

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Accountants' Reports and Financial Statements
September 30, 2012 and 2011



Harper County Community Hospital
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September 30, 2012 and 2011

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Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Control
Harper County Community Hospital
Buffalo, Oklahoma

We have audited the accompanying balance sheets of Harper County Community Hospital (the Hospital), a component unit of Harper County, Oklahoma, as of September 30, 2012 and 2011, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Harper County Community Hospital as of September 30, 2012 and 2011, and its changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 31, 2013, 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 listed in the table of contents be presented to supplement the basic financial statements. Such information, although not 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 audits 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.

BKD, LLP

January 31, 2013

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Management's Discussion and Analysis
Years Ended September 30, 2012 and 2011

Introduction

This management's discussion and analysis of the financial performance of Harper County Community Hospital (the Hospital) provides an overview of the Hospital's financial activities for the years ended September 30, 2012 and 2011. It should be read in conjunction with the accompanying financial statements of the Hospital.

Financial Highlights

- Cash, cash equivalents and short-term certificates of deposit increased in 2012 by \$475,851 or 60% and in 2011 by \$59,009 or 8%.
- The Hospital's net assets increased in 2012 by \$66,261 or 4% and in 2011 by \$566,184 or 47%.
- In fiscal 2012 and 2011, the Hospital invested in capital assets costing \$89,786 and \$90,043, respectively.
- The Hospital reported operating losses of \$627,196 in 2012 and \$63,274 in 2011.
- The Hospital's unrestricted appropriations from Harper County, Oklahoma, increased \$35,830 or 6% in 2012 compared to 2011 and \$166,812 or 37% in 2011 compared to 2010.
- In fiscal 2011, the Hospital accrued an amount due from the state Medicaid program of \$450,000 in connection with its participation in the Electronic Health Records Incentive Program.

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 statements provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by creditors, contributors, grantors or enabling legislation. The Hospital is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

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

One of the most important questions asked about any hospital's finances is, "Is the hospital as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses and changes in net assets report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. Using the accrual basis of accounting means that all of the current year's revenues 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. The Hospital's total net assets—the difference between assets and liabilities—is one measure of the Hospital's financial health or financial position. Over time, increases or decreases in the Hospital's net assets are an indicator of whether its financial health is improving or deteriorating. Other nonfinancial factors, such as changes in the Hospital's patient base, changes in legislation and regulations, measures of the quantity and quality of services provided to its patients and local economic factors, should also be considered to assess the overall financial health of the Hospital.

The Statement of Cash Flows

The statement of cash flows reports cash receipts, cash payments and net changes in cash and cash equivalents resulting from four defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for and what was the change in cash and cash equivalents during the reporting period.

The Hospital's Net Assets

The Hospital's net assets are the difference between its assets and liabilities reported in the balance sheet. The Hospital's net assets increased by \$66,261 or 4% in 2012 and by \$566,184 or 47% in 2011 as shown in Table 1.

Table 1: Assets, Liabilities and Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Assets			
Cash, cash equivalents and short-term certificates of deposit	\$ 1,271,134	\$ 795,283	\$ 736,274
Patient accounts receivable, net	410,805	367,865	451,057
Other current assets	298,546	643,290	215,686
Capital assets, net	<u>448,211</u>	<u>428,942</u>	<u>417,163</u>
Total assets	<u>\$ 2,428,696</u>	<u>\$ 2,235,380</u>	<u>\$ 1,820,180</u>
Liabilities			
Long-term debt (including current maturities)	\$ 149,356	\$ 126,132	\$ 79,165
Other current and noncurrent liabilities	<u>430,725</u>	<u>326,894</u>	<u>524,845</u>
Total liabilities	<u>580,081</u>	<u>453,026</u>	<u>604,010</u>
Net Assets			
Invested in capital assets, net of related debt	298,855	302,810	298,108
Unrestricted	<u>1,549,760</u>	<u>1,479,544</u>	<u>918,062</u>
Total net assets	<u>1,848,615</u>	<u>1,782,354</u>	<u>1,216,170</u>
Total liabilities and net assets	<u>\$ 2,428,696</u>	<u>\$ 2,235,380</u>	<u>\$ 1,820,180</u>

A significant change in the Hospital's financial position in 2012 was an increase in cash and cash equivalents and short-term investments and a corresponding decrease in other current assets, primarily due to the receipt of the Medicaid Electronic Health Records Incentive Program payment during 2012, which was accrued at September 30, 2011.

