

**Waverly Health Center
Waverly, Iowa**

FINANCIAL REPORT

June 30, 2012

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**Waverly Health Center
OFFICIALS
June 30, 2012**

BOARD OF TRUSTEES

Expiration of term

Officers

Susan Vallem, Chair
Roger Johnson, Secretary

December 31, 2012
December 31, 2013

Members

John Johnston
Jill Kwikkel
Jennifer Seward

December 31, 2012
December 31, 2013
December 31, 2012

CHIEF EXECUTIVE OFFICER

Kyle Richards

CHIEF FINANCIAL OFFICER

Lisa Bennett

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Waverly Health Center
Waverly, Iowa

We have audited the accompanying balance sheets of Waverly Health Center, an enterprise fund of the City of Waverly, Iowa, as of June 30, 2012 and 2011, and the related statements of revenues, expenses, and changes in fund equity, and cash flows for the years then ended. These financial statements are the responsibility of the Health Center's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Waverly Health Center as of June 30, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 8, 2012 on our consideration of Waverly Health Center's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 read in conjunction with this report in assessing the results of our audit.

Management's discussion and analysis on pages 5-9 is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.


DENMAN & COMPANY, LLP

West Des Moines, Iowa
October 8, 2012

**Waverly Health Center
MANAGEMENT'S DISCUSSION AND ANALYSIS**

As management of Waverly Health Center, we offer readers of the financial statements this narrative overview and analysis of the Health Center's financial performance during the fiscal years ended June 30, 2012 and 2011. Please read it in conjunction with the Health Center's financial statements, which follow this section.

Overview of the Financial Statements

This annual report includes this management's discussion and analysis report, the independent auditor's report, the basic financial statements of the Health Center, and supplementary information. The financial statements also include notes that explain in more detail some of the information in the financial statements.

Required Financial Statements

The financial statements of the Health Center report information of the Health Center using accounting methods similar to those used by private sector companies. These statements offer short and long-term financial information about its activities. The balance sheet includes all of the Health Center's assets and liabilities and provides information about the nature and amounts of investments in resources, assets, and the obligations to Health Center's creditors, liabilities. It also provides the basis for evaluating the capital structure of the Health Center and assessing the liquidity and financial flexibility of the Health Center.

All of the current year's revenues and expenses are accounted for in the statement of revenues, expenses, and changes in fund equity. This statement measures the success of the Health Center operations over the past year and can be used to determine whether the Health Center has successfully recovered all its costs through its patient service revenue and other revenue sources, profitability and credit worthiness.

The final required financial statement is the statement of cash flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, noncapital financing, capital and related financing and investing activities and provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

Financial Highlights

- Total assets increased by \$1,217,397, or 3%, to \$41,166,752
- Total noncurrent assets whose use is limited decreased by \$205,816 to \$6,010,707
- Total property and equipment decreased by \$1,002,812 to \$22,022,993
- Total fund equity increased by \$3,011,023 to \$27,070,508
- Total long-term debt decreased by \$1,403,362 to \$10,672,005
- Net patient service revenue increased by \$2,909,277, or 7%, to \$44,866,303
- Expenses increased by \$2,811,700, or 6%, to \$46,481,124

Financial Analysis of the Health Center

The balance sheet and the statement of revenues, expenses, and changes in fund equity report the net assets of the Health Center and the changes in them. The Health Center's net assets, the difference between assets and liabilities, are a way to measure financial health or financial position. Over time, sustained increases or decreases in the Health Center's net assets are one indicator of whether its financial health is improving or deteriorating. However, other nonfinancial factors such as changes in economic conditions, population growth and new or changed government legislation should also be considered.

A summary of the Health Center's balance sheets is presented in Table 1.

Table 1
Condensed Balance Sheets

| | June 30 | | |
|---|---------------------|---------------------|---------------------|
| | 2012 | 2011 | 2010 |
| Current assets | \$12,599,442 | \$10,097,443 | \$11,808,649 |
| Noncurrent assets whose use is limited | 6,010,707 | 6,216,523 | 4,877,027 |
| Property and equipment | 22,022,993 | 23,025,805 | 24,288,992 |
| Other assets | <u>533,610</u> | <u>609,584</u> | <u>298,367</u> |
| Total assets | <u>\$41,166,752</u> | <u>\$39,949,355</u> | <u>\$41,273,035</u> |
| Current liabilities | \$ 5,130,549 | \$ 5,626,765 | \$ 5,913,575 |
| Long-term debt, less current maturities | <u>8,965,695</u> | <u>10,263,105</u> | <u>12,075,367</u> |
| Total liabilities | <u>\$14,096,244</u> | <u>\$15,889,870</u> | <u>\$17,988,942</u> |
| Invested in capital assets, net of related debt | \$11,350,988 | \$10,950,438 | \$10,293,978 |
| Restricted | 1,891,049 | 1,950,359 | 1,941,016 |
| Unrestricted | <u>13,828,471</u> | <u>11,158,688</u> | <u>11,049,099</u> |
| Total fund equity | <u>\$27,070,508</u> | <u>\$24,059,485</u> | <u>\$23,284,093</u> |

As depicted in Table 1, total assets increased in fiscal year 2012 to \$41,166,752. The change in total assets results primarily from an increase in cash due to an increase in other operating revenue.

A summary of the Health Center's statements of historical revenues, expenses, and changes in fund equity is presented in Table 2.

Table 2
Condensed Statements of Revenue, Expenses, and Changes in Fund Equity

| | Year ended June 30 | | |
|-----------------------------------|---------------------------|---------------------|---------------------|
| | 2012 | 2011 | 2010 |
| Net patient service revenue | \$44,866,303 | \$41,957,026 | \$38,795,596 |
| Other revenue | 4,611,080 | 2,485,838 | 2,468,849 |
| Total operating revenue | <u>49,477,383</u> | <u>44,442,864</u> | <u>41,264,445</u> |
| Salaries | 22,475,276 | 20,549,908 | 18,366,504 |
| Supplies and expenses | 21,073,602 | 20,153,633 | 18,613,441 |
| Provision for depreciation | 2,932,246 | 2,965,883 | 2,810,121 |
| Total expenses | <u>46,481,124</u> | <u>43,669,424</u> | <u>39,790,066</u> |
| Operating income | <u>2,996,259</u> | <u>773,440</u> | <u>1,474,379</u> |
| Investment income | 130,569 | 134,833 | 137,028 |
| Interest and amortization expense | (670,793) | (755,337) | (841,811) |
| Gain (loss) on disposal of assets | (65,594) | (21,894) | 5,944 |
| Transfer from related foundation | 620,582 | 644,350 | 45,951 |
| Total nonoperating gains (losses) | <u>14,764</u> | <u>1,952</u> | <u>(652,888)</u> |
| Change in fund equity | 3,011,023 | 775,392 | 821,491 |
| Total fund equity, beginning | <u>24,059,485</u> | <u>23,284,093</u> | <u>22,462,602</u> |
| Total fund equity, ending | <u>\$27,070,508</u> | <u>\$24,059,485</u> | <u>\$23,284,093</u> |

Operating and Financial Performance

The following summarizes the Health Center's statement of revenue, expenses and changes in fund equity between June 30, 2012 and 2011.

Net Patient Service Revenue: Net patient service revenue is a product of volume, price increases and payor mix.

