

Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

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

Together with Independent Auditor's Report

Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

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Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

Officials
June 30, 2012

Name	Title	Term Expires
Board of Trustees:		
	Jeff Ritchie - Chairman	March 2014
	Randy Fry - Vice Chair	March 2013
	Daryl Russ - Secretary / Treasurer	March 2015
	Adam Grier	March 2015
	Cindy Tindal	March 2015
	Lindsey Jergens	March 2014
	Charles Merritt	March 2013
Hospital Officials:		
	Barry Goettsch - Chief Executive Officer	Indefinite

Independent Auditor's Report

To the Board of Trustees
Marengo Memorial Hospital
Marengo, Iowa:

We have audited the accompanying basic financial statements of Marengo Memorial Hospital (Hospital), a component unit of the City of Marengo, Iowa, as of and for the year ended June 30, 2012, as listed in the table of contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Hospital for the year ended June 30, 2011, were audited by other auditors whose report, dated September 24, 2012, expressed an unqualified opinion on those financial statements.

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

As explained in Note 1, the accompanying financial statements present only the Hospital Fund of the city of Marengo, Iowa, and are not intended to present fairly the financial position of the city of Marengo, Iowa, and the results of its operations, changes in fund balance and its cash flows in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the 2012 financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of June 30, 2012, and the results of its operations, changes in net assets, and its cash flows for the year 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 24, 2012 on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by 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 basic financial statements as a whole. The other supplementary statements (Exhibits 1 – 6) are presented for the purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

SEIM JOHNSON, LLP

Omaha, Nebraska,
September 24, 2012.

Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

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

This discussion and analysis of Marengo Memorial Hospital (Hospital) financial performance provides an overview of financial activities for the fiscal years ended June 30, 2012 and 2011. This discussion and analysis should be read in conjunction with financial statements, which begin on page 8.

Financial Highlights

- The Hospital's net assets decreased in 2012 by \$412,206 or 5%. In 2011, net assets increased by \$210,349 or 3%.
- The Hospital reported an operating loss in 2012 of \$737,681 compared to an operating loss of \$102,311 in 2011.
- The Hospital's non-operating revenues increased by \$12,815 in 2012 compared to 2011.

Using This Annual Report

The Hospital's financial statements consist of three statements—a Balance Sheet; a Statement of Revenues, Expenses, and Changes in Net Assets; and a Statement 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.

The Balance Sheet and Statement of Revenue, Expenses, and Changes in Net Assets

Analysis of the Hospital's finances begins on page 8. The Balance Sheet and the Statement of Revenue, Expenses, and Changes in Net Assets report information about the Hospital's resources and 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. Over time, increases or decreases in net assets are an indicator of whether its financial health is improving or deteriorating. To access the overall health of the Hospital, non-financial factors, such as changes in the patient base of the Hospital and measures of the quality of service it provides to the community, as well as local economic factors, need to be considered.

The Statement of Cash Flows

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash 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 cash balance during the reporting period.

Marengo Memorial Hospital
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Management's Discussion and Analysis
June 30, 2012 and 2011

Net Assets

The Hospital's net assets are the difference between assets and liabilities reported in the Balance Sheet on page 8. The Hospital's net assets decreased in 2012 by \$412,206 or 5%, as shown in **Table 1**.

Table 1: Assets, Liabilities, and Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>Dollar Change</u>	<u>Percent Change</u>
Assets:					
Total current assets	\$ 4,825,270	3,732,013	3,368,169	1,093,257	29%
Capital assets, net	8,891,106	9,731,342	9,909,159	(840,236)	-9%
Assets limited as to use	2,234,158	4,870,915	5,052,376	(2,636,757)	-54%
Other non-current assets	299,597	185,090	204,890	114,507	62%
Total assets	<u>\$ 16,250,131</u>	<u>18,519,360</u>	<u>18,534,594</u>	<u>(2,269,229)</u>	-12%
Liabilities:					
Long-term debt	\$ 7,490,000	9,035,354	9,538,423	(1,545,354)	-17%
Estimated third-party payor settlements	--	--	280,000	--	0%
Other current and non-current liabilities	1,035,909	1,347,578	790,092	(311,669)	-23%
Total liabilities	8,525,909	10,382,932	10,608,515	(1,857,023)	-18%
Net Assets:					
Net assets	7,724,222	8,136,428	7,926,079	(412,206)	-5%
Total liabilities and net assets	<u>\$ 16,250,131</u>	<u>18,519,360</u>	<u>18,534,594</u>	<u>(2,269,229)</u>	-12%

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

Operating Results and Changes in Net Assets

In 2012, the Hospital's operating revenue decreased by \$635,370 as shown in **Table 2**. The majority of this decrease is caused by an increase in salaries and employee benefits.