One significant change in the Hospital's financial position in 2011 was an increase in other current assets, due primarily to management accruing \$450,000 due from the state Medicaid program under the Electronic Health Records (EHR) Incentive Program. Another significant change in the Hospital's financial position in 2011 is the decrease in accounts payable and accrued expenses over 2010. This is primarily due to payroll being paid before year-end and a decrease in accounts payable due to fixed asset purchases in accounts payable at the prior year-end. Also, there was a significant decrease in patient accounts receivable over 2010 due to patient volume decreases.

Operating Results and Changes in the Hospital's Net Assets

In 2012, the Hospital's net assets increased by \$66,261 or 4% as shown in Table 2. This increase is made up of several different components and compares to the increase in net assets for 2011 of \$566,184 or 47% and the increase in net assets for 2010 of \$189,990 or 19%.

Table 2: Operating Results and Changes in Net Assets

	2012	2011	2010
Operating Revenues			
Net patient service revenue	\$ 3,050,119	\$ 2,833,442	\$ 2,950,863
Other operating revenues	49,753	503,765	41,345
Total operating revenues	<u>3,099,872</u>	<u>3,337,207</u>	<u>2,992,208</u>
Operating Expenses			
Salaries and wages and employee benefits	2,434,700	2,256,065	2,196,055
Purchased services and professional fees	426,770	382,641	302,914
Depreciation	89,786	78,264	74,113
Other operating expenses	775,812	683,511	694,441
Total operating expenses	<u>3,727,068</u>	<u>3,400,481</u>	<u>3,267,523</u>
Operating Loss	<u>(627,196)</u>	<u>(63,274)</u>	<u>(275,315)</u>
Nonoperating Revenues (Expenses)			
County appropriations – unrestricted	659,517	623,687	456,875
Investment income	3,920	4,051	5,379
Interest expense	(5,724)	(8,135)	(7,130)
Noncapital gifts	35,744	9,855	10,181
Total nonoperating revenues (expenses)	<u>693,457</u>	<u>629,458</u>	<u>465,305</u>
Increase in Net Assets	<u>\$ 66,261</u>	<u>\$ 566,184</u>	<u>\$ 189,990</u>

Operating Losses

The first component of the overall change in the Hospital's net assets is its operating income or loss—generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. In each of the past three years, the Hospital has reported an operating loss. This is consistent with the Hospital's recent operating history as the Hospital was formed and is operated primarily to serve residents of Harper County, Oklahoma, and the surrounding area. Harper County levies sales taxes which are provided to the Hospital as unrestricted appropriations to assist with operations and capital improvements.

The operating loss increased by \$563,922 for 2012 as compared to 2011. The primary components of the changes in operating losses for 2012 are:

- A decrease in other operating revenues of \$454,012 or 90% as compared to 2011 caused primarily by the recognition of an EHR incentive program payment in the amount of \$450,000 in 2011.
- An increase in salaries and wages and employee benefits of \$178,635 or 8% due to an increase in number of employees and increases in employee health insurance.
- An increase in other operating expenses of \$92,301 or 14% due to additional expenses required for the operation of the CT scanner.
- An increase in purchased services and professional fees of \$44,129 or 12% primarily due to increased costs for emergency room coverage by contracted physicians.

The operating loss decreased by \$212,041 for 2011 as compared to 2010. The primary components of the changes in operating losses for 2011 are:

- An increase in other operating revenues caused primarily by the Hospital accruing \$450,000 due from the state Medicaid program under the EHR incentive program.
- A decrease in net patient service revenue of \$117,421 or 4% primarily due to decreases in volumes and the suspension of obstetrics services.
- An increase in salaries and wages and employee benefits of \$60,010 or 3% due to an increase in nursing salaries to be in line with market wages.
- An increase in purchased services and professional fees of \$79,727 or 26% primarily due to therapy labor being provided by contracted providers rather than salaried employees.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of unrestricted county appropriations, noncapital gifts, investment income and interest expense. County appropriations from sales taxes increased by \$35,830 or 6% in 2012 compared to 2011 and by \$166,812 or 37% in 2011 compared to 2010.