Volume: Medical, surgical and obstetrical discharges for fiscal year 2012 were 825 compared to 909 in fiscal year 2011. Average length of stay decreased slightly as patient days decreased to 2,329 from 2,605 in 2011. Volume on the outpatient side indicated significant positive growth in 2012. In 2012, gross outpatient charges increased to \$62,775,308 compared to \$55,400,072 in 2011. Operating and recovery rooms, pharmacy and clinics were the departments with the most significant growth in 2012.

Price Increase: As is customary annually, the Health Center did review its charge structure and incorporated certain price increases in 2012. Overall, gross patient service revenue increased to \$72,066,858 from \$64,032,997 in 2011.

Payor Mix: The Health Center is designated a Critical Access Hospital. As a Critical Access Hospital, most services related to Medicare and Medicaid beneficiaries are paid based on a cost reimbursement methodology. Under this designation, contractual adjustments and bad debts increased to \$27,200,555 in 2012 from \$22,075,971 in 2011. This represents 38% and 34% of gross patient charges for 2012 and 2011, respectively.

A summary of the percentages of gross charges for patient services by payor is presented in Table 3.

Table 3
Payor Mix by Percentage

| | Year ended June 30 | | |
|----------------------|---------------------------|-------------|-------------|
| | 2012 | 2011 | 2010 |
| Medicare | 33% | 34% | 35% |
| Medicaid | 8 | 7 | 7 |
| Commercial insurance | 56 | 54 | 54 |
| Patients | <u>3</u> | <u>5</u> | <u>4</u> |
| Totals | <u>100%</u> | <u>100%</u> | <u>100%</u> |

Other Revenue

Other revenue was \$4,611,080 in 2012 compared to \$2,485,838 in 2011. The increase in other revenue resulted from receipt of electronic health records incentive revenue, in 2012.

Expenses

Approximately 49% of Health Center's expenses are for salaries. Total salaries increased by 9% to \$22,475,276 in 2012 from \$20,549,908 in 2011. The Health Center departments experiencing the most significant increase in 2012 included emergency service and clinics.

Approximately 45% of Health Center's expenses are for supplies and expenses. Total supplies and expenses increased by 5% to \$21,073,602 in 2012 from \$20,153,633 in 2011. The most significant increases related to operating and recovery rooms, administrative services and IPERS.

Approximately 6% of Health Center's expenses relate to provision for depreciation. This provision for depreciation decreased to \$2,932,246 in 2012 from \$2,965,883 in 2011.

Nonoperating Gains (Losses)

Nonoperating gains (losses) increased to \$14,764 in 2012 from \$1,952 in 2011.

Property and Equipment

At the end of 2012, the Health Center had \$22,022,993 invested in property and equipment, net of accumulated depreciation. The Notes to the Financial Statements provide more detail of changes in property and equipment. In 2012, \$2,084,084 was spent to acquire new equipment.

A summary of the Health Center's property and equipment is presented in Table 4.

Table 4
Property and Equipment

| | June 30 | | |
|-------------------------------|---------------------|---------------------|---------------------|
| | 2012 | 2011 | 2010 |
| Land | \$ 2,206,302 | \$ 2,206,302 | \$ 2,156,302 |
| Land improvements | 2,217,135 | 2,165,128 | 2,165,128 |
| Buildings | 6,655,261 | 6,069,921 | 6,069,921 |
| Fixed equipment | 18,379,218 | 17,840,775 | 17,736,540 |
| Major movable equipment | 17,523,748 | 15,845,679 | 15,669,161 |
| Construction in progress | <u>173,821</u> | <u>1,248,665</u> | <u>—</u> |
| Subtotal | 47,155,485 | 45,376,470 | 43,797,052 |
| Less accumulated depreciation | <u>(25,132,492)</u> | <u>(22,350,665)</u> | <u>(19,508,060)</u> |
| Property and equipment | <u>\$22,022,993</u> | <u>\$23,025,805</u> | <u>\$24,288,992</u> |

Construction in progress at June 30, 2012 relates to the construction of a retaining wall and equipment installations in progress.

Debt Administration

At year end, the Health Center had a combined \$9,895,000 in current and long-term debt related to Hospital Revenue Capital Loan Notes, Series 1999, 2003 and 2004. This has decreased by \$1,160,000 in fiscal year 2012, which was the required amount of principal payments on the outstanding Notes. More detailed information about the Health Center's outstanding debt is presented in the Notes to Financial Statements. The Notes represent 70% of the Health Center's total liabilities as of year end.

At year end, the Health Center had \$777,005 in current and long-term notes payable. This has decreased by \$243,362 in fiscal year 2012, which was the required amount of principal payment on the outstanding notes payable for the fiscal year 2012, net of an increase of \$480,300 related to the issuance of new debt. More detailed information about the Health Center's notes payable is presented in the Notes to Financial Statements. The notes payable represent 6% of the Health Center's total liabilities at year end.

Performance Compared to Hospital Budget

The Health Center annually adopts a budget and presents it to the City Council for inclusion in the City's annual budget, which is adopted following required public notice and hearings for all funds. The City's annual budget may be amended during the year utilizing statutorily-prescribed procedures. A comparison of the Health Center's fiscal year 2012 actual results to its adopted budget is presented in Table 5.

**Table 5
Actual vs Budget**

| | <u>Actual results</u> | <u>Adopted budget</u> | <u>Variance</u> |
|-----------------------------|---------------------------|---------------------------|--------------------|
| Total revenue | \$49,477,383 | \$48,896,421 | \$ 580,962 |
| Total expenses | (46,481,124) | (46,824,163) | 343,039 |
| Nonoperating gains (losses) | <u>14,764</u> | <u>(84,488)</u> | <u>99,252</u> |
| Net | <u>\$ 3,011,023</u> | <u>\$ 1,987,770</u> | <u>\$1,023,253</u> |

Actual total revenue was higher than adopted budget primarily due to electronic health records incentive revenue received during the current year. Actual operating expenses were less than adopted budget primarily due to decreased supplies expense.

Economic and Other Factors and Next Year's Budget

The Health Center's board and management considered many factors when setting the fiscal year 2013 budget. Of primary importance are the market forces and environmental factors impacting healthcare such as:

- Medicare and Medicaid reimbursement rates
- Reimbursement rates of other payors
- Cost of supplies
- Facility expansion and growth in demand for services
- Technology advancements

Contacting Waverly Health Center's Management

This financial report is designed to provide users with a general overview of the Health Center's finances and to demonstrate the Health Center's accountability. If you have questions about this report or need additional information, contact Waverly Health Center at (319) 352-4120 or write care of: Chief Financial Officer, Waverly Health Center, 312 Ninth Street SW, Waverly, Iowa 50677.

