

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

**Basic Financial Statements
and Supplementary Information
June 30, 2014 and 2013**

Together with Independent Auditor's Report

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Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Officials
June 30, 2014

	<u>Address</u>	<u>Term Expires</u>
Board of Trustees:		
Matt Hummel, President	Hawarden, Iowa	December 2015
Kathy Jacobs, Vice-President	Hawarden, Iowa	December 2015
Glea Hamik, Secretary	Hawarden, Iowa	December 2015
Denny Hulshof	Ireton, Iowa	December 2017
Stan Hoekstra	Hawarden, Iowa	December 2017
Hospital Officials:		
Jayson Pullman, Chief Executive Officer	Hawarden, Iowa	Indefinite

Independent Auditor's Report

To the Board of Trustees
Hawarden Regional Healthcare
Hawarden, Iowa:

Report on the Financial Statements

We have audited the accompanying basic financial statements of Hawarden Regional Healthcare (Hospital), a component unit of the city of Hawarden, Iowa, as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Hospital, as of and for the years ended June 30, 2014 and 2013, and the respective change in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the financial statements, in 2014 Hawarden Regional Healthcare adopted new accounting guidance to reflect the provisions of Statement No. 65 of the Governmental Accounting Standards Board (GASB), *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to this matter.

Other Matters

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

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Hospital's basic financial statements. The supplementary statements (Exhibits 1 - 6) are presented for the purposes of additional analysis and are not a required part of the financial statements.

The other supplementary information (Exhibits 1 - 6) are the responsibility of management and were derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such 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 other supplementary information (Exhibits 1 - 6) are fairly stated in all material respects in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 30, 2014 on our consideration of the Hospital's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control over financial reporting and compliance.

SEIM JOHNSON, LLP

Omaha, Nebraska,
October 30, 2014.

Management's Discussion and Analysis
June 30, 2014 and 2013

Our discussion and analysis of Hawarden Regional Healthcare's financial performance provides an overview of the Hospital's financial activities for the fiscal years ended June 30, 2014 and 2013. Please read it in conjunction with the Hospital's financial statements, which begin on page 7.

Financial Highlights

The Hospital's net position for 2014 was \$548,195 or a 8.9% decrease from 2013. The Hospital's net position in 2013 was \$602,133 or a 12.5% from 2012. The Hospital reported operating income in 2014 of \$329,794 which was a \$33,847 increase from 2013. The operating income in 2013 decreased by \$431,574 from the income reported in 2012 of \$727,521.

Operating revenues increased by \$33,847 or 1.1% over the revenues reported in 2013. 2013 operating revenue decreased by \$431,574 or 59.3% over the revenues reported in 2012.

Nonoperating revenues and restricted gifts received decreased by \$110,046 or 38.8% in 2014 compared to an increase of \$8,164 or 2.7% in 2013 and an increase of \$44,505 or 17.6% in 2012 compared to 2011.

Using This Annual Report

The Hospital's financial statements consist of three statements; a Statement of Financial Position (Balance Sheet); a Statement of Revenue, Expenses, and Changes in Net Position; 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 Statement of Financial Position and Statement of Revenue, Expenses, and Changes in Net Position

Our analysis of the Hospital finances begins on page 5. The Statement of Financial Position and the Statement of Revenue, Expenses, and Changes in Net Position report information about the Hospital's resources and its activities in a way that helps answer the question of whether the Hospital, as a whole, is better or worse off as a result of the year's activities. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenue and expenses are taken into account regardless of when cash is received or paid.

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

The 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.

The Hospital's Net Position

The Hospital's net position is the difference between its assets and liabilities reported in the Balance Sheet on page 5. The Hospital's net position increased in each of the past two years by \$448,195 (8.3%) in 2014 and \$602,133 (12.5%) in 2013, as you can see from **Table 1**.

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Management's Discussion and Analysis
June 30, 2014 and 2013

Table 1: Assets, Liabilities, and Net Assets

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Assets:			
Current assets	\$ 4,151,018	3,894,106	4,595,615
Capital assets, net	2,172,256	1,267,324	1,389,486
Other noncurrent assets	1,373,817	1,459,815	541,578
Total assets	\$ 7,697,091	6,621,245	6,526,679
Liabilities:			
Long-term debt outstanding	\$ 918,468	775,000	--
Other current and noncurrent liabilities	823,963	438,752	1,718,089
Total liabilities	\$ 1,742,431	1,213,752	1,718,089
Net Position:			
Net investment in capital assets	\$ 1,253,788	492,324	1,389,486
Expendable for capital acquisitions and operating activities	134,695	89,680	67,157
Nonexpendable permanent endowments	96,123	96,123	96,123
Unrestricted	4,479,095	4,737,379	3,260,607
Total net position	\$ 5,963,701	5,415,506	4,813,373

In 2014, the total assets increased by \$1,075,846. The change was due to the increase in Capital assets, which was primarily a result in asset acquisitions relating to a new CT Scanner and Electronic Health Record equipment and software.

In 2014, the total liabilities increased by \$528,679. This change was a result of the estimated amount due to estimated third party payor settlements as well as the purchase of a new CT Scanner.

Operating Results and Changes in The Hospital's Net Position

In 2013, the Hospital's net position decreased by \$548,195 (8.9%), as shown in **Table 2**. This increase is made up of very different components.

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Management's Discussion and Analysis
June 30, 2014 and 2013

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

	2014	2013	2012
Operating Revenue:			
Net patient service revenue	\$ 6,456,610	6,886,259	7,255,445
Provision for bad debt	(364,240)	(296,572)	(602,900)
Other operating revenues	1,502,265	703,539	723,729
Loss on sale of property and equipment	(26,649)	(93,856)	--
Total operating revenue	7,567,986	7,199,370	7,376,274
Operating Expenses:			
Salaries and benefits	3,635,868	2,977,596	2,955,662
Purchased services and other	3,210,913	3,646,669	3,438,276
Depreciation and amortization	391,359	278,808	254,144
Interest	52	350	671
Total operating expenses	7,238,192	6,903,423	6,648,753
Operating income (loss)	329,794	295,947	727,521
Nonoperating Revenues (Expenses)			
Joint venture and clinic investment loss, net	(125,125)	(38,947)	(15,085)
Investment income	6,214	12,690	12,310
Sales tax revenue	292,197	307,775	278,233
Gifts, grants and contributions, net	45,115	24,668	22,564
Total nonoperating revenue (expenses), net	218,401	306,186	298,022
Increase in net position	548,195	602,133	1,025,543
Net position beginning of year	5,415,506	4,813,373	3,787,830
Net position end of year	\$ 5,963,701	5,415,506	4,813,373

Nonoperating Revenues and Expenses

Nonoperating revenues consist primarily of local option sales taxes, interest revenue, investment earnings and gifts, grants and bequests for the purchase of property and equipment.