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

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>Dollar Change</u>	<u>Percent Change</u>
Operating revenue:					
Net patient service revenue	\$ 15,030,191	14,958,551	15,189,837	71,640	0%
Provision for bad debt	(614,093)	(442,104)	(449,886)	(171,989)	39%
Other operating revenue	806,983	138,955	144,522	668,028	481%
Total operating revenue	<u>15,223,081</u>	<u>14,655,402</u>	<u>14,884,473</u>	<u>567,679</u>	4%
Operating Expenses:					
Salaries and employee benefits	8,730,624	8,108,209	8,581,998	622,415	8%
Purchased services and other	5,470,337	5,023,010	4,579,461	447,327	9%
Depreciation and amortization	1,297,192	1,151,418	1,224,054	145,774	13%
Interest	462,609	475,076	498,324	(12,467)	-3%
Total operating expenses	<u>15,960,762</u>	<u>14,757,713</u>	<u>14,883,837</u>	<u>1,203,049</u>	8%
Operating income (loss)	<u>(737,681)</u>	<u>(102,311)</u>	<u>636</u>	<u>(635,370)</u>	
Non-Operating Revenue and Expenses					
Property taxes	41,581	41,372	39,831	209	1%
Ambulance subsidy	158,054	135,361	129,119	22,693	17%
Investment income	110,698	129,953	122,227	(19,255)	-15%
Transfer from related foundation	15,142	5,974	13,334	9,168	153%
Total non-operating revenue, net	<u>325,475</u>	<u>312,660</u>	<u>304,511</u>	<u>12,815</u>	4%
Increase (decrease) in net assets	(412,206)	210,349	305,147	(622,555)	-296%
Net assets – beginning of year	<u>8,136,428</u>	<u>7,926,079</u>	<u>7,620,932</u>	<u>210,349</u>	3%
Net assets – end of year	<u>\$ 7,724,222</u>	<u>8,136,428</u>	<u>7,926,079</u>	<u>(412,206)</u>	-5%

Operating Income (Loss)

The first component of the overall change in the Hospital's net assets is its operating income (loss) - generally, the difference between net patient service revenues and the expenses incurred to perform those services.

The primary components affecting operating income are:

- Rate and volume increases.
- Medicare/Medicaid Cost Report Settlements and other third party contractual relationships.
- Salary adjustments to stay competitive.
- Employee health insurance.
- Professional/Physician contracts for ancillary departments.

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

A component of the Hospital's costs is expenses for salaries and benefits. In 2012 salaries and benefit costs totaled \$8,730,624. In 2011 salaries and benefit costs totaled \$8,108,209. Part of the reason for the increase of 8% is that the Hospital added over 6 full time equivalent employees.

The Hospital at times provides care for patients who have little or no health insurance or other means of repayment. Because there is no expectation of repayment, charity care is not reported as patient service revenues of the Hospital.

Non-operating Revenues and Expenses

Non-operating revenues consist primarily of property taxes levied for the Hospital, ambulance subsidies, interest revenue, and transfers from related foundation. Non-operating revenue increased \$12,815 in 2012.

Cash Flows

Changes in cash flows are consistent with changes in operating income and non-operating revenues and expenses, discussed earlier. Cash flows provided by operating activities decrease in 2012 due to increases in patient accounts receivable and increase in estimated third-party payor settlements.

Capital Asset and Debt Administration

Capital Assets

At the end of 2012, the Hospital had \$8,891,106 invested in capital assets, net of accumulated depreciation. Approximately \$437,000 was spent to acquire new equipment in 2012.

Debt

In 2012, \$7,490,000 in Series 2012 refunding revenue bonds were issued to obtain interest rates ranging from 1.00% to 3.75%. The refunding revenue bonds are expected to save over \$1,100,000 in interest cost.

Other Economic Factors

The 2012 fiscal year provided the Hospital substantial challenges due to federal program reimbursement requirements, pressures from other insurers, and the fluctuation of patient demand.

Inflation continued in 2012 with supply and equipment costs increasing at market rates and the pressure on nursing and other salary costs being driven by the shortage of supply of these health care professionals.

Contacting Hospital Financial Management

This financial report is designed to provide patients, suppliers, taxpayers, and creditors with a general overview of the Hospital finances. Questions about this report or requests for additional information should be directed to:

Marengo Memorial Hospital
Attn: Barry Goetsch, CEO
300 West May Street
Marengo IA 52301
319-642-5543

Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

Balance Sheets
June 30, 2012 and 2011

ASSETS	<u>2012</u>	<u>2011</u>
Current assets:		
Cash and cash equivalents	\$ 605,288	645,393
Assets limited as to use or restricted, current portion	702,312	292,500
Receivables -		
Patient receivables, net of estimated uncollectible accounts of \$282,896 and \$220,000 in 2012 and 2011, respectively	2,548,513	2,246,761
Other - county tax revenue	19,487	--
Estimated third-party payor settlements	426,706	80,000
Inventories	306,362	283,731
Prepaid expenses	<u>216,602</u>	<u>183,628</u>
Total current assets	4,825,270	3,732,013
Assets limited as to use or restricted	2,234,158	4,870,915
Capital assets, net	8,891,106	9,731,342
Deferred financing costs	<u>299,597</u>	<u>185,090</u>
Total assets	<u>\$ 16,250,131</u>	<u>18,519,360</u>
 LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term debt	\$ 700,000	524,853
Accounts payable	327,783	749,451
Accrued salaries, vacation and benefits payable	705,814	560,627
Accrued interest payable	<u>2,312</u>	<u>37,500</u>
Total current liabilities	1,735,909	1,872,431
Long-term debt, net of unamortized discount and current portion	<u>6,790,000</u>	<u>8,510,501</u>
Total liabilities	<u>8,525,909</u>	<u>10,382,932</u>
Commitments and contingencies		
Net assets:		
Invested in capital assets, net of related debt	2,455,419	1,580,053
Unrestricted	<u>5,268,803</u>	<u>6,556,375</u>
Total net assets	<u>7,724,222</u>	<u>8,136,428</u>
Total liabilities and net assets	<u>\$ 16,250,131</u>	<u>18,519,360</u>