**Waverly Health Center
BALANCE SHEETS**

| | June 30 | |
|--|-------------------------|-------------------------|
| ASSETS | 2012 | 2011 |
| CURRENT ASSETS | | |
| Cash | \$ 1,801,139 | \$ 460,587 |
| Assets whose use is limited-required for current liabilities | 1,256,706 | 1,206,342 |
| Patient receivables, less allowances for contractual adjustments and bad debts | 7,497,009 | 6,341,491 |
| Other receivables | 211,599 | 306,499 |
| Inventories | 1,496,139 | 1,573,041 |
| Prepaid expenses | 336,850 | 209,483 |
| Total current assets | <u>12,599,442</u> | <u>10,097,443</u> |
| ASSETS WHOSE USE IS LIMITED | | |
| Designated by board for plant replacement and expansion | | |
| Cash | 5,365,278 | 5,463,403 |
| Interest receivable | 11,086 | 9,103 |
| | <u>5,376,364</u> | <u>5,472,506</u> |
| Restricted for payment of long-term debt and interest | | |
| Cash | 146,801 | 233,703 |
| Certificates of deposit | 1,744,248 | 1,716,656 |
| Total assets whose use is limited | <u>7,267,413</u> | <u>7,422,865</u> |
| Less assets whose use is limited and that are required for current liabilities | <u>1,256,706</u> | <u>1,206,342</u> |
| Noncurrent assets whose use is limited | <u>6,010,707</u> | <u>6,216,523</u> |
| PROPERTY AND EQUIPMENT | 47,155,485 | 45,376,470 |
| Less accumulated depreciation | <u>25,132,492</u> | <u>22,350,665</u> |
| Total property and equipment | <u>22,022,993</u> | <u>23,025,805</u> |
| OTHER ASSETS | | |
| Unamortized financing costs | 223,857 | 261,112 |
| Physician practice intangibles | 309,753 | 348,472 |
| Total other assets | <u>533,610</u> | <u>609,584</u> |
| Totals | <u>\$41,166,752</u> | <u>\$39,949,355</u> |

Waverly Health Center
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND EQUITY

| | Year ended June 30 | |
|---|---------------------------|---------------------|
| | 2012 | 2011 |
| NET PATIENT SERVICE REVENUE , net of provision for bad debts 2012 \$1,544,064; 2011 \$1,573,109 | \$44,866,303 | \$41,957,026 |
| OTHER REVENUE | <u>4,611,080</u> | <u>2,485,838</u> |
| Total revenue | <u>49,477,383</u> | <u>44,442,864</u> |
| EXPENSES | | |
| Nursing service | 9,383,409 | 8,657,887 |
| Other professional service | 19,340,756 | 17,774,888 |
| General service | 2,953,853 | 2,951,774 |
| Fiscal and administrative service and unassigned expenses | 11,870,860 | 11,318,992 |
| Provision for depreciation | <u>2,932,246</u> | <u>2,965,883</u> |
| Total expenses | <u>46,481,124</u> | <u>43,669,424</u> |
| Operating income | <u>2,996,259</u> | <u>773,440</u> |
| NONOPERATING GAINS (LOSSES) | | |
| Investment income | 130,569 | 134,833 |
| Interest and amortization expense | (670,793) | (755,337) |
| Loss on disposal of assets | (65,594) | (21,894) |
| Transfer from related foundation | <u>620,582</u> | <u>644,350</u> |
| Total nonoperating gains (losses) | <u>14,764</u> | <u>1,952</u> |
| Change in fund equity | 3,011,023 | 775,392 |
| TOTAL FUND EQUITY | | |
| Beginning | <u>24,059,485</u> | <u>23,284,093</u> |
| Ending | <u>\$27,070,508</u> | <u>\$24,059,485</u> |

**Waverly Health Center
STATEMENTS OF CASH FLOWS**

| | Year ended June 30 | |
|---|---------------------------|---------------------|
| | 2012 | 2011 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Cash received from patients and third-party payors | \$43,410,785 | \$42,916,491 |
| Cash paid to suppliers for goods and services | (21,422,031) | (20,361,766) |
| Cash paid to employees for services | (22,168,040) | (20,867,276) |
| Other operating revenue received | <u>4,611,080</u> | <u>2,485,838</u> |
| Net cash provided by operating activities | <u>4,431,794</u> | <u>4,173,287</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | |
| Transfer from related foundation | <u>620,582</u> | <u>644,350</u> |
| Net cash provided by noncapital financing activities | <u>620,582</u> | <u>644,350</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | |
| Acquisition of property and equipment | (2,084,084) | (1,724,590) |
| Acquisition of physician practice intangibles | - | (387,191) |
| Proceeds from sales of property and equipment | 89,056 | - |
| Interest paid on long-term debt | (599,455) | (683,576) |
| Proceeds from issuance of debt | 480,300 | - |
| Principal payments on long-term debt | <u>(1,883,662)</u> | <u>(1,919,647)</u> |
| Net cash (used in) capital and related financing activities | <u>(3,997,845)</u> | <u>(4,715,004)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Proceeds from maturities of investments | - | 502,363 |
| Interest received | <u>100,994</u> | <u>133,472</u> |
| Net cash provided by investing activities | <u>100,994</u> | <u>635,835</u> |
| NET INCREASE IN CASH | 1,155,525 | 738,468 |
| CASH | | |
| Beginning | <u>6,157,693</u> | <u>5,419,225</u> |
| Ending | <u>\$ 7,313,218</u> | <u>\$ 6,157,693</u> |

See Notes to Financial Statements.

Waverly Health Center
STATEMENTS OF CASH FLOWS (continued)

| | Year ended June 30 | |
|--|---------------------------|--------------------|
| | 2012 | 2011 |
| RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES | | |
| Operating income | \$2,996,259 | \$ 773,440 |
| Adjustments to reconcile operating income to net cash provided by operating activities | | |
| Depreciation | 2,932,246 | 2,965,883 |
| Changes in assets and liabilities | | |
| Patient receivables | (1,155,518) | 759,465 |
| Other receivables | 94,900 | (248,071) |
| Inventories | 76,902 | (17,658) |
| Prepaid expenses | (127,367) | 115,440 |
| Accounts payable | (293,188) | (103,604) |
| Accrued employee compensation | 307,236 | (317,368) |
| Payroll taxes and amounts withheld from employees | (99,676) | 45,760 |
| Estimated third-party payor settlements | <u>(300,000)</u> | <u>200,000</u> |
| Net cash provided by operating activities | <u>\$4,431,794</u> | <u>\$4,173,287</u> |
| RECONCILIATION OF CASH PER STATEMENT OF CASH FLOWS TO THE BALANCE SHEET | | |
| Per balance sheet | | |
| Current assets, cash | \$1,801,139 | \$ 460,587 |
| Assets whose use is limited | | |
| Designated by board for plant replacement and expansion, cash | 5,365,278 | 5,463,403 |
| Restricted for payment of long-term debt and interest, cash | <u>146,801</u> | <u>233,703</u> |
| Total per statement of cash flows | <u>\$7,313,218</u> | <u>\$6,157,693</u> |

See Notes to Financial Statements.

Waverly Health Center
NOTES TO FINANCIAL STATEMENTS

NOTE 1 SIGNIFICANT ACCOUNTING POLICIES

The Health Center is a municipal hospital and is an enterprise fund of the City of Waverly, Iowa, organized under Chapter 392, Code of Iowa, not subject to taxes on income or property. The Health Center is governed by a five member Board of Trustees.

Reporting Entity

For financial reporting purposes, Waverly Health Center has included all funds, organizations, account groups, agencies, boards, commissions and authorities that are not legally separate. The Health Center has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Health Center are such that exclusion would cause the Health Center's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Health Center to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Health Center. These criteria also include organizations that are fiscally dependent on the Health Center. The Waverly Health Center has no component units which meet the Governmental Accounting Standards Board criteria.

Measurement Focus and Basis of Accounting

The Health Center is accounted for on the flow of economic resources measurement focus. The fundamental objective of this focus is to measure whether the Health Center is better or worse off economically as a result of events and transactions of the period.

The financial statements have been prepared in accordance with accounting principles which are applicable to health care proprietary funds of a governmental entity. The Health Center uses the accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded when incurred, even though actual payment or receipt may not occur until after the period ends.

Accounting Standards

The Health Center has elected to apply all applicable Governmental Accounting Standards Board pronouncements.

Inventories

Inventories are stated at cost, based on the first-in, first-out method.