The Hospital's Cash Flows

Changes in the Hospital's cash flows are consistent with changes in operating losses and nonoperating revenues and expenses for 2012 and 2011 as discussed earlier.

Capital Asset and Debt Administration

Capital Assets

In 2012 and 2011, the Hospital acquired new capital assets costing \$111,895 and \$90,043, respectively. In 2012, the Hospital financed with a certain vendor and borrowed \$67,625 for equipment purchases. In 2011, \$21,590 of these assets were acquired under capital lease.

Debt

During 2012, the Hospital incurred a new note payable for \$67,625 and a financing arrangement with a vendor for \$115,950. During 2011, two new notes payable were incurred totaling \$91,397. The Hospital also entered into a capital lease for \$21,590 to purchase equipment.

Contacting the Hospital's Financial Management

This financial report is designed to provide the Hospital's 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. Questions about this report and requests for additional financial information should be directed to the Hospital administration office by telephoning 580.735.2555.

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Balance Sheets
September 30, 2012 and 2011

Assets

	2012	2011
Current Assets		
Cash and cash equivalents	\$ 667,640	\$ 625,069
Short-term certificates of deposit	603,494	170,214
Patient accounts receivable, net of allowance; 2012 – \$786,000, 2011 – \$688,000	410,805	367,865
Estimated amounts due from third-party payers	105,000	394,398
Supplies and prepaid expenses	148,418	193,739
Other receivables	45,128	55,153
Total current assets	1,980,485	1,806,438
Capital Assets, Net	448,211	428,942
Total assets	\$ 2,428,696	\$ 2,235,380

Liabilities and Net Assets

Current Liabilities		
Current maturities of long-term debt	\$ 45,241	\$ 50,375
Accounts payable	136,597	164,111
Accrued expenses	294,128	162,783
Total current liabilities	475,966	377,269
Long-Term Debt	104,115	75,757
Total liabilities	580,081	453,026
Net Assets		
Invested in capital assets, net of related debt	298,855	302,810
Unrestricted	1,549,760	1,479,544
Total net assets	1,848,615	1,782,354
Total liabilities and net assets	\$ 2,428,696	\$ 2,235,380

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2012 and 2011

	2012	2011
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2012 – \$341,126, 2011 – \$286,966	\$ 3,050,119	\$ 2,833,442
Other	49,753	503,765
	3,099,872	3,337,207
Operating Expenses		
Salaries and wages	2,011,783	1,859,866
Employee benefits	422,917	396,199
Purchased services and professional fees	426,770	382,641
Medical supplies and drugs	97,836	121,440
Supplies and other	677,976	562,071
Depreciation	89,786	78,264
	3,727,068	3,400,481
	(627,196)	(63,274)
Operating Loss		
Nonoperating Revenues (Expenses)		
County appropriations – unrestricted	659,517	623,687
Investment income	3,920	4,051
Interest expense	(5,724)	(8,135)
Noncapital gifts	35,744	9,855
	693,457	629,458
	66,261	566,184
Excess of Revenues over Expenses and Increase in Net Assets		
Net Assets, Beginning of Year	1,782,354	1,216,170
Net Assets, End of Year	\$ 1,848,615	\$ 1,782,354

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Statements of Cash Flows
Years Ended September 30, 2012 and 2011

	2012	2011
Operating Activities		
Receipts from and on behalf of patients	\$ 3,296,577	\$ 2,460,165
Payments to suppliers and contractors	(1,163,185)	(1,094,252)
Payments to and on behalf of employees	(2,303,355)	(2,340,687)
Other receipts and payments, net	52,593	503,765
Net cash used in operating activities	(117,370)	(471,009)
Noncapital Financing Activities		
Noncapital appropriations – Harper County	669,542	607,213
Noncapital gifts	35,744	9,855
Net cash provided by noncapital financing activities	705,286	617,068
Capital and Related Financing Activities		
Principal paid on long-term debt	(60,351)	(66,020)
Interest paid on long-term debt	(5,724)	(8,135)
Purchase of capital assets	(117,535)	(108,343)
Proceeds from issuance of note payable to bank	67,625	91,397
Net cash used in capital and related financing activities	(115,985)	(91,101)
Investing Activities		
Interest on investments	3,920	4,051
Net sales (purchases) of certificates of deposit	(433,280)	24,283
Net cash provided by (used in) investing activities	(429,360)	28,334
Increase in Cash and Cash Equivalents	42,571	83,292
Cash and Cash Equivalents, Beginning of Year	625,069	541,777
Cash and Cash Equivalents, End of Year	\$ 667,640	\$ 625,069