See notes to financial statements

Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

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

	<u>2012</u>	<u>2011</u>
OPERATING REVENUE:		
Net patient service revenue before provision for bad debt	\$ 15,030,191	14,958,551
Provision for bad debt	<u>(614,093)</u>	<u>(442,104)</u>
Net patient service revenue	14,416,098	14,516,447
Other operating revenue	<u>806,983</u>	<u>138,955</u>
Total operating revenue	<u>15,223,081</u>	<u>14,655,402</u>
OPERATING EXPENSES:		
Salaries	6,660,834	6,279,317
Employee benefits	2,069,790	1,828,892
Professional fees and purchased services	2,714,535	2,492,250
Supplies and other	2,573,752	2,366,399
Insurance	182,050	164,361
Depreciation and amortization	1,297,192	1,151,418
Interest	<u>462,609</u>	<u>475,076</u>
Total operating expenses	<u>15,960,762</u>	<u>14,757,713</u>
OPERATING LOSS	<u>(737,681)</u>	<u>(102,311)</u>
NONOPERATING REVENUE:		
County tax revenues	41,581	41,372
Ambulance subsidy	158,054	135,361
Investment income	110,698	129,953
Transfer from related foundation	<u>15,142</u>	<u>5,974</u>
Nonoperating revenues, net	<u>325,475</u>	<u>312,660</u>
INCREASE (DECREASE) IN NET ASSETS	(412,206)	210,349
NET ASSETS, Beginning of year	<u>8,136,428</u>	<u>7,926,079</u>
NET ASSETS, End of year	<u>\$ 7,724,222</u>	<u>8,136,428</u>

See notes to financial statements

Marengo Memorial Hospital
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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	\$ 13,767,640	14,564,739
Cash paid for employee salaries and benefits	(8,585,437)	(8,096,543)
Cash paid to suppliers and contractors	(5,947,610)	(4,627,883)
Other receipts and payments, net	<u>806,983</u>	<u>138,955</u>
Net cash provided by operating activities	<u>41,576</u>	<u>1,979,268</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Transfer from related foundation	15,142	5,974
Ambulance subsidy	158,054	135,361
County tax receipts	<u>22,094</u>	<u>41,372</u>
Net cash provided by noncapital financing activities	<u>195,290</u>	<u>182,707</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of property and equipment, net	(437,156)	(953,801)
Interest payments	(497,797)	(478,376)
Bond issuance costs	(134,307)	--
Receipts from issuance of long-term debt	7,490,000	--
Principal payments on long-term debt	<u>(9,035,354)</u>	<u>(503,069)</u>
Net cash used in capital and related financing activities	<u>(2,614,614)</u>	<u>(1,935,246)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Change in investments and assets limited as to use or restricted, net	2,226,945	(111,039)
Investment income	<u>110,698</u>	<u>129,953</u>
Net cash provided by investing activities	<u>2,337,643</u>	<u>18,914</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(40,105)	245,643
CASH AND CASH EQUIVALENTS, Beginning of year	<u>645,393</u>	<u>399,750</u>
CASH AND CASH EQUIVALENTS, End of year	<u>\$ 605,288</u>	<u>645,393</u>

See notes to financial statements

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

	<u>2012</u>	<u>2011</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating loss	\$ (737,681)	(102,311)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	1,297,192	1,151,418
Interest expense included in operating expenses	462,609	475,076
(Increase) decrease in current assets -		
Receivables - patients	(301,752)	408,292
Inventories	(22,631)	(6,051)
Prepaid expenses	(32,974)	(147,942)
Estimated third-party payor settlements	(346,706)	(360,000)
Increase (decrease) in current liabilities -		
Accounts payable	(421,668)	549,120
Accrued salaries, vacation and benefits payable	145,187	11,666
Net cash provided by operating activities	\$ <u>41,576</u>	<u>1,979,268</u>

See notes to financial statements

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

The following is a summary of significant accounting policies of Marengo Memorial Hospital (Hospital). These policies are in accordance with accounting principles generally accepted in the United States of America. The Hospital is a city public hospital organized under Chapter 392 of the Code of Iowa and governed by a five member Board of Trustees elected for terms of four years.

A. Reporting Entity

The Hospital's financial statements are an integral part of the City of Marengo, Iowa. The accompanying financial statements are not intended to present fairly the financial position and changes in financial position of the City of Marengo, Iowa, in conformity with accounting principles generally accepted in the United States of America.