Investments and Investment Income

The Health Center's investments are nonnegotiable certificates of deposit reported at cost.

The nonnegotiable certificates of deposit are nonparticipating contracts not significantly affected by impairment of the issuer's credit standing or other factors.

Investment income is reported as nonoperating gains.

Waverly Health Center
NOTES TO FINANCIAL STATEMENTS

NOTE 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed on the straight-line method. The range of estimated useful lives applied by the Health Center is three to forty years.

Unamortized Financing Costs

Unamortized financing costs are amortized over the life of the issues, using the straight-line method.

Physician Practice Intangibles

Physician practice intangibles, acquired in connection with the purchase of a medical clinic, are being amortized over a ten year period using the straight-line method.

Fund Equity

Fund equity is presented in the following three components:

Invested in capital assets, net of related debt

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

Restricted

Restricted fund equity consists of funds on which constraints have been externally imposed by creditors, such as through debt covenants, grantors, contributors, or laws or regulations of other governments.

Unrestricted

Unrestricted fund equity has no externally imposed restrictions on use.

When the Health Center has both restricted and unrestricted resources available to finance a particular program or project, it is the Health Center's policy to use restricted resources before unrestricted resources.

Charity Care

The Health Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Health Center does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Net Patient Service Revenue

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

**Waverly Health Center
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenues, Expenses and Changes in Fund Equity

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

Credit Policy

The Health Center grants credit to patients, substantially all of whom are residents of the City and surrounding areas.

Accounting Estimates and Assumptions

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

NOTE 2 CASH AND INVESTMENTS

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

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

As to interest rate risk, the Health Center's investment policy limits the investment of operating funds in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days but the maturities shall be consistent with the needs and use of the Health Center.

NOTE 3 PATIENT RECEIVABLES

Patient receivables reported as current assets consisted of amounts from certain payors as follows:

| | Year ended June 30 | |
|---|----------------------------|---------------------------|
| | <u>2012</u> | <u>2011</u> |
| Medicare | \$ 2,706,352 | \$2,420,459 |
| Medicaid | 861,696 | 383,113 |
| Commercial insurance | 3,975,602 | 3,728,086 |
| Patients | 2,770,170 | 2,439,833 |
| Other governmental | <u>118,189</u> | <u>—</u> |
| Total patient receivables | 10,432,009 | 8,971,491 |
| Less allowances for contractual adjustments and bad debts | <u>(2,935,000)</u> | <u>(2,630,000)</u> |
| Net patient receivables | <u>\$ 7,497,009</u> | <u>\$6,341,491</u> |

**Waverly Health Center
NOTES TO FINANCIAL STATEMENTS**

NOTE 4 ASSETS WHOSE USE IS LIMITED

Assets whose use is limited restricted for payment of long-term debt and interest on Hospital Revenue Capital Loan Notes are as follows for the year ended June 30, 2012:

| | <u>Sinking Funds</u> | <u>Debt Reserve Funds</u> | <u>Total</u> |
|------------------------------------|--------------------------|-----------------------------------|--------------------|
| BALANCE , beginning of year | \$ 233,703 | \$1,716,656 | \$1,950,359 |
| Transfer from current assets, cash | 1,623,095 | - | 1,623,095 |
| Interest earned | 6,107 | 27,592 | 33,699 |
| Principal and interest payments | (1,716,104) | - | (1,716,104) |
| BALANCE , end of year | <u>\$ 146,801</u> | <u>\$1,744,248</u> | <u>\$1,891,049</u> |

NOTE 5 PROPERTY AND EQUIPMENT

A summary of property and equipment and related accumulated depreciation follows:

| | <u>June 30, 2012</u> | | <u>June 30, 2011</u> | |
|--------------------------|----------------------|-------------------------------------|----------------------|-------------------------------------|
| | <u>Cost</u> | <u>Accumulated depreciation</u> | <u>Cost</u> | <u>Accumulated depreciation</u> |
| Land | \$ 2,206,302 | \$ - | \$ 2,206,302 | \$ - |
| Land improvements | 2,217,135 | 1,142,247 | 2,165,128 | 1,028,068 |
| Buildings | 6,655,261 | 2,017,179 | 6,069,921 | 1,823,784 |
| Fixed equipment | 18,379,218 | 9,717,801 | 17,840,775 | 8,693,792 |
| Major movable equipment | 17,523,748 | 12,255,265 | 15,845,679 | 10,805,021 |
| Construction in progress | <u>173,821</u> | <u>-</u> | <u>1,248,665</u> | <u>-</u> |
| Totals | <u>\$47,155,485</u> | <u>\$25,132,492</u> | <u>\$45,376,470</u> | <u>\$22,350,665</u> |

A summary of changes in property and equipment for the year ended June 30, 2012 follows:

| | <u>Beginning balance</u> | <u>Additions</u> | <u>Deletions</u> | <u>Transfers</u> | <u>Ending balance</u> |
|-------------------------------|------------------------------|---------------------|-------------------|--------------------|---------------------------|
| Land | \$ 2,206,302 | \$ - | \$ - | \$ - | \$ 2,206,302 |
| Land improvements | 2,165,128 | 52,007 | - | - | 2,217,135 |
| Buildings | 6,069,921 | 113,317 | - | 472,023 | 6,655,261 |
| Fixed equipment | 17,840,775 | 162,701 | - | 375,742 | 18,379,218 |
| Major movable equipment | 15,845,679 | 1,582,238 | 305,069 | 400,900 | 17,523,748 |
| Construction in progress | <u>1,248,665</u> | <u>173,821</u> | <u>-</u> | <u>(1,248,665)</u> | <u>173,821</u> |
| Totals | 45,376,470 | 2,084,084 | 305,069 | - | 47,155,485 |
| Less accumulated depreciation | <u>(22,350,665)</u> | <u>(2,932,246)</u> | <u>(150,419)</u> | <u>-</u> | <u>(25,132,492)</u> |
| Net property and equipment | <u>\$23,025,805</u> | <u>\$ (848,162)</u> | <u>\$ 154,650</u> | <u>\$ -</u> | <u>\$22,022,993</u> |

Construction in progress at June 30, 2012 consists of costs related to construction of a retaining wall and equipment installations in progress.

**Waverly Health Center
NOTES TO FINANCIAL STATEMENTS**

NOTE 5 PROPERTY AND EQUIPMENT (continued)

A summary of changes in property and equipment for the year ended June 30, 2011 follows:

| | <u>Beginning balance</u> | <u>Additions</u> | <u>Deletions</u> | <u>Ending balance</u> |
|-------------------------------|------------------------------|-----------------------|-------------------|---------------------------|
| Land | \$ 2,156,302 | \$ 50,000 | \$ - | \$ 2,206,302 |
| Land improvements | 2,165,128 | - | - | 2,165,128 |
| Buildings | 6,069,921 | - | - | 6,069,921 |
| Fixed equipment | 17,736,540 | 104,235 | - | 17,840,775 |
| Major movable equipment | 15,669,161 | 427,868 | 251,350 | 15,845,679 |
| Construction in progress | - | 1,248,665 | - | 1,248,665 |
| Totals | <u>43,797,052</u> | <u>1,830,768</u> | <u>251,350</u> | <u>45,376,470</u> |
| Less accumulated depreciation | <u>(19,508,060)</u> | <u>(2,965,883)</u> | <u>(123,278)</u> | <u>(22,350,665)</u> |
| Net property and equipment | <u>\$24,288,992</u> | <u>\$ (1,135,115)</u> | <u>\$ 128,072</u> | <u>\$23,025,805</u> |