The loss for the joint venture and clinic investment was \$(125,125) in 2014 compared to \$(38,947) in 2013. We continue to fund the clinic as part of our mission to provide for the health and wellness of all the people in our community.

Management's Discussion and Analysis
June 30, 2014 and 2013

The Hospital's Cash Flows

Changes in the Hospital's cash flows are consistent with changes in operating income and nonoperating revenues and expenses, discussed earlier. Cash flows provided by operating activities in 2014 increased compared to 2013 due to a increase in cash received from patients and third party payors.

Capital Asset and Debt Administration

Capital Assets

As of end of the year 2013, the Hospital had \$2,172,256 invested in capital assets, net of accumulated depreciation, as compared to \$1,267,324 in 2013 and \$1,389,486 in 2012, as detailed in Note 7 of the financial statements. In 2014, the hospital purchased depreciable capital assets costing \$1,006,484 compared to \$44,293 being spent in 2013. Some of the major purchases the Hospital made were a boiler system for \$33,317, CT Scanner for \$273,436, new phone system for \$77,404 and \$583,055 for Electronic Health Records.

Debt

As of end of the year 2014, the Hospital had loans and a capital lease obligations that were outstanding. This includes a purchase agreement with Therapeutic Health Services to purchase a clinic that will provide physical and occupational therapy services for the Hospital. This agreement includes annual payments to be made through fiscal year 2020. The Hospital also entered into a Capital Lease agreement for a CT Scanner in the amount of \$264,750. This agreement has monthly payment to be made thru fiscal year 2018. The Hospital's formal debt issuances, revenue notes, cannot be issued without approval of the Board of Directors.

Contacting the Hospital's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the CEO, at Hawarden Regional Healthcare, 1111 11th Street, Hawarden, Iowa 51023.

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Statements of Financial Position
June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,377,107	1,473,091
Receivables -		
Patients, net of allowance for doubtful accounts of \$433,310 in 2014 and \$549,393 in 2013	1,788,682	1,436,064
Due from related party, net	540,237	396,470
Other	88,463	91,067
Inventories	135,538	102,244
Prepaid expenses	125,686	95,170
Estimated third-party payor settlements	<u>95,305</u>	<u>300,000</u>
Total current assets	<u>4,151,018</u>	<u>3,894,106</u>
Assets limited as to use -		
By board for capital improvements and endowments	547,733	526,497
By donor	<u>100,042</u>	<u>101,026</u>
	<u>647,775</u>	<u>627,523</u>
Capital assets, net	2,172,256	1,267,324
Other assets, net	<u>9,041</u>	<u>8,013</u>
Total assets	<u>6,980,090</u>	<u>5,796,966</u>
DEFERRED OUTFLOWS OF RESOURCES		
Intangible asset, net	<u>726,042</u>	<u>832,292</u>
LIABILITIES		
Current liabilities:		
Current portion of long-term debt	155,538	75,000
Accounts payable -		
Mercy	101,165	65,792
Capital assets	208,152	--
Trade	231,881	68,290
Salaries, wages and accrued benefits payable	250,322	201,778
Payroll taxes withheld and accrued	19,150	45,587
Other accrued liabilities	<u>13,293</u>	<u>57,305</u>
Total current liabilities	<u>979,501</u>	<u>513,752</u>
Long-term debt, net of current portion	<u>762,930</u>	<u>700,000</u>
Total liabilities	<u>1,742,431</u>	<u>1,213,752</u>
NET POSITION		
Net investment in capital assets	1,253,788	492,324
Restricted:		
Expendable for capital acquisitions and operating activities	134,695	89,680
Nonexpendable permanent endowments	96,123	96,123
Unrestricted	<u>4,479,095</u>	<u>4,737,379</u>
Total net position	<u>\$ 5,963,701</u>	<u>5,415,506</u>

See notes to financial statements

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

**Statements of Revenue, Expenses and Changes in Net Position
For the Years Ended June 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
OPERATING REVENUE:		
Net patient service revenue before provision for bad debt	\$ 6,456,610	6,886,259
Provision for bad debts	(364,240)	(296,572)
Net patient service revenue	6,092,370	6,589,687
Other operating revenue	1,502,265	703,539
Loss on sale of capital assets	(26,649)	(93,856)
Total operating revenue	<u>7,567,986</u>	<u>7,199,370</u>
OPERATING EXPENSES:		
Salaries and wages	2,877,158	2,355,669
Employee benefits	758,710	621,927
Purchased services and professional fees	2,185,583	2,367,969
Utilities	90,167	71,850
Supplies and other expenses	850,284	1,138,659
Depreciation and amortization	391,359	278,808
Insurance	84,879	68,191
Interest	52	350
Total operating expenses	<u>7,238,192</u>	<u>6,903,423</u>
OPERATING INCOME	<u>329,794</u>	<u>295,947</u>
NONOPERATING REVENUE (EXPENSE):		
Joint venture and clinic investment loss, net	(125,125)	(38,947)
Investment income	6,214	12,690
Sales tax revenue	292,197	307,775
Noncapital grants and contributions	100	1,914
Nonoperating revenue, net	<u>173,386</u>	<u>283,432</u>
EXCESS OF REVENUE OVER EXPENSES BEFORE CAPITAL GRANTS AND CONTRIBUTIONS	503,180	579,379
CAPITAL GRANTS AND CONTRIBUTIONS	<u>45,015</u>	<u>22,754</u>
INCREASE IN NET POSITION	548,195	602,133
NET POSITION, beginning of year	<u>5,415,506</u>	<u>4,813,373</u>
NET POSITION, end of year	<u>\$ 5,963,701</u>	<u>5,415,506</u>