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

The Budget Reconciliation Act of 1997 (Act) contained many provisions impacting Medicare reimbursement for Health Services. The Act established the Medicare Rural Hospital Flexibility Program to assist states and rural communities to improve access to essential health care services through limited service hospitals and rural health networks. The Hospital is a Critical Access Hospital (CAH), operating with 25 acute-care beds. CAH's are acute care facilities that provide emergency, outpatient and short-term inpatient services. Medicare reimburses CAH's on a reasonable cost basis.

B. Industry Environment

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

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

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

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Notes to Financial Statements
June 30, 2012 and 2011

C. *Basis of Presentation*

The Balance Sheets display the Hospital's assets and liabilities, with the difference reported as net assets. When both restricted and unrestricted resources are available for use, generally it is the Hospital's policy to use restricted resources first. Net assets are reported as follows:

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

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

D. *Measurement Focus and Basis of Accounting*

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

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

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

E. *Use of Estimates*

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

F. *Cash and Cash Equivalents*

Cash and cash equivalents for purposes of the statements of cash flows include investments in highly liquid debt instruments with original maturities of three months or less, excluding amounts limited as to use by the Board of Trustees and under debt agreements.

G. *Investments*

Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in excess of expenses over revenue unless the income is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of expenses over revenue unless the investments are trading securities. Periodically the Hospital reviews its investments to determine whether any unrealized losses are other than temporary. During 2012 and 2011, there were no investment declines that were determined to be other than temporary.

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Notes to Financial Statements
June 30, 2012 and 2011

H. Patient Receivables, Net

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

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

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

I. Inventories

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

J. Property Tax Receivable

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

K. Assets Limited as to Use or Restricted

Assets limited as to use or restricted include the following:

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

By Debt Agreement - These funds are reserve funds held as security for the Series 2012 bonds. These funds are used for the payment of principal and interest on the Series 20012 bonds when insufficient funds are available in the sinking fund.

L. Fair Value of Financial Instruments

The carrying value of all financial instruments approximates estimated fair value. Cash and cash equivalents, assets limited as to use, accounts receivable, and accounts payable approximate fair value due to the relatively short period of time between their origination and expected realization. Fair values for investments are based on quoted market prices, if available, or estimated using quoted market prices of similar securities. The carrying value of long-term debt approximates fair value since the interest rates closely reflect current market rates.

M. Capital Assets

Capital asset acquisitions in excess of \$5,000 are capitalized and recorded at cost. Depreciation is provided over the estimated life of each depreciable asset and is computed using the straight-line method.

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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	5 to 20 years
Buildings and building improvements	5 to 40 years
Equipment, computers and furniture	3 to 20 years

The Hospital's long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum of the expected cash flows is less than the carrying amount of the asset, a loss is recognized.

Gifts of long-lived assets such as land, buildings or equipment are reported as unrestricted support and are excluded from the excess of revenue over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed into service.

N. Deferred Financing Costs

Deferred financing costs related to the issuance of the Hospital revenue refunding bonds are being amortized over the life of the related bonds under the straight-line method. Amortization expense of \$19,800 for 2012 and 2011, respectively, is included in depreciation and amortization in the accompanying statements of revenue, expenses and changes in net assets.

O. Compensated Absences

Paid Time Off (PTO) vests bi-weekly and may be carried forward by an employee in an amount not to exceed 280 hours. PTO expense is accrued as an expense and a liability as it is earned. PTO expenditures are recognized to the extent it is paid during the year and the vested amount is recorded as a current liability.

P. Income Taxes

Under the Code of Iowa, Chapter 392, the Hospital is an instrumentality of the City of Marengo, Iowa. As such, the Hospital is exempt from paying income taxes.

Q. Net Patient Service Revenue

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

R. Charity Care

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

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The Hospital is dedicated to providing comprehensive healthcare services to all segments of society, including the aged and otherwise economically disadvantaged. In addition, the Hospital provides a variety of community health services at or below cost.

S. *Grants and Contributions*

From time to time, the Hospital receives 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 restricted for a specific operating purpose are reported as nonoperating revenue. Amounts restricted to capital acquisitions are reported after nonoperating revenue and expenses.

T. *County Tax Revenue*

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

U. *Operating Loss*

Transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as operating revenue and expenses. Peripheral or incidental transactions are reported as nonoperating revenue and expenses.

V. *Risk Management*

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

W. *Reclassification*

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

X. *Subsequent Events*

The Hospital considered events occurring through September 24, 2012 for recognition or disclosure in the financial statements as subsequent events. That date is the date the financial statements were available to be issued.

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

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

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

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The Hospital manages the following risks in accordance with their formal investment policy:

Credit Risk: Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2012 and 2011, the Hospital is invested in certificate of deposits and mutual funds that are not rated.

Interest Rate Risk: The Hospital has a formal investment policy that limits investment maturities to 397 days or less as a means of managing its exposure to fair value losses arising from changes in interest rates for current operating funds. Other investments are to have maturities consistent with the needs of the Hospital.

