717	 551
 Emergency Room visits	 3,414	 2,755
 Full-time equivalents personnel	 143.73	 138.32

Grundy County Memorial Hospital

Schedule of Expenditures of Federal Awards For the Year Ended June 30, 2012

Federal Grantor/Pass Through Agency/Program Title	CFDA Number	Passthrough Identifying Number	Federal Expenditures
US Department of Health and Human Services			
Passed through Iowa Department of Public Health			
Small Rural Hospital Improvement Grant Program	93.301	5881SH28	\$ 7,323
National Bioterrorism Hospital Preparedness Program	93.889	5881BHO07	<u>13,816</u>
Total US Department of Health and Human Services			<u>21,139</u>
US Department of Commerce			
Passed through Central Iowa Hospital Corporation			
Broadband Technologies Opportunities Program (BTOP) - Recovery Act	11.557	19-43-B10575	<u>581,519</u>
Total Federal Awards Expended			<u>\$ 602,658</u>

The accompanying notes are an integral part of this schedule

Notes to the Schedule

Note 1: Basis of Presentation

The schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of the Hospital under programs of the federal government for the year ended June 30, 2012. The information in this Schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the Hospital, it is not intended to and does not present the financial position, changes in net assets or cash flows of the Hospital.

Note 2: Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, where in certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available.

**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 Commissioners of
Grundy County Memorial Hospital
Grundy Center, Iowa:

We have audited the financial statements of Grundy County Memorial Hospital (Hospital) as of and for the year ended June 30, 2012, and have issued our report thereon dated September 18, 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.

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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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 noncompliance 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 were reported to management of the Hospital in a separate letter dated September 18, 2012.

The Hospital'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 Hospital's responses, 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 Grundy County Memorial Hospital and other parties to whom Grundy County Memorial Hospital may report. This report is not intended to and should not be used by anyone other than those specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Grundy County Memorial Hospital during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

SEIM JOHNSON, LLP

Omaha, Nebraska,
September 18, 2012.

**Independent Auditor's Report on Compliance with Requirements
That Could Have A Direct and Material Effect on Each Major Program and
Internal Control Over Compliance in Accordance with OMB Circular A-133**

To the Board of Commissioners of
Grundy County Memorial Hospital
Grundy Center, Iowa:

Compliance

We have audited Grundy County Memorial Hospital's (Hospital) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Hospital's major Federal programs for the year ended June 30, 2012. The Hospital's major Federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major Federal programs is the responsibility of the Hospital's management. Our responsibility is to express an opinion on the Hospital's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major Federal program occurred. An audit includes examining, on a test basis, evidence about the Hospital's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Hospital's compliance with those requirements.

In our opinion, the Hospital complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major Federal programs for the year ended June 30, 2012.

Internal Control Over Compliance

Management of the Hospital is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to Federal programs. In planning and performing our audit, we considered the Hospital's internal control over compliance with requirements that could have a direct and material effect on a major Federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the audit committee, management, Federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

SEIM JOHNSON, LLP

Omaha, Nebraska,
September 18, 2012.

Grundy County Memorial Hospital

Schedule of Findings and Questioned Costs June 30, 2012

Part I: Summary of the Independent Auditor's Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified? _____ Yes x No
- Significant deficiency(ies) identified? _____ Yes x None reported
- Noncompliance material to financial statements noted? _____ Yes x No

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? _____ Yes x No
- Significant deficiency(ies) identified? _____ Yes x None reported

Type of auditor's report issued on compliance for major programs: Unqualified

- Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? _____ Yes x No

Identification of major program:

CFDA Number(s)

11.557

Names of Federal Program or Cluster

Broadband Technology Opportunities Program (BTOP)

Dollar threshold used to distinguish between type A and type B programs

 \$ 300,000

Auditee qualified as low-risk auditee?