See Notes to Financial Statements

	<u>2012</u>	<u>2011</u>
Reconciliation of Operating Loss to Net Cash Used in Operating Activities		
Operating loss	\$ (627,196)	\$ (63,274)
Depreciation	89,786	78,264
Loss on disposal of capital assets	2,840	-
Changes in operating assets and liabilities		
Patient accounts receivable, net	(42,940)	83,192
Estimated amounts due from or to third-party payers	289,398	(456,469)
Accounts payable and accrued expenses	125,421	(95,990)
Supplies and prepaid expenses	45,321	(16,732)
	<u>\$ (117,370)</u>	<u>\$ (471,009)</u>
Supplemental Cash Flows Information		
Capital lease obligations incurred for capital assets	\$ -	\$ 21,590
Financing arrangement incurred for capital assets	\$ 15,950	\$ -

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Notes to Financial Statements
September 30, 2012 and 2011

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Reporting Entity

Harper County Community Hospital (the Hospital) is a critical access hospital located in Buffalo, Oklahoma. The Hospital is a component unit of Harper County, Oklahoma (the County). The Board of County Commissioners of Harper County, Oklahoma, appoints members to the Board of Control of the Hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in northwestern Oklahoma and also operates physician clinics in the same geographic area.

Basis of Accounting and Presentation

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally, unrestricted county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific (such as unrestricted county appropriations, investment income and interest on capital assets-related debt) are included in nonoperating revenues and expenses. The Hospital first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

The Hospital prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Harper County Community Hospital
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Notes to Financial Statements
September 30, 2012 and 2011

Cash and Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At September 30, 2012 and 2011, cash equivalents consisted of certificates of deposit.

Risk Management

The Hospital is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Investments and Investment Income

Investments consist of certificates of deposit, which are carried at amortized cost. Investment income consists of interest income.

Patient Accounts Receivable

The Hospital reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Hospital provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions. As a service to the patient, the Hospital bills third-party payers directly and bills the patient when the patient's liability is determined. Patient accounts receivable are due in full when billed. Accounts are considered delinquent and subsequently written off as uncollectible accounts based on individual credit evaluation and specific circumstances of the account.

Supplies

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital:

Land improvements	10–20 years
Buildings	5–50 years
Equipment	3–20 years

Harper County Community Hospital
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Notes to Financial Statements
September 30, 2012 and 2011

Compensated Absences

Hospital policies permit many employees to accumulate vacation benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as vacation benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments, such as Social Security and Medicare taxes, computed using rates in effect at that date.

Net Assets

Net assets of the Hospital are classified in two components. Net assets invested in capital assets, net of related debt consist of capital assets, net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the definition of invested in capital assets, net of related debt.

Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

County Appropriations

Effective May 1, 1990, the citizens of Harper County, Oklahoma, approved a 1% sales tax for the operations and capital improvements of county health care facilities. The tax expires April 30, 2013. On May 6, 2012, the voters of Harper County, Oklahoma, approved an extension of the sales tax beginning May 1, 2013 and expiring April 30, 2018. The County appropriates these amounts monthly to the Hospital. The Hospital received approximately 17% and 16% in 2012 and 2011, respectively, of its financial support from county appropriations related to the sales tax. Revenue from county appropriations is recognized in the year in which the sales taxes are earned.

Charity Care

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

Harper County Community Hospital
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Notes to Financial Statements
September 30, 2012 and 2011

Income Taxes

As an essential government function of the County, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Hospital is subject to federal income tax on any unrelated business taxable income. At September 30, 2012 and 2011, no provision has been made for tax on unrelated business taxable income.