Custodial credit risk: Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Hospital's investment policy requires the fund to be deposited into banking institutions that have the ability to collateralize any deposits made in excess of the Federal Deposit Insurance Corporation's insurance limits.

The Hospital's investments are carried at fair value. All bank deposit accounts are fully insured or collateralized by securities held by the Hospital's agent in the Hospital's name.

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

	<u>2012</u>	<u>2011</u>
Assets Limited as to Use or Restricted:		
By the Board of Trustees for capital improvements:		
Cash and cash equivalents	\$ --	106,192
Certificates of deposit	2,181,754	3,825,737
Marketable securities	--	407,673
	<u>2,181,754</u>	<u>4,339,602</u>
By Debt Agreements:		
Cash and cash equivalents	64,963	124,838
Certificates of deposit	480,331	488,147
U.S. treasury note	209,422	210,828
	<u>754,716</u>	<u>823,813</u>
Total assets limited as to use or restricted	2,936,470	5,163,415
Less amounts required to meet current obligations	<u>702,312</u>	<u>292,500</u>
Long-term portion	\$ <u>2,234,158</u>	<u>4,870,915</u>

(3) Net Patient Service Revenue

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

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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. Outpatient services related to Medicare beneficiaries are also paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audit thereof by the Medicare fiscal intermediary. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2010.

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

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

The following illustrates the Hospital's patient service revenue at its established rates and revenue deductions by major third-party payors:

	<u>2012</u>	<u>2011</u>
Gross patient service revenue:		
Inpatient services and swing bed	\$ 4,092,010	3,712,171
Outpatient	14,162,296	11,402,901
Clinics	<u>1,921,431</u>	<u>1,525,367</u>
Total gross patient service revenue	<u>20,175,737</u>	<u>16,640,439</u>
Deductions from patient service revenue:		
Medicare	3,140,946	278,060
Medicaid	251,588	186,800
Other payors	1,710,144	1,089,388
Charity care	<u>42,868</u>	<u>127,640</u>
Total deductions from patient service revenue	<u>5,145,546</u>	<u>1,681,888</u>
Net patient service revenue before provision for bad debt	<u>\$ 15,030,191</u>	<u>14,958,551</u>

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

Revenue from the Medicare and Medicaid programs accounts for approximately 57% and 7%, respectively, of the Hospital's net patient revenue for the year ended June 30, 2012 compared to 59% for Medicare and 9% for Medicaid in 2011. The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

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(4) Other Revenue

Other revenue for the years ended June 30, 2012 and 2011 consisted of the following:

	<u>2012</u>	<u>2011</u>
Electronic health record incentive payments	\$ 667,105	--
Dietary	27,963	25,213
Miscellaneous	22,713	23,253
Dietary	20,216	24,868
Ideal protein	14,450	17,691
Professional services to others	54,536	47,930
	<u>\$ 806,983</u>	<u>138,955</u>

The Health Information Technology for Economic and Clinical Health Act contains specific financial incentives designed to accelerate the adoption of electronic health record (EHR) systems among health care providers. During 2012, the Hospital qualified for the financial incentives payments by attesting it met specific criteria set by the Centers for Medicare and Medicaid Services (CMS). Management's attestation is subject to audit by the federal government or its designee.

The EHR incentive payment will be earned and received through various payments through 2015. The incentive amount is computed using several elements, one of which includes using the value of un-depreciated assets required to implement the EHR system. The Hospital has elected to record \$667,105 of the incentive payment as other operating revenue in the period earned, and defer approximately \$650,000 related to future Medicare reimbursement. In addition, the Iowa Department of Health and Human Services (DHHS) provides EHR incentive payments that will be earned and received through various payments through 2014. The amounts recognized are based on management's best estimates and are subject to change, which would be recognized in the period in which the change occurs.

(5) Composition of Patient Receivables

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

	<u>2012</u>	<u>2011</u>
Patient receivables	\$ 3,384,059	2,666,761
Less estimated third-party contractual adjustments	(552,650)	(200,000)
Less allowance for doubtful accounts	(282,896)	(220,000)
	<u>\$ 2,548,513</u>	<u>2,246,761</u>

The Hospital is located in Marengo, Iowa. The Hospital grants credit without collateral to its patients, most of whom are local residents and 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	44%	47%
Medicaid	5	5
Other third-party payors	35	29
Private pay	16	19
	<u>100%</u>	<u>100%</u>

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Notes to Financial Statements
June 30, 2012 and 2011