See notes to financial statements

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Statements of Cash Flows
For the Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from patients and third party payors	\$ 5,944,447	5,123,929
Cash paid for employee salaries and benefits	(3,613,761)	(2,953,809)
Cash paid to suppliers and contractors	(3,117,167)	(3,655,535)
Other receipts and payments, net	<u>1,358,498</u>	<u>718,133</u>
Net cash provided by (used in) operating activities	<u>572,017</u>	<u>(767,282)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Sales tax received	292,197	307,775
Noncapital grants and contributions	<u>100</u>	<u>1,914</u>
Net cash provided by noncapital financing activities	<u>292,297</u>	<u>309,689</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of capital assets, net	(743,788)	(232,794)
Capital grants and contributions	45,015	22,754
Payments on purchase agreement	(75,000)	(75,000)
Payments on capital lease obligations	(46,282)	--
Interest paid on long-term debt and capital lease obligations	<u>(52)</u>	<u>(350)</u>
Net cash used in capital and related financing activities	<u>(820,107)</u>	<u>(285,390)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Joint venture and clinic investment loss, net	(125,125)	(38,947)
Deposits to assets limited as to use	(20,252)	(85,945)
Investment income	6,214	12,690
Withdrawals to other assets	<u>(1,028)</u>	<u>(3,230)</u>
Net cash used in investing activities	<u>(140,191)</u>	<u>(115,432)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(95,984)	(858,415)
CASH AND CASH EQUIVALENTS - beginning of year	<u>1,473,091</u>	<u>2,331,506</u>
CASH AND CASH EQUIVALENTS - end of year	<u>\$ 1,377,107</u>	<u>1,473,091</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Capital asset additions acquired with capital lease obligations	<u>\$ 264,750</u>	<u>--</u>
Seller financed note	<u>\$ --</u>	<u>850,000</u>

See notes to financial statements

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Statements of Cash Flows (Continued)
For the Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:		
Operating gain	\$ 329,794	295,947
Adjustments to reconcile operating income to net cash provided by (used in) operating activities -		
Depreciation and amortization	391,359	278,808
Interest expense	52	350
Loss on sale of capital assets	26,649	93,856
(Increase) decrease in current assets -		
Receivables -		
Patients	(352,618)	54,976
Due from related party	(143,767)	14,594
Other	2,604	77,078
Inventories	(33,294)	1,707
Prepaid expenses	(30,516)	(5,261)
Estimated third-party payor settlements	204,695	(300,000)
Increase (decrease) in current liabilities -		
Accounts payable -		
Mercy	35,373	11,305
Trade	163,591	(47,058)
Salaries, wages and accrued benefits payable	48,544	25,463
Payroll taxes withheld and accrued	(26,437)	(1,676)
Other accrued liabilities	(44,012)	(46,637)
Estimated third-party payor settlements	--	(1,220,734)
Net cash provided by (used in) operating activities	<u>\$ 572,017</u>	<u>(767,282)</u>

See notes to financial statements

Notes to Financial Statements
June 30, 2014 and 2013

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

The following is a summary of significant accounting policies of Hawarden Regional Healthcare (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 financial statements of the Hospital are used to account for the provisions of acute hospital and physician clinic services to the residents of the City of Hawarden and the surrounding area.

The Hospital's financial statements are an integral part of the City of Hawarden, Iowa. The accompanying financial statements are not intended to present fairly the financial position and changes in financial position of the City of Hawarden, 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. During fiscal year 2000, the Hawarden Regional Healthcare Board of Trustees approved the Health Services' plan to obtain Critical Access Hospital (CAH) designation. CAH's are acute care facilities that provide emergency, outpatient and short-term inpatient services. Medicare reimburses CAH's on a reasonable cost basis.

The Hospital's application to become certified as a CAH was approved by the Iowa Department of Public Health and the certification was effective November 2, 2000.

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 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.

Notes to Financial Statements
June 30, 2014 and 2013

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

C. *Basis of Presentation*

The statements of net position display the Hospital's assets and liabilities, with the differences reported as net position. Net position is reported in three categories:

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

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

Unrestricted – This component of net position consists of net position items not meeting the definition of the two preceding categories. Unrestricted net positions often have constraints on resources imposed by management which can be removed or modified.

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

D. *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. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

E. *Basis of Accounting and Accounting Standards*

The Hospital's financial statements are presented on the accrual basis of accounting. Revenue is recognized when earned, expenses are recognized when incurred.

The Hospital's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is primarily responsible for establishing GAAP for state and local governments through its pronouncements. Governments had been also required to follow the statements and interpretations of the Financial Accounting Standards Board, Accounting Principles Board opinions, and Accounting Research Bulletins issued through November 30, 1989, that do not conflict with or contradict GASB pronouncements. In December 2010, GASB issued statement No. 62 which incorporated all relevant guidance in GASB standards.

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.

Notes to Financial Statements
June 30, 2014 and 2013

G. Patient Receivables, Net

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

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

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

H. Inventories

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

I. Assets Limited as to Use

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

By Donor – These funds are restricted for specified purposes as directed by the grantor or donor.

J. 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.

K. Capital Assets

Capital assets acquisitions in excess of \$5,000 are capitalized and recorded at cost. Depreciation is computed using the straight-line method based upon useful lives set forth using general guidelines from the American Hospital Association Guide for Estimated Useful Lives of Depreciable Hospital Assets. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in the depreciation and amortization in the financial statements.

Lives range by capital asset classification as follows:

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

The Hospital's capital 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.

Notes to Financial Statements
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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.

L. Intangible Assets

Intangible assets are recorded at cost, less accumulated amortization. Amortization on finite-lived intangible assets is calculated on a straight-line basis over the estimated life of the asset.

M. Compensated Absences

Paid time off (PTO) vests and may be carried forward by an employee in an amount not to exceed 240 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. Accrued PTO payable at June 30, 2014 and 2013 was \$175,930 and \$143,670, respectively.

N. Statement of Revenue, Expenses and Changes in Net Position

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

O. 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 per discharge, reimbursed costs, discounted charges and per diem payments. 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.

P. 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 that are restricted to a specific operating purpose are reported as nonoperating revenue. Amounts restricted to capital acquisitions are reported after nonoperating revenue and expenses.

Q. 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 in the statements of revenue, expenses and changes in net position.

Notes to Financial Statements
June 30, 2014 and 2013

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.

R. Sales Tax Revenue

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

S. Income Taxes

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

T. 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.

U. Reclassifications

Certain amounts in the 2013 financial statements have been reclassified to conform to the 2014 format.

V. Subsequent Events

The Hospital considered events occurring through October 30, 2014 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

The Hospital's deposits in banks at June 30, 2014 and 2013 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 instrumentality's; 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; and certain joint investment trusts, and warrants or improvement certificates of a drainage district.