NOTE 6 LONG-TERM DEBT

Long-term debt is summarized as follows:

| | <u>Year ended June 30</u> | |
|--|---------------------------|---------------------|
| | <u>2012</u> | <u>2011</u> |
| Hospital Revenue Capital Loan Notes, Series 2004 | \$ 4,455,000 | \$ 4,700,000 |
| Hospital Revenue Capital Loan Notes, Series 2003 | 4,945,000 | 5,635,000 |
| Hospital Revenue Capital Loan Notes, Series 1999 | 495,000 | 720,000 |
| Notes payable, equipment | <u>777,005</u> | <u>1,020,367</u> |
| Total | 10,672,005 | 12,075,367 |
| Less current maturities | <u>1,706,310</u> | <u>1,812,262</u> |
| Long-term debt, net of current maturities | <u>\$ 8,965,695</u> | <u>\$10,263,105</u> |

Hospital Revenue Capital Loan Notes, Series 2004

The Health Center issued Hospital Revenue Capital Loan Notes, Series 2004 in the original amount of \$6,200,000. The Notes are payable solely from future revenues of the Health Center and are due serially each June 1 through 2019, at remaining interest rates ranging from 4.2% to 4.85%. At June 30, 2012, the remaining balance on these Notes is \$4,455,000.

The Hospital Revenue Capital Loan Notes, Series 2004 require certain funds be maintained as follows:

A Reserve Fund in an amount equal to the lesser of the maximum annual amount of principal and interest due on all parity obligations in any succeeding fiscal year or 10% of the aggregate original amount, \$521,656.

A Sinking Fund requiring monthly deposits in an amount equal to 1/6 of the next semiannual interest payment and 1/12 of the next annual principal payment. Deposits are to be made from the general funds of the Health Center. Future funding requirements of the Sinking Fund for the next five years total 2013 \$461,734; 2014 \$561,234; 2015 \$620,394; 2016 \$730,384; 2017 \$728,546.

Waverly Health Center
NOTES TO FINANCIAL STATEMENTS

NOTE 6 LONG-TERM DEBT (continued)

Hospital Revenue Capital Loan Notes, Series 2004 (continued)

The amounts set aside as assets whose use is limited for payment of long-term debt and interest meet the requirements of the Notes at June 30, 2012.

The Notes contain a number of covenants regarding the operation of the Health Center, and the Health Center is in substantial compliance with those covenants.

Hospital Revenue Capital Loan Notes, Series 2003

The Health Center issued Hospital Revenue Capital Loan Notes, Series 2003 in the original amount of \$9,800,000. The Notes are payable solely from future revenues of the Health Center and are due serially each June 1 through 2018, at remaining interest rates ranging from 5% to 5.5%. At June 30, 2012, the remaining balance on these Notes is \$4,945,000.

The Hospital Revenue Capital Loan Notes, Series 2003 require certain funds be maintained as follows:

A Reserve Fund in an amount equal to the lesser of the maximum annual amount of principal and interest due on all parity obligations in any succeeding fiscal year or 10% of the aggregate original amount, \$980,000.

A Sinking Fund requiring monthly deposits in an amount equal to 1/6 of the next semiannual interest payment and 1/12 of the next annual principal payment. Deposits are to be made from the general funds of the Health Center. Future funding requirements of the Sinking Fund for the next five years total 2013 \$985,345; 2014 \$984,095; 2015 \$985,335; 2016 \$983,735; 2017 \$984,215.

The amounts set aside as assets whose use is limited for payment of long-term debt and interest meet the requirements of the Notes at June 30, 2012.

The Notes contain a number of covenants regarding the operation of the Health Center, and the Health Center is in substantial compliance with those covenants.

Hospital Revenue Capital Loan Notes, Series 1999

The Health Center issued Hospital Revenue Capital Loan Notes, Series 1999 in the original amount of \$2,150,000. The Notes are payable solely from future revenues of the Health Center and are due serially each June 1 through 2015, at remaining interest rates ranging from 5.7% to 5.8%. At June 30, 2012, the remaining balance on these Notes is \$495,000.

The Hospital Revenue Capital Loan Notes, Series 1999 require certain funds be maintained as follows:

A Reserve Fund in an amount equal to the lesser of the maximum annual amount of principal and interest due on all parity obligations in any succeeding fiscal year or 10% of the aggregate original amount, \$215,000.

A Sinking Fund requiring monthly deposits in an amount equal to 1/6 of the next semiannual interest payment and 1/12 of the next annual principal payment. Deposits are to be made from the general funds of the Health Center. Future funding requirements of the Sinking Fund for the next five years total 2013 \$268,392; 2014 \$169,713; 2015 \$105,800.

The amounts set aside as assets whose use is limited for payment of long-term debt and interest meet the requirements of the Notes at June 30, 2012.

**Waverly Health Center
NOTES TO FINANCIAL STATEMENTS**

NOTE 6 LONG-TERM DEBT (continued)

Hospital Revenue Capital Loan Notes, Series 1999 (continued)

The Notes contain a number of covenants regarding the operation of the Health Center, and the Health Center is in substantial compliance with those covenants.

As to the above Notes, Series 2004, 2003 and 1999, the Health Center has pledged all future revenues, net of certain operating expenses, to repay the principal and interest. The Notes were issued to finance capital improvements of the Health Center. The net revenues are pledged through June, 2019. As of June 30, 2012 the remaining principal and interest on the Series 2004, 2003 and 1999 Notes was \$11,999,984. The following is a comparison of the pledged net revenues and the principal and interest requirements of the Notes for the years ended June 30, 2012 and 2011:

| | <u>Year ended June 30</u> | |
|--|---------------------------|------------------------|
| | <u>2012</u> | <u>2011</u> |
| Change in fund equity | \$3,011,023 | \$ 775,392 |
| Provision for depreciation | 2,932,246 | 2,965,883 |
| Interest expense on the Notes | <u>551,468</u> | <u>602,444</u> |
| Pledged net revenues | <u>\$6,494,737</u> | <u>\$4,343,719</u> |
| Principal and interest requirements | | |
| Hospital Revenue Capital Loan Notes, Series 2004 | \$ 466,534 | \$ 465,346 |
| Hospital Revenue Capital Loan Notes, Series 2003 | 983,465 | 983,165 |
| Hospital Revenue Capital Loan Notes, Series 1999 | <u>266,105</u> | <u>268,145</u> |
| Totals | <u>\$1,716,104</u> | <u>\$1,716,656</u> |

Notes Payable, Equipment

The Health Center has a note agreement to finance the purchase of certain equipment. The note requires monthly payments of \$49,415, including interest at 4.99%, with the final payment due March, 2013. The note is collateralized by the equipment purchased by the Health Center. At June 30, 2012, the remaining balance on this note is \$353,529.

The Health Center has a second note agreement to finance the purchase of certain equipment. The note requires monthly payments of \$2,950, including interest at 4.6%, with the final payment due November, 2012. The note is collateralized by the equipment purchased by the Health Center. At June 30, 2012, the remaining balance on this note is \$11,683.

The Health Center has a third note agreement to finance the purchase of certain equipment. The note requires annual payments of \$45,518, including interest at 3.05%, with the final payment due January, 2014. The note is collateralized by the equipment purchased by the Health Center. At June 30, 2012, the remaining balance on this note is \$87,046.

The Health Center has a fourth note agreement to finance the purchase of certain equipment. The note requires monthly payments of \$8,033, including interest at 4.59%, with the final payment due March, 2016. The note is collateralized by the equipment purchased by the Health Center. At June 30, 2012, the remaining balance on this note is \$324,747.