(7) Long-Term Debt

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

	<u>June 30,</u> <u>2011</u>	<u>Borrowings</u>	<u>Payments</u>	<u>June 30,</u> <u>2012</u>	<u>Due Within</u> <u>One Year</u>
Series 2012 (a)	\$ --	7,490,000	--	7,490,000	700,000
Series 2005 (b)	4,000,000	--	(4,000,000)	--	--
Series 2004 (c)	4,555,000	--	(4,555,000)	--	--
Note payable, equipment (d)	480,354	--	(480,354)	--	--
	<u>\$ 9,035,354</u>	<u>7,490,000</u>	<u>(9,035,354)</u>	<u>7,490,000</u>	<u>700,000</u>
	<u>June 30,</u> <u>2010</u>	<u>Borrowings</u>	<u>Payments</u>	<u>June 30,</u> <u>2011</u>	<u>Due Within</u> <u>One Year</u>
Series 2005 (b)	\$ 4,000,000	--	--	4,000,000	--
Series 2004 (c)	4,800,000	--	(245,000)	4,555,000	255,000
Note payable, equipment (d)	738,423	--	(258,069)	480,354	269,853
	<u>\$ 9,538,423</u>	<u>--</u>	<u>(503,069)</u>	<u>9,035,354</u>	<u>524,853</u>

- (a) The Hospital issued \$7,490,000 of Hospital Revenue Refunding Bonds, Series 2012. The proceeds of these bonds were used to achieve a current refunding of its Hospital Revenue Notes, Series 2005 and Series 2004. The Series 2012 bonds bear interest at rates ranging from 1.00% to 3.75%. Annual principal payments are due in amounts ranging from \$695,000 to \$855,000 through June 2022.

The Series 2012 bonds grant a security interest in all revenue either accrued or received in connection with operations of the Hospital. The terms of the trust indenture require the Hospital to comply with certain covenants. The covenants provide for restrictions as to financial reporting, restrictions on the sale of the health care facilities and require the Hospital to maintain debt service and sinking fund accounts and to maintain specified debt service coverage and liquidity ratios.

- (b) The Hospital issued Hospital Revenue Notes, Series 2005 in the original amount of \$4,000,000. Funds from the issuance of the Hospital Revenue Refunding Bonds, Series 2012, were deposited into an escrow account and were used to pay off the defeased Series 2005 notes principal and interest balances effective July 15, 2012.
- (c) The Hospital issued Hospital Revenue Notes, Series 2004 in the original amount of \$6,000,000. Funds from the issuance of the Hospital Revenue Refunding Bonds, Series 2012, were deposited into an escrow account and were used to pay off the defeased Series 2004 notes principal and interest balances effective July 15, 2012.
- (d) The Hospital entered into a note payable to finance the purchase of certain equipment. The note required monthly payments of \$23,830, including interest at 4.5%, with final payment due April 2013. During 2012, the Hospital paid the note off in full.

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

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 700,000	170,164	870,164
2014	695,000	175,863	870,863
2015	700,000	167,523	867,523
2016	715,000	155,273	870,273
2017	730,000	141,688	871,688
2018 - 2022	<u>3,950,000</u>	<u>409,558</u>	<u>4,359,558</u>
	<u>\$ 7,490,000</u>	<u>1,220,069</u>	<u>8,710,069</u>

(8) 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 \$4,000,000 per occurrence and in aggregate coverage. These policies provide coverage on a claims-incurred basis covering only those claims which have occurred and are reported to the insurance company.

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.

(9) Pension Plan

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

Plan members are required to contribute 5.38% of their annual salary and the Hospital is required to contribute 8.07% of annual covered payroll. Contribution requirements are established by State statute. The Hospital's contribution to IPERS for the years ended June 30, 2012, 2011, and 2010 were \$543,878, \$446,011, and \$445,694, respectively, equal to the required contributions for each year.

(10) Commitments and Contingencies

Litigation – The Hospital is involved in litigation arising in the normal course of business. After consultation with legal counsel, management estimates these matters will be resolved without material adverse affect on the Hospital's future financial position or results from operations.

Operating Leases – The Hospital leases certain equipment under operating leases expiring at various dates though 2017. The following is a schedule by year of future minimum lease payments under operating leases as of June 30, 2012, that have initial lease terms in excess of one year:

2013	\$ 44,597
2014	44,597
2015	44,597
2016	44,597
2017	<u>33,448</u>
	<u>\$ 211,836</u>

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Notes to Financial Statements
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(11) Risks and Uncertainties

Investment securities, in general, are exposed to various risks, such as interest rate risk, credit risk and overall market volatility. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the financial statements.