Electronic Health Records Incentive Programs

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records technology (EHR). Critical access hospitals are eligible to receive incentive payments for up to four years under the Medicare program for its reasonable costs of the purchase of certified EHR technology multiplied by the Hospital's Medicare utilization plus 20%, limited to 100% of the costs incurred. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs are contingent on the Hospital continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year under both programs is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Hospital recognizes revenue at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

In 2011, the Hospital completed the first-year requirements under Medicaid and recorded revenue of approximately \$450,000. Revenue from Medicaid is included in other revenue within operating revenues in the accompanying statement of revenues, expenses and changes in net assets.

In 2012, the Hospital began complying with the first-year requirements under Medicare for its clinic operations, but because the meaningful use criteria for attestation have not been met, no revenue has been recognized in the 2012 financial statements.

Supplemental Hospital Offset Payment Program

On January 17, 2012, the Centers for Medicare and Medicaid Services (CMS) approved the State of Oklahoma's Supplemental Hospital Offset Payment Program (SHOPP). The SHOPP program is retroactive back to July 1, 2011, and is currently scheduled to sunset on December 31, 2014. The SHOPP program is designed to assess Oklahoma hospitals a supplemental hospital offset fee which will be placed in pools after receiving federal matching funds. The total fees and matching funds will then be allocated to hospitals as directed by legislation.

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Critical access hospitals are excluded from paying the supplemental hospital offset fee but are still eligible to receive SHOPP funds. During 2012, the Hospital received approximately \$47,000 in SHOPP funds. The estimated annual amount to be received by the Hospital over the term of the SHOPP program is \$38,000.

Reclassifications

Certain reclassifications have been made to the 2011 financial statements to conform to the 2012 financial statement presentation. These reclassifications had no effect on the changes in financial position.

Note 2: Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. The payment arrangements include:

- **Medicare** – The Hospital is reimbursed based on a cost reimbursement methodology for inpatient and outpatient services provided to Medicare program beneficiaries as a critical access hospital. The Hospital is reimbursed at tentative rates 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 the year ended September 30, 2010.
- **Medicaid** – The Hospital has also been reimbursed for services rendered to patients covered by the state Medicaid program at prospectively determined rates per discharge and fee schedules with no retroactive adjustments. The payment rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Approximately 65% and 56% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended September 30, 2012 and 2011, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Notes to Financial Statements
September 30, 2012 and 2011

Note 3: Deposits

Custodial credit risk is the risk that in the event of a bank failure a government's deposits may not be returned to it. The Hospital does not have a formal policy to address custodial credit risk.

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to \$250,000. Pursuant to legislation enacted in 2010, the FDIC will fully insure all noninterest-bearing transaction accounts beginning December 31, 2010 through December 31, 2012, at all FDIC-insured institutions.

At September 30, 2012 and 2011, none of the Hospital's bank balances of \$1,319,854 and \$883,321, respectively, were exposed to custodial credit risk.

Summary of Carrying Values

The carrying values of deposits shown below are included in the accompanying balance sheets as follows:

	<u>2012</u>	<u>2011</u>
Cash and cash equivalents	\$ 667,640	\$ 625,069
Short-term certificates of deposit	<u>603,494</u>	<u>170,214</u>
	<u>\$ 1,271,134</u>	<u>\$ 795,283</u>

Note 4: Patient Accounts Receivable

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at September 30, 2012 and 2011, consisted of:

	<u>2012</u>	<u>2011</u>
Medicare	\$ 157,094	\$ 138,521
Medicaid	27,452	26,656
Other third-party payers	143,108	123,602
Patients	<u>869,151</u>	<u>767,086</u>
	1,196,805	1,055,865
Less allowance for uncollectible accounts	<u>786,000</u>	<u>688,000</u>
	<u>\$ 410,805</u>	<u>\$ 367,865</u>

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Notes to Financial Statements
September 30, 2012 and 2011

Note 5: Capital Assets

Capital assets activity for the years ended September 30 was:

	2012				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 8,875	\$ -	\$ -	\$ -	\$ 8,875
Land improvements	38,373	-	-	-	38,373
Buildings	536,276	-	-	-	536,276
Equipment	<u>1,225,747</u>	<u>111,895</u>	<u>(21,883)</u>	<u>-</u>	<u>1,315,759</u>
	<u>1,809,271</u>	<u>111,895</u>	<u>(21,883)</u>	<u>-</u>	<u>1,899,283</u>
Less accumulated depreciation					
Land improvements	23,385	2,998	-	-	26,383
Buildings	331,212	16,247	-	-	347,459
Equipment	<u>1,025,732</u>	<u>70,541</u>	<u>(19,043)</u>	<u>-</u>	<u>1,077,230</u>
	<u>1,380,329</u>	<u>89,786</u>	<u>(19,043)</u>	<u>-</u>	<u>1,451,072</u>
Capital assets, net	<u>\$ 428,942</u>	<u>\$ 22,109</u>	<u>\$ (2,840)</u>	<u>\$ -</u>	<u>\$ 448,211</u>

	2011				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 8,875	\$ -	\$ -	\$ -	\$ 8,875
Land improvements	26,998	11,375	-	-	38,373
Buildings	500,259	49,957	(13,940)	-	536,276
Equipment	<u>1,304,790</u>	<u>28,711</u>	<u>(107,754)</u>	<u>-</u>	<u>1,225,747</u>
	<u>1,840,922</u>	<u>90,043</u>	<u>(121,694)</u>	<u>-</u>	<u>1,809,271</u>
Less accumulated depreciation					
Land improvements	21,216	2,169	-	-	23,385
Buildings	332,235	12,917	(13,940)	-	331,212
Equipment	<u>1,070,308</u>	<u>63,178</u>	<u>(107,754)</u>	<u>-</u>	<u>1,025,732</u>
	<u>1,423,759</u>	<u>78,264</u>	<u>(121,694)</u>	<u>-</u>	<u>1,380,329</u>
Capital assets, net	<u>\$ 417,163</u>	<u>\$ 11,779</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 428,942</u>

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Notes to Financial Statements
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Note 6: Medical Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care 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 claim experience, the Hospital has accrued \$10,000 at September 30, 2012 and 2011. It is reasonably possible that this estimate could change materially in the near term.

Note 7: Long-Term Debt

The following is a summary of long-term debt transactions for the Hospital for the years ended September 30:

	2012				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Note payable to bank (A)	\$ 6,746	\$ -	\$ (6,746)	\$ -	\$ -
Note payable to bank (B)	1,569	-	(1,569)	-	-
Note payable to bank (C)	14,628	-	(14,628)	-	-
Note payable to bank (D)	4,320	-	(4,320)	-	-
Note payable to bank (E)	34,071	-	(11,014)	23,057	10,756
Note payable to bank (F)	45,922	-	(8,999)	36,923	9,405
Financing arrangement (G)	-	15,950	(3,988)	11,962	5,004
Note payable to bank (H)	-	67,625	(5,231)	62,394	16,218
Capital lease obligation	18,876	-	(3,856)	15,020	3,858
	<u>\$ 126,132</u>	<u>\$ 83,575</u>	<u>\$ (60,351)</u>	<u>\$ 149,356</u>	<u>\$ 45,241</u>

	2011				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Note payable to bank (A)	\$ 15,285	\$ -	\$ (8,539)	\$ 6,746	\$ 6,746
Note payable to bank (B)	10,697	-	(9,128)	1,569	1,569
Note payable to bank (C)	42,634	-	(28,006)	14,628	14,628
Note payable to bank (D)	10,549	-	(6,229)	4,320	4,320
Note payable to bank (E)	-	42,442	(8,371)	34,071	10,284
Note payable to bank (F)	-	48,955	(3,033)	45,922	8,970
Capital lease obligation	-	21,590	(2,714)	18,876	3,858
	<u>\$ 79,165</u>	<u>\$ 112,987</u>	<u>\$ (66,020)</u>	<u>\$ 126,132</u>	<u>\$ 50,375</u>

Harper County Community Hospital
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Notes to Financial Statements
September 30, 2012 and 2011