Waverly Health Center
NOTES TO FINANCIAL STATEMENTS

NOTE 6 LONG-TERM DEBT (continued)

Maturities required on long-term debt are as follows:

| <u>Year ending June 30</u> | <u>Capital Loan Notes</u> | <u>Notes payable</u> | <u>Total principal</u> | <u>Interest</u> | <u>Total</u> |
|--------------------------------|-------------------------------|--------------------------|----------------------------|--------------------|---------------------|
| 2013 | \$1,215,000 | \$ 491,310 | \$ 1,706,310 | \$ 522,594 | \$ 2,228,904 |
| 2014 | 1,275,000 | 131,308 | 1,406,308 | 450,650 | 1,856,958 |
| 2015 | 1,335,000 | 91,215 | 1,426,215 | 381,713 | 1,807,928 |
| 2016 | 1,405,000 | 63,172 | 1,468,172 | 310,212 | 1,778,384 |
| 2017 | 1,475,000 | - | 1,475,000 | 237,761 | 1,712,761 |
| 2018-2019 | <u>3,190,000</u> | <u>-</u> | <u>3,190,000</u> | <u>241,062</u> | <u>3,431,062</u> |
| Total | 9,895,000 | 777,005 | 10,672,005 | 2,143,992 | 12,815,997 |
| Less current maturities | <u>1,215,000</u> | <u>491,310</u> | <u>1,706,310</u> | <u>522,594</u> | <u>2,228,904</u> |
| Total long-term debt | <u>\$8,680,000</u> | <u>\$ 285,695</u> | <u>\$ 8,965,695</u> | <u>\$1,621,398</u> | <u>\$10,587,093</u> |

A summary of changes in long-term debt for the year ended June 30, 2012 follows:

| | <u>Beginning balance</u> | <u>Additions</u> | <u>Principal Payments</u> | <u>Ending balance</u> | <u>Amount due within one year</u> |
|-------------------------------------|------------------------------|-------------------|-------------------------------|---------------------------|---|
| Hospital Revenue Capital Loan Notes | | | | | |
| Series 2004 | \$ 4,700,000 | \$ - | \$ 245,000 | \$ 4,455,000 | \$ 250,000 |
| Series 2003 | 5,635,000 | - | 690,000 | 4,945,000 | 725,000 |
| Series 1999 | 720,000 | - | 225,000 | 495,000 | 240,000 |
| Notes payable | <u>1,020,367</u> | <u>480,300</u> | <u>723,662</u> | <u>777,005</u> | <u>491,310</u> |
| Totals | <u>\$12,075,367</u> | <u>\$ 480,300</u> | <u>\$1,883,662</u> | <u>\$10,672,005</u> | <u>\$1,706,310</u> |

A summary of changes in long-term debt for the year ended June 30, 2011 follows:

| | <u>Beginning balance</u> | <u>Additions</u> | <u>Principal Payments</u> | <u>Ending balance</u> | <u>Amount due within one year</u> |
|-------------------------------------|------------------------------|------------------|-------------------------------|---------------------------|---|
| Hospital Revenue Capital Loan Notes | | | | | |
| Series 2004 | \$ 4,935,000 | \$ - | \$ 235,000 | \$4,700,000 | \$ 245,000 |
| Series 2003 | 6,295,000 | - | 660,000 | 5,635,000 | 690,000 |
| Series 1999 | 935,000 | - | 215,000 | 720,000 | 225,000 |
| Notes payable | <u>1,830,014</u> | <u>-</u> | <u>809,647</u> | <u>1,020,367</u> | <u>652,262</u> |
| Totals | <u>\$13,995,014</u> | <u>\$ -</u> | <u>\$1,919,647</u> | <u>\$12,075,367</u> | <u>\$1,812,262</u> |

**Waverly Health Center
NOTES TO FINANCIAL STATEMENTS**

NOTE 7 NET PATIENT SERVICE REVENUE

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

Medicare and Medicaid

The Health Center is designated a Critical Access Hospital. As a Critical Access Hospital, most services related to Medicare and Medicaid beneficiaries are paid based on a cost reimbursement methodology. The Health Center is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Health Center and audits thereof by the fiscal intermediary. The Health Center's classification of patients under the programs and the appropriateness of their admission are subject to an independent review by peer review organizations. The Health Center's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2010.

Other

The Health Center has payment agreements with Blue Cross, other commercial insurance carriers and health maintenance organizations. The basis for reimbursement under these agreements includes discounts from established charges and prospectively determined rates.

NOTE 8 DEFINED BENEFIT PENSION PLAN

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

For the year ended June 30, 2012, regular plan members were required to contribute 5.38% of their annual salary and the Health Center is required to contribute 8.07% of annual covered payroll. Contribution requirements are established by State statute. The Health Center's contributions to IPERS for the years ended June 30, 2012, 2011 and 2010 were \$1,674,361, \$1,367,075 and \$1,162,155, respectively, equal to the required contributions for each year.

NOTE 9 CHARITY CARE

The Health Center maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy and equivalent service statistics. The following information measures the level of charity care provided during the years ended June 30, 2012 and 2011.

| | 2012 | 2011 |
|---|-------------------|-------------------|
| Charges foregone, based on established rates | \$ <u>289,895</u> | \$ <u>298,685</u> |
| Equivalent percentage of charity care patients to all patients served | <u>.4%</u> | <u>.4%</u> |

Waverly Health Center
NOTES TO FINANCIAL STATEMENTS

NOTE 10 MALPRACTICE CLAIMS

The Health Center is insured by a claims-made policy for protection against liability claims resulting from professional services provided or which should have been provided. Coverage limits are \$1,000,000 per claim and \$3,000,000 in the aggregate.

The Health Center is from time to time subject to claims and suits alleging malpractice. In the opinion of management, the ultimate cost, if any, related to the resolution of such pending legal proceedings will be within the limits of insurance coverage and, accordingly, will not have a significant impact on the financial position or the results of operations of the Health Center.

Incidents occurring through June 30, 2012 may result in the assertion of claims. Management is unable to estimate the ultimate cost, if any, of the resolution of such potential claims and, accordingly, no accrual has been made for them, however, management believes that these claims, if asserted, would be settled within the limits of insurance coverage.

NOTE 11 RISK MANAGEMENT

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

INDEPENDENT AUDITOR'S REPORT ON THE SUPPLEMENTARY INFORMATION

Board of Trustees
Waverly Health Center
Waverly, Iowa

We have audited the financial statements of Waverly Health Center as of and for the periods ended June 30, 2012 and 2011, and our report thereon dated October 8, 2012, which expressed an unqualified opinion on those financial statements, appears on page 4. Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Denman & Company, LLP
DENMAN & COMPANY, LLP