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

Credit Risk: The Hospital's investments are categorized to give an indication of the level of risk assumed by the Hospital at year end. The Hospital's investments are all category 1 which means that the investments are insured or registered or the securities are held by the Hospital or its agent in the Hospital's name.

Notes to Financial Statements
June 30, 2014 and 2013

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

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.

Investment return, including return on assets limited as to use, for the years ended June 30, 2014 and 2013 is included in investment income on the statements of revenue, expenses and changes in net position.

(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 payers follows:

Medicare. Inpatient acute care services rendered to Medicare program beneficiaries in a Critical Access Hospital are paid based on Medicare defined costs of providing the services. Inpatient nonacute services, certain outpatient services and certain rural health clinic services related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed on a prospectively determined rate per episode for home care services rendered to Medicare beneficiaries. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor. The Hospital's Medicare cost reports have been audited by the Medicare Administrative Contractor through June 30, 2012.

The "Budget Control Act of 2011" requires, among other things, mandatory across-the-board reductions in Federal spending, also known as sequestration. The "American Taxpayer Relief Act of 2012" postponed sequestration for two months. As required by law, President Obama issued a sequestration order on March 1, 2013. In general, Medicare claims with dates of service or dates of discharge on or after April 1, 2013, will incur a two percent reduction in Medicare payment.

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.

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

Hawarden Regional Healthcare
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Notes to Financial Statements
June 30, 2014 and 2013

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

	<u>2014</u>	<u>2013</u>
Gross patient service revenue		
Inpatient services and swing bed	\$ 1,760,267	1,231,855
Outpatient	<u>8,028,812</u>	<u>8,220,734</u>
Total gross patient service revenue	<u>9,789,079</u>	<u>9,452,589</u>
Deductions from gross patient service revenue		
Medicare	2,339,400	1,352,743
Medicaid	287,643	164,275
Other payors	643,651	932,442
Charity care	<u>61,775</u>	<u>116,870</u>
Total deductons from gross patient service revenue	<u>3,332,469</u>	<u>2,566,330</u>
Net patient service revenue before provision for bad debt	<u>\$ 6,456,610</u>	<u>6,886,259</u>

The Hospital reports net patient services revenue at estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period 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 accounted for approximately 56% and 7%, respectively, of the Hospital's net patient revenue for the year ended June 30, 2014 compared to 52% and 6%, respectively in 2013. 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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Notes to Financial Statements
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(4) Other Revenue

Other revenue for the years ended June 30, 2014 and 2013, consisted of the following:

	<u>2014</u>	<u>2013</u>
Electronic health records incentive payments	\$ 687,134	130,578
Services provided to clinic	435,825	412,966
Outsourced physical therapy revenue	240,816	--
Medical office building rent	27,600	27,600
Medical records transcript fee	21,720	20,586
Specialty clinic rent	16,381	18,514
MediMate	14,824	13,996
Other	14,541	13,473
Occupational health consulting	11,371	5,038
Meals	8,452	7,524
Purchasing rebates	7,994	5,601
HRSA grant	7,943	30,936
Ambulance service fee billing revenue	3,220	13,300
Wellness center dues	2,548	1,730
Vending	1,896	1,697
	<u>\$ 1,502,265</u>	<u>703,539</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 2013 the Hospital qualified for the financial incentives payments by attesting it met specific criteria set by the Center for Medicare and Medicaid services (CMS). Management's attestation is subject to audit by the federal government or its designee.

(5) Composition of Patient Receivables

Patient receivables as of June 30, 2014 and 2013 consist of the following:

	<u>2014</u>	<u>2013</u>
Patient accounts receivable	\$ 2,383,992	2,150,457
Less estimated third-party contractual adjustments	(162,000)	(120,000)
Less allowance for uncollectibles	<u>(433,310)</u>	<u>(594,393)</u>
	<u>\$ 1,788,682</u>	<u>1,436,064</u>

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June 30, 2014 and 2013

The Hospital is located in Hawarden, Iowa. The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The approximate mix of receivables from patients and third-party payors was as follows:

	<u>2014</u>	<u>2013</u>
Medicare	40%	47%
Medicaid	12	6
Blue Cross Blue Shield	10	7
Other third-party payors	18	21
Private pay	20	19
	<u>100%</u>	<u>100%</u>

(6) Assets Limited as to Use

Cash deposits and investments designated by the Board for future capital improvements, and endowments as of June 30, 2014 and 2013, are summarized as follows:

	<u>2014</u>	<u>2013</u>
Capital Improvements and Endowments -		
Cash	\$ 526,992	478,480
Certificates of deposit	20,741	48,017
	<u>547,733</u>	<u>526,497</u>

Cash deposits and investments restricted by donor for future capital improvements, and endowments as of June 30, 2014 and 2013, are summarized as follows:

	<u>2014</u>	<u>2013</u>
Capital Improvements and Endowments -		
Certificates of deposit	\$ 100,042	101,026

(7) Capital Assets, Net

Capital asset additions, retirements and balances as of June 30, 2014 and 2013, are summarized as follows:

Hawarden Regional Healthcare
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Notes to Financial Statements
June 30, 2014 and 2013