Notes Payable to Banks and Financing Arrangement

- (A) Bank note payable dated June 26, 2007, in the original amount of \$39,620 has monthly payments of \$769, including interest at 6% and matured in 2012. The note is unsecured.
- (B) Bank note payable dated April 17, 2007, in the original amount of \$129,450 has monthly payments of \$2,473, including interest at 6.0% and matured in 2012. The note is unsecured.
- (C) Bank note payable dated November 30, 2006, in the original amount of \$41,004 with monthly payments of \$793, including interest at 5.5%. The note is unsecured.
- (D) Bank note payable dated June 2, 2009, in the original amount of \$18,398 has monthly payments of \$552, including interest at 5% and matured in 2012. The note is secured by certain equipment.
- (E) Bank note payable dated November 11, 2010, in the original amount of \$42,442 has monthly payments of \$968, including interest at 4.5% and matures in fiscal 2015. The note is unsecured.
- (F) Bank note payable dated June 30, 2011, in the original amount of \$48,955 has monthly payments of \$916, including interest at 4.75% and matures in 2016. The note is secured by certain equipment.
- (G) Financing arrangement with vendor dated November 18, 2011, payable quarterly beginning January 15, 2012, in the amount of \$2,060, which includes \$731 of warranty expense, principal and imputed interest at 3.25%, and matures in 2015. The arrangement is secured by certain equipment.
- (H) Bank note payable dated June 8, 2012, in the original amount of \$67,625, has monthly payments of \$1,506, including interest at 3.25% and matures in 2016. The note is secured by certain equipment.

The debt service requirements as of September 30, 2012, are as follows:

Year Ending September 30,	Total to be Paid	Principal	Interest
2013	\$ 45,967	\$ 41,383	\$ 4,584
2014	45,968	43,034	2,934
2015	31,897	30,488	1,409
2016	19,772	19,431	341
	<u>\$ 143,604</u>	<u>\$ 134,336</u>	<u>\$ 9,268</u>

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Notes to Financial Statements
September 30, 2012 and 2011

Capital Lease Obligations

The Hospital is obligated under a lease for equipment that is accounted for as a capital lease. Assets under the capital lease at September 30, 2012 and 2011, totaled \$21,590, net of accumulated depreciation of \$5,655 and \$2,570, respectively. The following is a schedule by year of future minimum lease payments under the capital lease, including interest at a rate of 4.75% together with present value of the future minimum lease payments as of September 30, 2012:

Year Ending September 30,		
2013	\$	5,253
2014		5,253
2015		5,253
2016		1,446
Total minimum lease payments		17,205
Less amount representing interest		2,185
Present value of future minimum lease payments	\$	15,020

Note 8: Operating Leases

Rental expense under month-to-month and other operating lease agreements totaled approximately \$37,000 for the years ended September 30, 2012 and 2011.

Note 9: Pension Plan

In fiscal 2007, the Hospital began contributing to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's contributions determined in accordance with the terms of the plan. The plan is administered by a third-party administrator. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Hospital's governing body. Contribution rates for plan members and the Hospital expressed as a percentage of covered payroll were 7% and 4%, respectively, for 2012 and 8% and 4%, respectively, for 2011. Contributions actually made by plan members and the Hospital aggregated approximately \$87,000 and \$49,000 during 2012 and \$87,000 and \$50,000 during 2011, respectively.

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Notes to Financial Statements
September 30, 2012 and 2011

Note 10: Significant Estimates and Concentrations

Current Economic Conditions

The current protracted economic decline continues to present hospitals with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair values of investments and other assets, large declines in contributions, constraints on liquidity and difficulty obtaining financing. The accompanying financial statements have been prepared using values and information currently available to the Hospital.

Current economic conditions, including the rising unemployment rate, have made it difficult for certain of the Hospital's patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net patient service revenue, which could have an adverse impact on the Hospital's future operating results. Further, the effect of economic conditions on the state may have an adverse effect on cash flows related to the Medicaid program.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the accompanying financial statements could change rapidly, resulting in material future adjustments in allowances for accounts that could negatively impact the Hospital's ability to maintain sufficient liquidity.

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

Board of Control
Harper County Community Hospital
Buffalo, Oklahoma

We have audited the financial statements of Harper County Community Hospital (the Hospital), a component unit of Harper County, Oklahoma, as of and for the year ended September 30, 2012, and have issued our report thereon dated January 31, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

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

Board of Control
Harper County Community Hospital

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*.

We noted certain matters that we reported to the Hospital's management in a separate letter dated January 31, 2013.

This report is intended solely for the information and use of the Board of Control, management and others within the Hospital and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

January 31, 2013

Harper County Community Hospital
A Component Unit of Harper County, Oklahoma
Schedule of Findings and Reponses
Year Ended September 30, 2012

Reference Number	Finding
	No matters are reportable.