_____ Yes x No

Part II: Findings Related to the Financial Statements

INTERNAL CONTROL DEFICIENCIES:

No matters were reported.

INSTANCES OF NON-COMPLIANCE:

No matters were reported.

Grundy County Memorial Hospital

Schedule of Findings and Questioned Costs June 30, 2012

Part III: Other Findings Related to Required Statutory Reporting

- III-A-11 Official Depositories: A resolution naming official depositories has been adopted by the Board. The maximum deposit amounts stated in the resolution were not exceeded during the year ended June 30, 2012.
- III-B-11 Certified Budget: Hospital disbursements during the year ended June 30, 2012 did not exceed budgeted amounts.
- III-C-11 Questionable Expenditures: We noted no expenditures that we believe would be in conflict with the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.
- III-D-11 Travel Expense: No expenditures of Hospital money for travel expenses of spouses of Hospital officials and/or employees were noted.
- III-E-11 Business Transactions: Business transactions between the Hospital officials and/or employees are detailed as follows:

Name, Title, and Business Connection	Transaction Description	Amount
Board Members	Reimbursement of travel expense for attending Iowa Hospital Association and other meetings.	\$ 134
Board Member – President/CEO, Nucara Home Medical Nucara Pharmacy	Medical supplies and equipment rental.	2,942

This does not appear to be a voidable conflict of interest pursuant to Chapter 347.9A(2)(a) of the Code of Iowa.

- III-F-11 Board Minutes: No transactions were found that we believe should have been approved in the Board minutes but were not.
- III-G-11 Deposits and Investments: No instances of non-compliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of the Code of Iowa were noted. The Hospital does not have a formal written investment policy as required by 12B.10B of the Code of Iowa.
- III-H-11 Publication of Bills Allowed and Salaries: Chapter 347.13(14) 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. The Hospital has no employees as all employees are leased from Iowa Health System (Allen Health System), who jointly exercises certain powers of the Hospital commission to operate the Hospital. Therefore, the salaries of Iowa Health System employees were not published.

Grundy County Memorial Hospital

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

Finding	Comment	Corrective Action Plan or Other Explanation
II-A-11	Segregation of duties over internal control over financial reporting.	Management is aware of this deficiency in internal control over financial reporting and believes it is not economically feasible for the Hospital to employ additional personnel for purpose of greater segregation of duties. Management incorporated additional segregation of duties and responsibilities over the financial reporting process and implemented additional compensating controls through oversight review performed by the CEO, CFO and Finance Committee of the Board of Commissioners to mitigate the risk over the financial reporting process. The Hospital will continue to maintain and improve its segregation of duties.

Grundy County Memorial Hospital

Audit Staff
For the Year Ended June 30, 2012

This audit was performed by:

Brian D. Green, FHFMA, CPA, Partner

Darren R. Osten, CPA, Manager

Marc D. Behrens, CPA, Staff Auditor

September 26, 2012

To the Board of Commissioners of
Grundy County Memorial Hospital
Grundy Center, Iowa:

In planning and performing our audit of the financial statements of Grundy County Memorial 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 weakness 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 did not consider to be a material weakness.

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 did not identify any deficiencies in internal control that we consider to be material weaknesses.

The following are descriptions of identified control deficiencies that we determined did not constitute significant deficiencies or material weaknesses:

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 control. 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 the Hospital continue to monitor and improve its segregation of duties.

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.

Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimations 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 following significant estimates made by management:

- Allowance for third-party payor adjustments
- Estimated third-party payor settlements

Management performed an analysis of the estimated collectability of accounts receivable based upon historical collection rates as well as an analysis of the estimated third-party settlements based upon reimbursement and settlements received from third-party payors during the year. As part of our audit procedures, additional tests of the allowance for third-party payor adjustments and estimated third-party settlements were performed which resulted in an audit adjustment. We recommend management continue to monitor and improve its current estimation process to compute an appropriate estimate for an allowance for third-party payor adjustments and settlements.