West Des Moines, Iowa
October 8, 2012

**Waverly Health Center
ANALYSIS OF PATIENT RECEIVABLES**

| <u>Age of accounts (by date of discharge)</u> | <u>Amounts</u> | | <u>Percent to total</u> | |
|--|---------------------|--------------------|-------------------------|----------------|
| | <u>June 30</u> | | <u>June 30</u> | |
| | <u>2012</u> | <u>2011</u> | <u>2012</u> | <u>2011</u> |
| 0 - 30 days (includes patients in Health Center at end of year) | \$ 5,873,321 | \$4,949,123 | 56.30% | 55.16% |
| 31 - 60 days | 1,741,329 | 1,402,424 | 16.69 | 15.63 |
| 61 - 90 days | 715,013 | 661,177 | 6.85 | 7.37 |
| 91 - 120 days | 465,011 | 406,159 | 4.46 | 4.53 |
| 121 - 365 days | 1,462,663 | 1,172,765 | 14.02 | 13.07 |
| Over one year | <u>174,672</u> | <u>379,843</u> | <u>1.68</u> | <u>4.24</u> |
| Totals | <u>10,432,009</u> | <u>8,971,491</u> | <u>100.00%</u> | <u>100.00%</u> |
| Allowances | | | | |
| Contractual | | | | |
| Medicare | 870,000 | 770,000 | | |
| Medicaid | 320,000 | 150,000 | | |
| Other | 1,070,000 | 960,000 | | |
| Bad debts | <u>675,000</u> | <u>750,000</u> | | |
| Total allowances | <u>2,935,000</u> | <u>2,630,000</u> | | |
| Totals | <u>\$ 7,497,009</u> | <u>\$6,341,491</u> | | |
| NET PATIENT SERVICE REVENUE PER CALENDAR DAY | <u>\$ 122,586</u> | <u>\$ 114,951</u> | | |
| NUMBER OF DAYS NET PATIENT SERVICE REVENUE IN NET PATIENT RECEIVABLES | <u>61</u> | <u>55</u> | | |

ANALYSIS OF ALLOWANCE FOR BAD DEBTS

| | <u>Amounts</u> | | <u>Percent of net patient service revenue</u> | |
|---|---------------------------|-------------------|---|-------------|
| | <u>Year ended June 30</u> | | <u>Year ended June 30</u> | |
| | <u>2012</u> | <u>2011</u> | <u>2012</u> | <u>2011</u> |
| BALANCE , beginning | \$ 750,000 | \$ 700,000 | | |
| ADD | | | | |
| Provision for bad debts | 1,544,064 | 1,573,109 | 3.44% | 3.75% |
| Recoveries of accounts previously written off | <u>444,702</u> | <u>464,207</u> | 0.99 | 1.11 |
| | 2,738,766 | 2,737,316 | | |
| DEDUCT | | | | |
| Accounts written off | <u>2,063,766</u> | <u>1,987,316</u> | 4.60 | 4.74 |
| BALANCE , ending | <u>\$ 675,000</u> | <u>\$ 750,000</u> | | |

Waverly Health Center
PATIENT SERVICE REVENUE
Year ended June 30, 2012, with comparative totals for 2011

| | <u>2012</u> | | | <u>2011</u> |
|---|--------------------|---------------------|---------------------|---------------------|
| | <u>Inpatient</u> | <u>Outpatient</u> | <u>Total</u> | <u>Total</u> |
| DAILY PATIENT SERVICES | | | | |
| Medical, surgical and obstetrical | \$2,582,902 | \$ 991,180 | \$ 3,574,082 | \$ 3,839,276 |
| Swing bed | 563,680 | - | 563,680 | 507,744 |
| Nursery | 593,171 | - | 593,171 | 558,986 |
| | <u>3,739,753</u> | <u>991,180</u> | <u>4,730,933</u> | <u>4,906,006</u> |
| OTHER NURSING SERVICES | | | | |
| Medical services | - | 654,586 | 654,586 | 625,279 |
| Operating and recovery rooms | 2,128,831 | 10,791,898 | 12,920,729 | 9,961,884 |
| Delivery and labor rooms | 426,648 | 7,540 | 434,188 | 334,585 |
| Emergency service | 35,721 | 5,883,904 | 5,919,625 | 6,018,237 |
| Ambulance | 12,719 | 1,792,270 | 1,804,989 | 1,685,354 |
| Hospice | 79,515 | - | 79,515 | 102,473 |
| | <u>2,683,434</u> | <u>19,130,198</u> | <u>21,813,632</u> | <u>18,727,812</u> |
| OTHER PROFESSIONAL SERVICES | | | | |
| Laboratory | 780,451 | 6,738,089 | 7,518,540 | 6,666,809 |
| Radiology | 305,796 | 11,972,438 | 12,278,234 | 10,891,826 |
| Pharmacy | 1,091,984 | 3,173,114 | 4,265,098 | 4,096,609 |
| Anesthesiology | 106,351 | 1,701,558 | 1,807,909 | 1,483,767 |
| Respiratory therapy and electrocardiology | 332,870 | 2,421,521 | 2,754,391 | 2,427,704 |
| Cardiac rehabilitation | - | 335,523 | 335,523 | 268,200 |
| Physical therapy | 348,352 | 3,781,462 | 4,129,814 | 3,830,512 |
| Speech therapy | 18,666 | 74,733 | 93,399 | 82,505 |
| Occupational therapy | 173,788 | 222,562 | 396,350 | 332,534 |
| Clinics | - | 12,080,118 | 12,080,118 | 10,476,371 |
| Medical spa | - | 152,812 | 152,812 | 141,027 |
| | <u>3,158,258</u> | <u>42,653,930</u> | <u>45,812,188</u> | <u>40,697,864</u> |
| Totals | <u>\$9,581,445</u> | <u>\$62,775,308</u> | 72,356,753 | 64,331,682 |
| Charity care charges foregone, based on established rates | | | (289,895) | (298,685) |
| Total gross patient service revenue | | | 72,066,858 | 64,032,997 |
| Provisions for contractual adjustments and bad debts | | | (27,200,555) | (22,075,971) |
| Total net patient service revenue | | | <u>\$44,866,303</u> | <u>\$41,957,026</u> |

Waverly Health Center
PROVISIONS FOR CONTRACTUAL ADJUSTMENTS AND BAD DEBTS

| | <u>Year ended June 30</u> | |
|-------------------------|---------------------------|-------------------------|
| | <u>2012</u> | <u>2011</u> |
| Contractual adjustments | | |
| Medicare | \$ 9,057,903 | \$ 7,155,135 |
| Medicaid | 2,284,998 | 1,468,479 |
| Other adjustments | 14,313,590 | 11,879,248 |
| Provision for bad debts | <u>1,544,064</u> | <u>1,573,109</u> |
| Totals | <u>\$27,200,555</u> | <u>\$22,075,971</u> |

OTHER REVENUE

| | <u>Year ended June 30</u> | |
|---|---------------------------|------------------------|
| | <u>2012</u> | <u>2011</u> |
| Electronic health records incentive revenue | \$2,121,691 | \$ — |
| Cafeteria | 167,985 | 165,334 |
| Wellness | 11,266 | 9,816 |
| Retail pharmacy | 1,830,508 | 1,907,036 |
| Rental income | 48,620 | 45,271 |
| Miscellaneous | <u>431,010</u> | <u>358,381</u> |
| Totals | <u>\$4,611,080</u> | <u>\$2,485,838</u> |