	<u>June 30, 2013</u>	<u>Additions</u>	<u>Transfers and Disposals</u>	<u>June 30, 2014</u>
Capital assets, not being depreciated:				
Land	\$ 172,313	--	--	172,313
Construction in progress	258,009	870,666	(660,460)	468,215
Total capital assets, not being depreciated	<u>430,322</u>	<u>870,666</u>	<u>(660,460)</u>	<u>640,528</u>
Capital assets, being depreciated:				
Land improvements	54,997	--	--	54,997
Hospital buildings	1,556,820	--	--	1,556,820
Fixed equipment	586,705	33,317	--	620,022
Major moveable equipment	2,112,871	390,112	(615,755)	1,887,228
Electronic health record - non-meaningful use	5,473	--	--	5,473
Electronic health record - meaningful use	132,540	583,055	(89,102)	626,493
Total capital assets, being depreciated	<u>4,449,406</u>	<u>1,006,484</u>	<u>(704,857)</u>	<u>4,751,033</u>
Less accumulated depreciation:				
Land improvements	35,816	1,794	--	37,610
Hospital buildings	1,199,176	36,703	--	1,235,879
Fixed equipment	438,171	26,543	--	464,714
Major moveable equipment	1,873,167	149,467	(607,100)	1,415,534
Electronic health record - non-meaningful use	18,040	912	(12,325)	6,627
Electronic health record - meaningful use	48,034	69,690	(58,783)	58,941
Total accumulated depreciation	<u>3,612,404</u>	<u>285,109</u>	<u>(678,208)</u>	<u>3,219,305</u>
Total capital assets, being depreciated, net	<u>837,002</u>	<u>721,375</u>	<u>(26,649)</u>	<u>1,531,728</u>
Total capital assets, net	<u>\$ 1,267,324</u>	<u>1,592,041</u>	<u>(687,109)</u>	<u>2,172,256</u>
	<u>June 30, 2012</u>	<u>Additions</u>	<u>Transfers and Disposals</u>	<u>June 30, 2013</u>
Capital assets, not being depreciated:				
Land	\$ 234,912	31,257	(93,856)	172,313
Construction in progress	264,744	157,243	(163,978)	258,009
Total capital assets, not being depreciated	<u>499,656</u>	<u>188,500</u>	<u>(257,834)</u>	<u>430,322</u>
Capital assets, being depreciated:				
Land improvements	54,997	--	--	54,997
Hospital buildings	1,556,820	--	--	1,556,820
Fixed equipment	566,300	20,405	--	586,705
Major moveable equipment	2,063,017	23,889	25,965	2,112,871
Electronic health record - non-meaningful use	--	--	5,473	5,473
Electronic health record - meaningful use	--	--	132,540	132,540
Total capital assets, being depreciated	<u>4,241,134</u>	<u>44,294</u>	<u>163,978</u>	<u>4,449,406</u>
Less accumulated depreciation:				
Land improvements	34,023	1,793	--	35,816
Hospital buildings	1,162,630	36,546	--	1,199,176
Fixed equipment	424,275	13,896	--	438,171
Major moveable equipment	1,730,376	142,791	--	1,873,167
Electronic health record - non-meaningful use	--	18,040	--	18,040
Electronic health record - meaningful use	--	48,034	--	48,034
Total accumulated depreciation	<u>3,351,304</u>	<u>261,100</u>	<u>--</u>	<u>3,612,404</u>
Total capital assets, being depreciated, net	<u>889,830</u>	<u>(216,806)</u>	<u>163,978</u>	<u>837,002</u>
Total capital assets, net	<u>\$ 1,389,486</u>	<u>(28,306)</u>	<u>(93,856)</u>	<u>1,267,324</u>

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Notes to Financial Statements
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Construction in progress consists of computer software and other miscellaneous costs. These items are to be paid for out of operations.

(8) Intangible Assets, Net

A summary of intangible assets at June 30, 2014 and 2013 is as follows:

	<u>2014</u>	<u>2013</u>
Non-compete agreements	\$ 850,000	850,000
Less accumulated amortization	<u>(123,958)</u>	<u>(17,708)</u>
Intangible assets, net	<u>\$ 726,042</u>	<u>832,292</u>

The noncompete agreements are being amortized over the term of the payment period for the purchase of Therapeutic Health Service, Inc (THS). Amortization for the years ended June 30, 2014 and 2013 was \$106,250 and \$17,708, respectively, and is included in the statements of revenue, expenses and changes in net position.

(9) Mercy Accounts Payable

Mercy accounts payable includes amounts due to Mercy Medical Services and Mercy Medical Center related to the Hospital's portion of financial support for the Hawarden Mercy Medical Clinic and Ireton Community Clinic and other professional and management fees. Mercy accounts payable as of June 30, 2014 and 2013 is summarized as follows:

	<u>2014</u>	<u>2013</u>
Mercy Medical Services for share of Hawarden Mercy Medical Clinic and Ireton Community Clinic operating support	\$ 50,823	21,599
Mercy Medical Center for professional and management services	<u>50,342</u>	<u>44,193</u>
	<u>\$ 101,165</u>	<u>65,792</u>

(10) Long-Term Obligations

A summary of long-term obligations at June 30, 2014 and 2013 follows:

	<u>June 30, 2013</u>	<u>Borrowings</u>	<u>Payments</u>	<u>June 30, 2014</u>	<u>Due Within One Year</u>
Capital lease obligations (A)	\$ --	264,750	(46,282)	218,468	55,538
Interest free loan financed by the seller (B)	<u>775,000</u>	<u>--</u>	<u>(75,000)</u>	<u>700,000</u>	<u>100,000</u>
	<u>\$ 775,000</u>	<u>264,750</u>	<u>(121,282)</u>	<u>918,468</u>	<u>155,538</u>
	<u>June 30, 2012</u>	<u>Borrowings</u>	<u>Payments</u>	<u>June 30, 2013</u>	<u>Due Within One Year</u>
Interest free loan financed by the seller (B)	\$ --	850,000	(75,000)	775,000	75,000
	<u>\$ --</u>	<u>850,000</u>	<u>(75,000)</u>	<u>775,000</u>	<u>75,000</u>

Notes to Financial Statements
June 30, 2014 and 2013

- (A) During 2014, the Hospital entered into a capital lease obligation at an imputed interest rate of .99%. Monthly payments of \$4,628 are to be made thru August 2014, and are collateralized by leased equipment with a cost of \$264,750.
- (B) On May 8, 2013, the Hospital entered into an asset purchase agreement with THS, a provider of physical and occupational health services and home health services in Northwest Iowa. The agreement was for the purchase of all contracts and contract rights of THS, equipment, fixtures, office equipment owned and utilized by THS in connection with the aforementioned contracts, inventory and therapy supplies used in connection with the contracts, and service records, marketing material and agreements relating to the acquired contracts and medical practice. THS agreement included a noncompete clause for the term of the payment period. The purchase agreement was for \$850,000 with the first payment of \$75,000 paid upon the closing of the agreement. Subsequent payments are due on January 10 of each year for varying amounts. The final payment in the amount of \$150,000 is due on January 10, 2019.