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:

Recovery Audit Contracts (RAC)

The Medicare Recovery Audit Contractor (RAC) program was established by the *Medicare Modernization Act of 2003*. The program was established as a three year demonstration project in three states as a means to identify Medicare overpayments and underpayments to providers. The *Tax Relief and Health Care Act of 2006* made the RAC program permanent and required the Centers for Medicare & Medicaid Services (CMS) to expand the program nationwide by 2010. RAC program audits began in August 2009 for the State of Iowa.

RAC audits are not performed directly by CMS, but rather by private contractors that are awarded contracts in one of the four CMS designated regions of the United States. Health Data Insights (HDI) is the contractor for the Midwest Region D, which includes Iowa. These private contracts are paid on a contingency fee basis by receiving a percentage of the improper overpayments and underpayments they collect from providers. RAC audits can be automated (claims selection solely based on data from CMS without human review of the medical record) or complex (human review of medical record required to identify discrepancies between the medical record and claim). RAC audits are focused on overpayments to the provider for the following: (1) incorrect payment amounts; (2) non-covered services; (3) incorrectly coded services; and (4) duplicate services. RAC audits are limited in the type of items they are contracted to review, RAC audits cannot review (1) services provided outside of Medicare fee-for-service; (2) cost report settlements; and (3) claims paid dates after October 1, 2007.

Although RAC audits have increased, we have not noted material findings in Iowa. We recommend management continue to stay aware of the ongoing RAC audit activity.

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)*, would increase required disclosures and require a change to the statement of operations. Certain health care entities would 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 would 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 writeoffs, the amount of third-party payor writeoffs, 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.

Accounting for Software Acquisition Costs

In 2012, the Hospital began implementation of an electronic health record system. FASB ASC Topic 350-40, *Internal-Use Software*, provides specific guidance on what types of costs associated with obtaining of computer software are to be capitalized and expensed, depending on the phase of implementation. General guidance on the phases are as follows:

- Preliminary project stage – Decision making process as to which software to obtain – Costs shall be expensed as incurred
- Application development stage – Costs incurred during configuration, installation and testing shall be capitalized. Software purchased to access or convert old system data shall also be capitalized. Training costs and the costs incurred to perform data conversion shall be expensed as incurred

- Post implementation-Operation stage – Training costs and application maintenance costs during this stage shall be expensed as incurred.

We recommend management review FASB ASC Topic 350-40 to ensure costs are appropriately capitalized and expensed based on the type of cost and phase of implementation.

Health Information Technology Incentives

The American Recovery and Reinvestment Act (Recovery Act) of 2009 provides for incentive payments beginning in federal fiscal year 2011 for eligible critical access hospitals (CAH) that are meaningful electronic health record (EHR) users. In July of 2010, the Office of the National Coordinator for Health Information Technology and the Centers for Medicare and Medicaid Services (CMS) issued final rules that define “meaningful use” of electronic medical records and set standards for implementation and certification of EHR technology. The primary impact of the final rules on CAHs is as follows:

- CAH incentive payments for EHR allow for the depreciation costs related to capital EHR costs to be claimed on the Medicare cost report in the year the CAH meets “meaningful use” requirements
- Medicare will pay their share plus 20% for these capital EHR costs (results can’t exceed 100%)
- CAHs with 9-30-2011 fiscal year-ends will be first eligible
- If a CAH has not demonstrated meaningful use by fiscal year 2015 a sliding scale reduction will reduce Medicare payment of reimbursable costs from 101% to 100%
- Established 14 core requirements and 10 menu requirements to achieve meaningful use
- Made CAHs eligible for Medicaid incentives

Additional resources can be found at <http://www.cms.gov/EHRIncentivePrograms/> on the CMS website. We recommend that management develop a strategy and timeframe to achieve meaningful use.