Waverly Health Center
EXPENSES
Year ended June 30, 2012, with comparative totals for 2011

| | <u>2012</u> | | | <u>2011</u> |
|---|-------------------|------------------|-------------------|-------------------|
| | <u>Salaries</u> | <u>Other</u> | <u>Total</u> | <u>Total</u> |
| NURSING SERVICE | | | | |
| Nursing administration | \$ 367,463 | \$ 50,219 | \$ 417,682 | \$ 444,143 |
| Medical, surgical and obstetrical | 1,849,228 | 293,566 | 2,142,794 | 2,165,218 |
| Nursery | 310,113 | 1,172 | 311,285 | 270,441 |
| Observation | 205,159 | 13,906 | 219,065 | 168,757 |
| Operating and recovery rooms | 1,003,414 | 2,042,797 | 3,046,211 | 2,666,855 |
| Delivery and labor rooms | 85,642 | 4,066 | 89,708 | 86,999 |
| Central supply | - | 24,311 | 24,311 | 9,370 |
| Emergency service | 2,298,903 | 156,499 | 2,455,402 | 2,164,525 |
| Ambulance | 594,436 | 45,736 | 640,172 | 633,478 |
| Hospice | 36,779 | - | 36,779 | 48,101 |
| Total nursing service | <u>6,751,137</u> | <u>2,632,272</u> | <u>9,383,409</u> | <u>8,657,887</u> |
| OTHER PROFESSIONAL SERVICE | | | | |
| Laboratory | 843,367 | 1,317,447 | 2,160,814 | 2,165,422 |
| Radiology | 861,371 | 604,124 | 1,465,495 | 1,479,536 |
| Pharmacy | 493,348 | 1,052,513 | 1,545,861 | 1,531,416 |
| Retail pharmacy | 305,983 | 1,447,308 | 1,753,291 | 1,802,695 |
| Anesthesiology | 693,359 | 94,708 | 788,067 | 715,564 |
| Respiratory therapy and electrocardiology | 404,000 | 288,874 | 692,874 | 664,086 |
| Cardiac rehabilitation | 131,504 | 18,828 | 150,332 | 144,185 |
| Physical therapy | - | 2,098,859 | 2,098,859 | 1,856,295 |
| Speech therapy | 63,842 | 2,587 | 66,429 | 70,615 |
| Occupational therapy | - | 289,663 | 289,663 | 286,580 |
| Integrative therapy | 52,451 | 332 | 52,783 | - |
| Occupational health | 13,098 | 5,468 | 18,566 | 24,140 |
| Clinics | 5,977,723 | 1,516,723 | 7,494,446 | 6,252,611 |
| Medical spa | 63,598 | 59,039 | 122,637 | 131,722 |
| Health information management | 529,024 | 40,679 | 569,703 | 566,550 |
| Social services | 68,514 | 2,422 | 70,936 | 83,471 |
| Total other professional service | <u>10,501,182</u> | <u>8,839,574</u> | <u>19,340,756</u> | <u>17,774,888</u> |
| GENERAL SERVICE | | | | |
| Nutrition services | 521,643 | 212,604 | 734,247 | 720,852 |
| Plant services | 410,973 | 961,449 | 1,372,422 | 1,399,931 |
| Environmental services | 598,084 | 137,942 | 736,026 | 727,035 |
| Laundry | 66,763 | 44,395 | 111,158 | 103,956 |
| Total general service | <u>1,597,463</u> | <u>1,356,390</u> | <u>2,953,853</u> | <u>2,951,774</u> |
| FISCAL AND AMINISTRATIVE SERVICE | | | | |
| Administrative services | 1,203,365 | 850,840 | 2,054,205 | 2,363,626 |
| Fiscal services | 170,423 | 6,008 | 176,431 | 174,820 |
| Human resources | 205,883 | 70,700 | 276,583 | 239,318 |
| Marketing | 280,598 | 155,461 | 436,059 | 487,841 |
| Business office | 1,036,327 | 354,338 | 1,390,665 | 1,323,574 |
| Data processing | 589,244 | 647,530 | 1,236,774 | 1,139,896 |
| Purchasing | 139,654 | 1,610 | 141,264 | 135,728 |

Waverly Health Center
EXPENSES (continued)
Year ended June 30, 2012, with comparative totals for 2011

| | <u>2012</u> | | | <u>2011</u> |
|--|---------------------|---------------------|---------------------|---------------------|
| | <u>Salaries</u> | <u>Other</u> | <u>Total</u> | <u>Total</u> |
| UNASSIGNED EXPENSES | | | | |
| FICA | \$ — | \$ 1,431,119 | \$ 1,431,119 | \$ 1,317,296 |
| IPERS | — | 1,674,361 | 1,674,361 | 1,367,075 |
| Group health, life and other benefits | — | 2,440,885 | 2,440,885 | 2,243,148 |
| Workers compensation insurance | — | 275,053 | 275,053 | 248,829 |
| Insurance | — | 337,461 | 337,461 | 277,841 |
| Total fiscal and administrative service and unassigned expenses | <u>3,625,494</u> | <u>8,245,366</u> | <u>11,870,860</u> | <u>11,318,992</u> |
| PROVISION FOR DEPRECIATION | <u>—</u> | <u>2,932,246</u> | <u>2,932,246</u> | <u>2,965,883</u> |
| Total expenses | <u>\$22,475,276</u> | <u>\$24,005,848</u> | <u>\$46,481,124</u> | <u>\$43,669,424</u> |

**Waverly Health Center
COMPARATIVE STATISTICS**

| | Year ended June 30 | |
|-----------------------------------|---------------------------|--------------------|
| | <u>2012</u> | <u>2011</u> |
| PATIENT DAYS | | |
| Medical, surgical and obstetrical | 2,329 | 2,605 |
| Swing bed | 1,040 | 984 |
| Nursery | <u>530</u> | <u>529</u> |
| Totals | <u>3,899</u> | <u>4,118</u> |
| DISCHARGES | | |
| Medical, surgical and obstetrical | 825 | 909 |
| Swing bed | 140 | 141 |
| Nursery | <u>247</u> | <u>226</u> |
| Totals | <u>1,212</u> | <u>1,276</u> |
| AVERAGE LENGTH OF STAY | | |
| Medical, surgical and obstetrical | 2.82 | 2.87 |
| Swing bed | 7.43 | 6.98 |
| Nursery | 2.15 | 2.34 |

**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**

Board of Trustees
Waverly Health Center
Waverly, Iowa

We have audited the financial statements of Waverly Health Center as of and for the year ended June 30, 2012, and have issued our report thereon dated October 8, 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

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Health Center'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*.

Comments involving statutory and other legal matters about the Health Center's operations for the year ended June 30, 2012 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Health Center. 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. Those comments are present in Part II of the accompanying Schedule of Findings.

This report, a public record by law, is intended solely for the information and use of the Board of Trustees, management, employees and citizens of the City of Waverly and other parties to whom the Health Center may report. This report is not intended to be and should not be used by anyone other than these specified parties.


DENMAN & COMPANY, LLP

West Des Moines, Iowa
October 8, 2012

**Waverly Health Center
SCHEDULE OF FINDINGS
Year ended June 30, 2012**

Part I—Findings Related to the Financial Statements

No matters regarding significant deficiencies, material weaknesses or instances of noncompliance relative to the financial statements were reported.

**Waverly Health Center
SCHEDULE OF FINDINGS
Year ended June 30, 2012**

Part II—Findings Related to Required Statutory Reporting

12-II-A CERTIFIED BUDGET

Based on a comparison of actual and budgeted expenditures, it appears the Health Center did not exceed its budget for the year ended June 30, 2012.

12-II-B QUESTIONABLE EXPENDITURES

No questionable expenditures of Health Center funds were noted.

12-II-C TRAVEL EXPENSES

No expenditures of Health Center money for travel expenses of spouses of Health Center officials and/or employees were noted.

12-II-D BUSINESS TRANSACTIONS

No business transactions were found between the Health Center and Health Center officials and/or employees.

12-II-E BOARD MINUTES

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

12-II-F DEPOSITS AND INVESTMENTS

We noted no instances of noncompliance with the deposit and investment provisions of Chapters 12B and 12C of the Code of Iowa and the Health Center's investment policy.