A summary of the Hospital's future principal and interest payments as of June 30, 2014 is as follows:

		Seller Financed Note		Capital Lease		Total	
		Principal	Interest	Principal	Interest	Principal	Interest
2015	\$	100,000	--	55,538	3,106	155,538	3,106
2016		100,000	--	55,538	3,106	155,538	3,106
2017		100,000	--	55,538	3,106	155,538	3,106
2018		100,000	--	51,855	3,106	151,855	3,106
2019		150,000	--	--	515	150,000	515
2020		150,000	--	--	--	150,000	-
	\$	<u>700,000</u>	<u>-</u>	<u>218,469</u>	<u>12,939</u>	<u>918,469</u>	<u>12,939</u>

(11) Professional Liability Insurance

The Hospital carries a professional liability policy (including malpractice) providing coverage of \$1,000,000 for injuries per occurrence and \$3,000,000 aggregate coverage. In addition, the Hospital carries an umbrella policy which also provides \$2,000,000 per occurrence and aggregate coverage. These policies provide coverage on a claims-made basis covering only those claims which have occurred and are reported to the insurance company while the coverage is in force. In the event the Hospital should elect not to purchase insurance from the present carrier or the carrier should elect not to renew the policy, any unreported claims which occurred during the policy year may not be recoverable from the carrier.

Accounting principles generally accepted in the United States of America require a healthcare provider to recognize the ultimate costs of malpractice claims or similar contingent liabilities, which include costs associated with litigating or settling claims, when the incidents that give rise to the claims occur. The Hospital does evaluate all incidents and claims along with prior claim experienced to determine if a liability is to be recognized. For the years ending June 30, 2014 and 2013, management determined no liability should be recognized for asserted or unasserted claims. Management is not aware of any such claim that would have a material adverse impact on the accompanying financial statements.

(12) Employee Retirement and Defined Benefit 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 50360-9117.

Notes to Financial Statements
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Plan members are required to contribute 5.95% and 5.78% of their annual salary and the Hospital is required to contribute 8.93% and 8.67% of annual covered payroll for the years ended June 30, 2014 and 2013, respectively. Contribution requirements are established by State statute. The Hospital's contribution to IPERS for the years ended June 30, 2014, 2013 and 2012 were \$258,473, \$190,450, and \$185,618, respectively, equal to the required contributions for each year.

(13) Related Party Transactions

Effective January 1, 2005, the Hospital and Mercy Medical Services (MMS) entered into a joint venture whereby each partner has a 50% sponsorship interest in Hawarden Regional Healthcare Clinics, LLC. (HRHC). The Hospital and MMS share equally in the net income (loss) of HRHC. HRHC operates clinics in Hawarden and Ireton, Iowa.

Hawarden Clinic

The Hospital's share of Hawarden Clinic's (HC) 2014 and 2013 operating loss was \$101,211 and \$31,136, respectively, and is included in joint venture loss, net in the accompanying statements of revenue, expenses and changes in net position.

The Hospital hires the employees of HC and leases them back to HC. Amounts received by the Hospital for expenses paid in 2014 and 2013 was \$387,527 and \$303,693, respectively, and is included in the accompanying statements of revenue, expenses and changes in net position. The Hospital also received management fees from HC totaling \$50,000 in 2014 and 2013, and monthly rent totaling \$27,600 for the years ended June 30, 2014 and 2013. These amounts are included in other revenue.

HC owed the Hospital \$558,545 and \$401,848 at June 30, 2014 and 2013, respectively. These amounts are recorded in due from related party on the statement of financial position.

Ireton Clinic

The Hospital's share of Ireton Clinic's (IC) 2014 and 2013 operating loss was \$23,914 and \$7,811, respectively, and is included in joint venture loss, net in the accompanying statements of revenue, expenses and changes in net position.

The Hospital hires the employees of IC and leases them back to IC. Amounts received by the Hospital for expenses paid in 2014 and 2013 was \$50,716 and \$49,861, respectively, and is included in the accompanying statements of revenue, expenses and changes in net position. The Hospital also received management fees from IC totaling \$10,000 in 2014 and 2013. These fees are included in other revenue.

The Hospital owed IC \$18,308 and \$5,378 at June 30, 2014 and 2013, respectively. These amounts are recorded in due from related party on the statement of financial position.

See Note 9 regarding amounts due Mercy Medical Services.

(14) Subsequent Events

On August 21, 2014, the Hospital issued \$500,000 of Hospital Revenue Project Notes, Series 2014A and \$5,500,000 Bank Note, Series 2014B. Both notes are available for periodic draws as project costs are incurred. The Hospital approved an \$11.3 million expansion and renovation project in the fall of 2013 to be funded through existing reserves and interim construction financing. Upon completion of the project, the final financing will be provided through a combination of USDA direct loan proceeds of \$8.8 million and \$2.0 million of bank qualified revenue bonds. The project is underway and will be completed in various phases over the next two years.

Patient Service Revenue
For the Years Ended June 30, 2014 and 2013

	2014				2013			
	Inpatient	Outpatient	Swing Bed	Total	Inpatient	Outpatient	Swing Bed	Total
NURSING SERVICES:								
Medical, surgical and obstetrics	\$ 223,673	611,644	--	835,317	255,047	538,165	--	793,212
Swing bed	--	--	503,895	503,895	--	--	266,156	266,156
Observation	--	64,958	--	64,958	--	76,511	--	76,511
	<u>223,673</u>	<u>676,602</u>	<u>503,895</u>	<u>1,404,170</u>	<u>255,047</u>	<u>614,676</u>	<u>266,156</u>	<u>1,135,879</u>
OTHER PROFESSIONAL SERVICES:								
Radiology	61,226	1,834,638	15,739	1,911,603	78,772	1,750,410	7,916	1,837,098
Laboratory	43,072	1,307,975	29,286	1,380,333	56,304	1,265,839	22,235	1,344,378
Physical therapy	17,207	963,685	122,510	1,103,402	15,412	949,457	87,873	1,052,742
Pharmacy	103,945	1,355,466	275,020	1,734,431	116,727	1,705,241	103,284	1,925,252
Emergency and outpatient service	2,992	697,547	3,867	704,406	9,182	751,613	701	761,496
Professional fees	51,078	313,387	2,679	367,144	49,731	333,771	2,379	385,881
Gastro-Intestinal	--	216,038	--	216,038	--	237,646	--	237,646
Respiratory therapy	65,663	73,201	61,039	199,903	588	57,371	311	58,270
Electrocardiology	3,267	147,486	1,200	151,953	8,422	148,658	1,200	158,280
Central services and supply	45,560	118,447	85,303	249,310	53,040	104,503	70,376	227,919
Cardiac rehab	--	75,553	--	75,553	--	74,421	--	74,421
Occupational therapy	1,425	107,998	36,225	145,648	825	64,224	16,725	81,774
Speech therapy	996	92,066	3,400	96,462	629	66,024	8,020	74,673
Anesthesiology	--	17,125	--	17,125	--	38,074	--	38,074
Operating and recovery rooms	--	24,142	--	24,142	--	47,593	--	47,593
Dietary consulting	--	7,456	--	7,456	--	11,213	--	11,213
	<u>396,431</u>	<u>7,352,210</u>	<u>636,268</u>	<u>8,384,909</u>	<u>389,632</u>	<u>7,606,058</u>	<u>321,020</u>	<u>8,316,710</u>
GROSS PATIENT SERVICE REVENUE	<u>\$ 620,104</u>	<u>8,028,812</u>	<u>1,140,163</u>	<u>9,789,079</u>	<u>644,679</u>	<u>8,220,734</u>	<u>587,176</u>	<u>9,452,589</u>
LESS:								
Contractual allowances and other deductions, primarily Medicare and Medicaid				<u>(3,332,469)</u>				<u>(2,566,330)</u>
NET PATIENT SERVICE REVENUE BEFORE PROVISION FOR BAD DEBT				<u>\$ 6,456,610</u>				<u>6,886,259</u>