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

	2012			2011		
	Inpatient	Outpatient	Total	Inpatient	Outpatient	Total
DAILY PATIENT SERVICES:						
Adult and pediatric	\$ 344,750	--	344,750	233,875	--	233,875
Skilled care	1,394,941	--	1,394,941	1,447,525	--	1,447,525
Intermediate Care	283,750	--	283,750	220,850	--	220,850
	<u>2,023,441</u>	<u>--</u>	<u>2,023,441</u>	<u>1,902,250</u>	<u>--</u>	<u>1,902,250</u>
OTHER PROFESSIONAL SERVICES:						
Emergency	892	2,286,721	2,287,613	872	2,118,725	2,119,597
Observation room	--	319,222	319,222	913	295,717	296,630
Operating and recovery room	117,034	1,233,426	1,350,460	18,763	732,349	751,112
Anesthesiology	7,715	81,875	89,590	1,548	34,905	36,453
Radiology	135,698	1,612,864	1,748,562	101,105	1,650,786	1,751,891
Respiratory therapy	140,192	324,066	464,258	178,269	307,923	486,192
Laboratory	263,574	1,625,043	1,888,617	226,458	1,494,288	1,720,746
Physical therapy	291,465	812,618	1,104,083	201,821	489,239	691,060
Speech therapy	15,490	7,183	22,673	22,114	6,253	28,367
Dialysis	--	3,730,218	3,730,218	--	1,609,340	1,609,340
Occupational therapy	284,781	99,162	383,943	230,865	48,152	279,017
Pharmacy	811,728	913,622	1,725,350	827,193	1,587,967	2,415,160
Ambulance	--	1,116,276	1,116,276	--	1,027,257	1,027,257
Clinics	--	1,921,431	1,921,431	--	1,525,367	1,525,367
	<u>2,068,569</u>	<u>16,083,727</u>	<u>18,152,296</u>	<u>1,809,921</u>	<u>12,928,268</u>	<u>14,738,189</u>
GROSS PATIENT SERVICE REVENUE	\$ <u>4,092,010</u>	<u>16,083,727</u>	<u>20,175,737</u>	<u>3,712,171</u>	<u>12,928,268</u>	<u>16,640,439</u>
LESS CONTRACTUAL ADJUSTMENTS			(5,145,546)			(1,681,888)
NET PATIENT SERVICE REVENUE BEFORE PROVISION FOR BAD DEBT			15,030,191			14,958,551
PROVISION FOR BAD DEBT			(614,093)			(442,104)
NET PATIENT SERVICE REVENUE			<u>14,416,098</u>			<u>14,516,447</u>

See accompanying independent auditor's report

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

	<u>2012</u>	<u>2011</u>
Electronic health record incentive payments	\$ 667,105	--
Dietary	27,963	25,213
Rental income	22,713	23,253
Grants	20,216	24,868
Gift shop	14,450	17,691
Miscellaneous	54,536	47,930
	<u>\$ 806,983</u>	<u>138,955</u>

See accompanying independent auditor's report

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

	2012			2011		
	Salaries and Wages	Other	Total	Salaries and Wages	Other	Total
NURSING SERVICES:						
Adults and pediatrics	\$ 1,599,022	194,681	1,793,703	1,595,073	230,170	1,825,243
Operating room	117,569	489,807	607,376	58,494	235,009	293,503
Emergency service	555,116	342,800	897,916	486,710	291,875	778,585
Ambulance	515,136	21,127	536,263	501,218	23,826	525,044
	<u>2,786,843</u>	<u>1,048,415</u>	<u>3,835,258</u>	<u>2,641,495</u>	<u>780,880</u>	<u>3,422,375</u>
OTHER PROFESSIONAL SERVICES:						
Laboratory	275,832	327,208	603,040	279,002	297,387	576,389
Radiology	173,489	571,344	744,833	166,383	587,959	754,342
Respiratory therapy	190,310	43,931	234,241	230,676	43,033	273,709
Pharmacy	61,214	752,589	813,803	48,128	799,727	847,855
Physical therapy	--	407,542	407,542	--	360,427	360,427
Speech therapy	--	9,382	9,382	--	17,396	17,396
Dialysis	98,014	252,933	350,947	49,374	84,407	133,781
Occupational therapy	--	149,157	149,157	--	161,191	161,191
Clinic	845,728	280,957	1,126,685	710,674	254,102	964,776
Health information management	221,252	32,712	253,964	184,792	28,558	213,350
	<u>1,865,839</u>	<u>2,827,755</u>	<u>4,693,594</u>	<u>1,669,029</u>	<u>2,634,187</u>	<u>4,303,216</u>
GENERAL SERVICES:						
Plant operation and maintenance	170,660	304,371	475,031	173,767	390,069	563,836
Dietary	176,131	123,736	299,867	176,909	114,664	291,573
Housekeeping	127,472	49,624	177,096	119,553	50,392	169,945
Central supply	46,645	--	46,645	45,495	--	45,495
	<u>520,908</u>	<u>477,731</u>	<u>998,639</u>	<u>515,724</u>	<u>555,125</u>	<u>1,070,849</u>
ADMINISTRATIVE SERVICES	<u>1,487,244</u>	<u>1,050,965</u>	<u>2,538,209</u>	<u>1,453,069</u>	<u>1,031,514</u>	<u>2,484,583</u>
NONDEPARTMENTAL:						
Lifeline	--	15,242	15,242	--	18,351	18,351
Group health and life	--	886,337	886,337	--	794,629	794,629
FICA	--	507,754	507,754	--	426,844	426,844
IPERS	--	543,878	543,878	--	446,011	446,011
Depreciation and amortization	--	1,297,192	1,297,192	--	1,151,418	1,151,418
Interest	--	462,609	462,609	--	475,076	475,076
Insurance	--	182,050	182,050	--	164,361	164,361
	<u>--</u>	<u>3,895,062</u>	<u>3,895,062</u>	<u>--</u>	<u>3,476,690</u>	<u>3,476,690</u>
TOTAL EXPENSES	<u>\$ 6,660,834</u>	<u>9,299,928</u>	<u>15,960,762</u>	<u>6,279,317</u>	<u>8,478,396</u>	<u>14,757,713</u>