Medicare Reimbursement

As you are aware, the Hospital is designated as a Critical Access Hospital (CAH). Under the CAH designation the Hospital is reimbursed 101% of Medicare allowable costs. The Medicare program determines allowable costs through the filing of an annual Medicare cost report. The Medicare cost report separates departments into the following categories:

- General cost centers (support departments)
- Reimbursable cost centers (routine and ancillary departments)
- Non-reimbursable cost centers (non-hospital departments and services)

Costs included in general cost centers are allocated to the reimbursable and non-reimbursable departments utilizing various statistical methods. The existence and size of the non-reimbursable cost centers directly impacts the allocation of the general service costs to the Medicare reimbursable departments. We encourage management to review these concepts and understand the negative Medicare and Medicaid reimbursement impact caused by allocations to non-reimbursable cost centers.

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.

In July 2011, IASB and FASB announced their intention to re-expose their revised proposals for a common leasing standard in order to allow interest parties an opportunity to comment on the revisions the boards have undertaken since publication of the initial exposure draft.

There currently is no indication of a proposed effective date. 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.

GASB Codification Section 2600

Section 2600 of the Governmental Accounting Standards Board Codification of Governmental Accounting and Financial Reporting Standards establishes financial reporting requirements for state and local governments that have qualifying fundraising foundations. The standard sets forth criteria on which a government is required to provide a discrete presentation that publishes financial information about its own activities as well as those of the affiliated organization. Organizations that meet all of the criteria should be presented discretely as component units. The criteria are:

- The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents.
- The primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization.
- The economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to that primary government.

Management's assessment of Grundy County Memorial Hospital Foundation (Foundation) is that it is not significant to the ongoing operations of the Hospital. Therefore it was not included with the financial statements of the Hospital. We recommend that management continue to evaluate the Hospital's relationship with the Foundation on a regular basis based on the above criteria in order to ensure proper financial reporting.

OMB Circular A-133 Audit Requirements – Proposed Changes

The US Office of Management and Budget (OMB) has issued an Advance Notice of Proposed Guidance titled, *Reform of Federal Policies Relating to Grants and Cooperative Agreements; cost principles and administrative requirements (including Single Audit Act)*. The federal government spends more than \$600 billion annually in the form of grants and cooperative agreements. OMB and the federal agencies have been talking for some time about how grant policies can be reformed to increase the efficiency and effectiveness of federal programs, as well as to eliminate unnecessary and duplicative requirements and focus in on areas that emphasize achieving better outcomes at a lower cost. Improving federal oversight has also been included in the discussion. OMB has issued the Advance Notice to more fully describe the reform ideas it is contemplating so that the public can provide feedback. OMB will consider the feedback received on the Advance Notice and move to the next step—that is, developing proposed revisions to various federal regulations.

The following describes a few of the items impacting single audits in accordance with OMB Circular A-133 that are covered in the Advance Notice:

- **Single Audit Threshold for Audit Increased.** Entities that expend less than \$1,000,000 in federal awards would not be required to undergo a single audit. This would represent an increase from the current threshold for single audits of \$500,000, which was established in 2003.
- **A New Category of Single Audit.** For those entities expending between \$1 million and \$3 million in federal awards, a single audit would be required, but major program audit procedures would be focused on testing only two compliance requirements—that is, allowable and unallowable costs and one additional requirement that would be selected by the federal agency responsible for the program.
- **Changes for Larger Single Audits.** For entities expending more than \$3 million in federal awards, a full single audit would be required. However, the proposal indicates that federal agencies may identify subsets of compliance requirements that they believe most effectively address improper payments, waste, fraud, abuse, and program performance and require additional testing for those requirements.

These proposed revisions could impact the extent of potential audit requirements for the Hospital in future years. We recommend management continue to monitor the amount of Federal awards expended on an annual basis and monitor these proposed revisions as to any changes in audit requirements as the proposed revisions become finalized.

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

Sincerely,

SEIM JOHNSON, LLP



Brian D. Green