See accompanying independent auditor's report

Other Operating Revenue
For the Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
CMS electronic health records incentive payments	\$ 583,055	--
Services provided to clinic	435,825	412,966
Outsourced physical therapy revenue	240,816	--
State of Iowa electronic health records incentive payments	103,151	130,578
Medical office building rent	27,600	27,600
Medical records transcript fee	21,720	20,586
Specialty clinic rent	16,381	18,514
MediMate	14,824	13,996
Other	14,143	13,473
Occupational health consulting	12,697	5,038
Meals	8,452	7,524
Purchasing rebates	7,994	5,601
HRSA grant	7,943	30,936
Ambulance service fee billing revenue	3,220	13,300
Vending	1,896	1,697
Wellness center dues	2,548	1,730
	<u>\$ 1,502,265</u>	<u>703,539</u>

See accompanying independent auditor's report

Department Expenses
For the Years Ended June 30, 2014 and 2013

	2014				2013			
	Salaries and Wages	Professional Fees and Purchased Services	Supplies and Other	Total	Salaries and Wages	Professional Fees and Purchased Services	Supplies and Other	Total
NURSING SERVICES:								
Medical and surgical	\$ 872,176	43,363	69,123	984,662	779,812	54,646	144,796	979,256
Observation	2,442	--	--	2,442	6,356	--	--	6,356
	<u>874,618</u>	<u>43,363</u>	<u>69,123</u>	<u>987,104</u>	<u>786,168</u>	<u>54,646</u>	<u>144,796</u>	<u>985,612</u>
OTHER PROFESSIONAL SERVICES:								
Physical therapy	535,295	3,538	12,752	551,585	131,090	432,874	23,077	587,041
Emergency room	33,841	870,184	222	904,247	33,519	836,987	--	870,506
Laboratory	199,872	186,486	92,546	478,904	194,884	187,327	105,968	488,179
Radiology	125,591	200,145	22,681	348,417	80,649	241,351	25,288	347,288
Hawarden community clinic	303,555	--	136	303,691	277,130	--	--	277,130
Pharmacy	8,362	41,073	369,315	418,750	12,022	37,572	542,174	591,768
Medical records	127,075	106,305	6,067	239,447	119,891	46,370	22,574	188,835
Respiratory therapy	90	16,100	7,136	23,326	293	16,250	5,447	21,990
Outpatient clinic	46,056	--	1,309	47,365	45,295	--	883	46,178
Central services and supply	27,234	--	5,431	32,665	1,390	--	48,359	49,747
Gastro-Intestinal	2,741	--	2,829	5,570	4,763	--	11,175	15,938
Occupational therapy	--	5,935	603	6,538	--	47,950	65	48,015
Intravenous therapy	7,232	--	--	7,232	19,361	--	--	19,361
Electrocardiology	10	3,650	--	3,660	548	5,148	--	5,696
Cardiac rehab	35,289	--	256	35,545	46,786	--	5,270	52,055
Home health	--	12,655	--	12,655	--	14,150	--	14,150
Occupation health	2,414	--	580	2,994	685	--	238	923
Operating and recovery room	(26)	18,794	11,265	30,033	1,291	10,976	2,250	14,517
Anesthesiology	--	10,300	119	10,419	--	17,840	--	17,840
Speech therapy	--	35,583	1,508	37,091	--	41,286	864	42,151
	<u>1,454,631</u>	<u>1,510,748</u>	<u>534,755</u>	<u>3,500,134</u>	<u>969,597</u>	<u>1,936,081</u>	<u>793,632</u>	<u>3,699,308</u>
GENERAL SERVICES:								
Plant operation and maintenance	95,818	8,057	121,200	225,075	91,262	--	137,782	229,044
Dietary	111,310	3,007	49,077	163,394	123,422	2,745	39,903	166,070
Housekeeping	55,347	--	7,372	62,719	58,607	--	13,677	72,284
Laundry and linen	--	--	20,593	20,593	--	--	21,546	21,546
	<u>262,475</u>	<u>11,064</u>	<u>198,242</u>	<u>471,781</u>	<u>273,291</u>	<u>2,745</u>	<u>212,908</u>	<u>488,944</u>
ADMINISTRATIVE SERVICES	<u>285,434</u>	<u>620,408</u>	<u>138,331</u>	<u>1,044,173</u>	<u>326,613</u>	<u>374,497</u>	<u>9,238</u>	<u>710,348</u>
NONDEPARTMENTAL:								
Employee benefits	--	--	758,710	758,710	--	--	671,863	671,863
Depreciation and amortization	--	--	391,359	391,359	--	--	278,808	278,808
Insurance	--	--	84,879	84,879	--	--	68,190	68,190
Interest	--	--	52	52	--	--	350	350
	<u>--</u>	<u>--</u>	<u>1,235,000</u>	<u>1,235,000</u>	<u>--</u>	<u>--</u>	<u>1,019,211</u>	<u>1,019,211</u>
GRAND TOTAL	<u>\$ 2,877,158</u>	<u>2,185,583</u>	<u>2,175,451</u>	<u>7,238,192</u>	<u>2,355,669</u>	<u>2,367,969</u>	<u>2,179,785</u>	<u>6,903,423</u>

See accompanying independent auditor's report

Patient Receivables and Allowance for Doubtful Accounts
June 30, 2014 and 2013

ANALYSIS OF AGING:

Days Since Discharge	2014		2013	
	Amount	Percent of Total	Amount	Percent of Total
0 - 30	\$ 1,041,907	43.70 %	717,958	33.39 %
31 - 60	317,749	13.33	283,811	13.20
61 - 90	261,990	10.99	113,638	5.28
91 - 120	125,657	5.27	88,345	4.11
Over 120	636,689	26.71	946,704	44.02
	<u>2,383,992</u>	<u>100.00 %</u>	<u>2,150,457</u>	<u>100.00 %</u>
Less:				
Allowance for doubtful accounts	(433,310)		(594,393)	
Allowance for contractual adjustments	<u>(162,000)</u>		<u>(120,000)</u>	
	<u>\$ 1,788,682</u>		<u>1,436,064</u>	

	2014	2013
ALLOWANCE FOR DOUBTFUL ACCOUNTS:		
Balance, beginning of year	\$ 594,393	808,619
Provision of uncollectible accounts	364,240	296,572
Recoveries of accounts previously written off	18,122	52,516
Accounts written off	<u>(543,445)</u>	<u>(563,314)</u>
Balance, end of year	<u>\$ 433,310</u>	<u>594,393</u>

See accompanying independent auditor's report

Inventories/Prepaid Expenses
June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
INVENTORIES:		
Pharmacy drugs	\$ 117,958	81,670
All other	<u>17,580</u>	<u>20,574</u>
	<u>\$ 135,538</u>	<u>102,244</u>
PREPAID EXPENSES:		
Insurance	\$ 56,126	21,758
Service contracts	65,577	68,899
Dues	<u>3,983</u>	<u>4,513</u>
	<u>\$ 125,686</u>	<u>95,170</u>

See accompanying independent auditor's report

Financial and Statistical Highlights
For the Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Patient days:		
Adult and pediatric -		
Medicare	219	212
Other	62	138
	<u>281</u>	<u>350</u>
Swing bed	<u>823</u>	<u>439</u>
Total	<u><u>1,104</u></u>	<u><u>790</u></u>
Patient discharges:		
Adult and pediatric -		
Medicare	76	70
Other	28	46
	<u>104</u>	<u>116</u>
Swing bed	<u>57</u>	<u>38</u>
Total	<u><u>161</u></u>	<u><u>155</u></u>
Average length of stay:		
Adult and pediatric -		
Medicare	2.9 days	3.0 days
Other	2.2 days	3.0 days
Swing bed	14.4 days	11.6 days
Emergency room visits	1,410	1,431
Specialty clinic visits	1,682	1,708
Number of employees - full-time equivalents		
Hospital	56.13	46.70
Clinic	8.36	6.94
	<u>64.49</u>	<u>53.64</u>

**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
Hawarden Regional Healthcare
Hawarden, Iowa:

We have audited, in accordance with the 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, the financial statements of Hawarden Regional Healthcare (Hospital), as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements, and have issued our report thereon dated October 30, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Hospital's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control.

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 Hospital's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as items II-A-14 and II-B-14 that we consider to be a significant deficiency in internal control over financial reporting.

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, 2014 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 Response to Findings

The Hospital's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Hospital's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance, and the results of that testing, and not to provide an opinion on the effectiveness of the Hospital's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

SEIM JOHNSON, LLP

Omaha, Nebraska,
October 30, 2014.

Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2014

Part I: Summary of the Independent Auditor's Results

- a. An unmodified opinion was issued on the financial statements.
- b. Two 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 Deficiency

II-A-14

Criteria: The design or operation of the Hospital's internal controls should allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements in the financial statements on a timely basis.

Condition: We identified misstatements in the financial statements during the audit that were not initially identified by the Hospital's internal controls.

Effect: Audit journal entries were made to adjust amounts recorded by management for certain settlement and contractual adjustments in accounts receivable.

Cause: Management did not perform third party payor estimates as of fiscal year end and did not properly reconcile capital assets, notes payable and cash as of fiscal year end.

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: The Hospital concurs with the recommendation.

Conclusion: Response accepted.

II-B-14

Criteria: Proper segregation of duties ensures an adequate internal control structure.

Condition: We identified instances where a lack of segregation of duties exists.

Effect: Without proper segregation of duties, a greater risk of fraud and defalcation may exist.

Cause: Due to a limited number of administrative personnel, a lack of segregation of duties exists.

Recommendation: We recommend the Hospital continue to monitor and improve its segregation of duties.

Response: Management is aware of this control deficiency and believes it is economically not feasible for the Hospital to employ additional personnel for the purpose of

Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2014

greater segregation of duties. The Hospital will continue to maintain and improve its segregation of duties.

Conclusion: Response accepted.

Part III: Other Findings Related to Required Statutory Reporting

- 111-A-14** 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.
- 111-B-14** Travel Expense: No expenditures of Hospital money for travel expenses of spouses of Hospital officials and/or employees were noted.
- 111-C-14** Business Transactions: The following transactions between the Hospital and Hospital officials:
- | | | |
|---|----|----------------------|
| Matt Hummel, Member Board of Trustees: | | |
| Hospital pharmacy supervision fee | \$ | 18,000 |
| Hospital purchases of drugs and supplies from
Businesses operated by Matt Hummel -
Booth Pharmacy | | <u>4,527</u> |
| Total | \$ | <u><u>22,527</u></u> |
| Glea Hamik, Member Board of Trustees: | | |
| Wages paid for being a part-time employee during the
year ended June 30, 2014 | \$ | <u>41,723</u> |
| Total | \$ | <u><u>41,723</u></u> |
- 111-D-14** Board Minutes: - No transactions were found that we believe should have been approved in the Board minutes but were not.
- 111-E-14** 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.
- 111-F-14** 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.

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

**Summary Schedule of Prior Year Audit Findings
For the Year Ended June 30, 2014**

Finding	Status	Corrective Action Plan or Other Explanation
II-A-13	Net realizable value of accounts receivable and third party settlements	Unresolved, similar finding reported at II-A-14
II-B-13	Segregation of duties over accounting functions	Unresolved, similar finding reported at II-B-14

Hawarden Regional Healthcare
A Component Unit of the City of Hawarden, Iowa

Audit Staff
For the Year Ended June 30, 2014

This audit was performed by:

- Brian D. Green, FHFMA, CPA, Partner
- J. Alex Morton, CPA, In-Charge Auditor
- John M. Shurtliff, Staff Auditor