See accompanying independent auditor's report

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

ANALYSIS OF AGING:

Days Since Discharge	2012		2011	
	Amount	Percent of Total	Amount	Percent of Total
0 - 30	\$ 1,882,400	55.63 %	1,514,612	56.80 %
31 - 60	664,131	19.63	443,386	16.63
61 - 90	263,403	7.78	201,053	7.54
91 - 120	241,348	7.13	171,795	6.44
121 and over	332,777	9.83	335,915	12.59
	<u>3,384,059</u>	<u>100.00 %</u>	<u>2,666,761</u>	<u>100.00 %</u>
Less:				
Allowance for doubtful accounts	(282,896)		(220,000)	
Allowance for contractual adjustments	<u>(552,650)</u>		<u>(200,000)</u>	
	<u>\$ 2,548,513</u>		<u>2,246,761</u>	

	2012	2011
ALLOWANCE FOR DOUBTFUL ACCOUNTS:		
Balance, beginning of year	\$ 220,000	223,100
Provision of uncollectible accounts	691,910	535,928
Recoveries of accounts previously written off	(87,501)	(48,462)
Accounts written off	<u>(541,513)</u>	<u>(490,566)</u>
Balance, end of year	<u>\$ 282,896</u>	<u>220,000</u>

See accompanying independent auditor's report

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

	<u>2012</u>	<u>2011</u>
INVENTORY:		
Pharmacy	\$ 148,790	113,030
Operating room	24,997	13,123
Laboratory	17,283	8,016
Other	<u>115,292</u>	<u>149,562</u>
	<u>\$ 306,362</u>	<u>283,731</u>
	<u>2012</u>	<u>2011</u>
PREPAID EXPENSES:		
Insurance	\$ 94,015	99,301
Maintenance contracts	<u>122,587</u>	<u>84,327</u>
	<u>\$ 216,602</u>	<u>183,628</u>

See accompanying independent auditor's report

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

	<u>2012</u>	<u>2011</u>
Patient days:		
Adult and pediatric	476	361
Swing-bed -		
Skilled	2,088	2,482
Intermediate	<u>1,766</u>	<u>1,578</u>
Total	<u><u>4,330</u></u>	<u><u>4,421</u></u>
Patient discharges:		
Adult and pediatric	158	130
Swing-bed -		
Skilled	157	142
Intermediate	<u>28</u>	<u>30</u>
	<u><u>343</u></u>	<u><u>302</u></u>
Average length of stay (based on discharge days):		
Adult and pediatric	3.01	2.78
Swing-bed -		
Skilled	13.30	17.48
Intermediate	63.07	52.6
Surgical procedures	351	250
Emergency room visits	3,363	3,217
Number of employees - full-time equivalents	172.67	166.58

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

To the Board of Trustees
Marengo Memorial Hospital
Nevada, Iowa:

We have audited the financial statements of Marengo Memorial Hospital (Hospital) as of and for the years ended June 30, 2012 and 2011, and have issued our report thereon, dated September 24, 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 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 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. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs as items II-A-12 and II-B-12 that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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*.

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.

The Hospital's responses to findings identified in our audit are described in the accompanying schedule of findings and questioned costs. 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 the Hospital and other parties to who the Hospital may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by the personnel of the 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 24, 2012

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

Part I: Summary of the Independent Auditor's Results

- (a) An unqualified opinion was issued on the financial statements.
- (b) Significant deficiencies in internal control over financial reporting were disclosed by the audit of the financial statements.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.

Part II: Findings Related to the Financial Statements

Instances of Non-Compliance:

No matters were reported.

Significant Deficiencies:

II-A-12

Management Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimations and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements. Audit journal entries were made to adjust amounts recorded by management for certain settlement, contractual adjustments in accounts receivable, and allowance for doubtful accounts estimates.

Recommendation: We recommend that management review their estimation processes in these areas and determine if additional procedures or templates can be added to enhance the estimation process at year end and on an interim basis.

Response: Management is aware of this deficiency and will develop additional procedures to improve the existing estimation process at year end and on an interim basis.

Conclusion: Response accepted.

II-B-12

Segregation of Duties: One important aspect of internal controls is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The limited number of office personnel prevents a proper segregation of accounting functions necessary to assure optimal internal control.

Recommendation: 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.

Response: 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.

Conclusion: Response accepted.

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

Part III: Other Findings Related to Required Statutory Reporting

III-A-12

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

III-B-12

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

III-C-12

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

III-D-12

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

III-E-12

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

III-F-12

Publishing Requirements: An annual condensed statement of total receipts and expenditures is to be published in a newspaper of the city in which the Hospital is located according to Chapter 392.6 of the Code of Iowa.

Marengo Memorial Hospital
A Component Unit of the City of Marengo, Iowa

Audit Staff
For the Year Ended June 30, 2012

This audit was performed by:

Brian D. Green, FHFMA, CPA, Partner

Jeremy J. Behrens, CHFP, CPA, Senior Manager

Vanessa L. Paswaters, Staff Auditor