Management's Discussion and Analysis
and Financial Statements
June 30, 2017 and 2016

Choctaw County – City of Hugo Hospital Authority

EideBailly

CPAs & BUSINESS ADVISORS

Independent Auditor's Report

Board of Trustees
Choctaw County – City of Hugo Hospital Authority
Hugo, Oklahoma

Report on the Financial Statements
We have audited the accompanying financial statements of Choctaw County – City of Hugo Hospital Authority (Authority), which comprise the statement of net position as of June 30, 2017, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit 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 Authority'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 Authority'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 financial position of Choctaw County – City of Hugo Hospital Authority as of June 30, 2017, and the results of its operations, changes in net position, and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters
The financial statements of Choctaw County – City of Hugo Hospital Authority as of June 30, 2016, were audited by other auditors, whose report dated December 21, 2016, expressed an unmodified opinion on those statements.

Required Supplementary Information
Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 6 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.

Other Reporting Required by *Government Auditing Standards*
In accordance with *Government Auditing Standards*, we have also issued our report dated January 23, 2018 on our consideration of the Authority'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* in considering the Authority's internal control over financial reporting and compliance.

Eide Bailly LLP

Oklahoma City, Oklahoma
January 23, 2018

Introduction

Our discussion and analysis for Choctaw County – City of Hugo Hospital Authority (Authority) financial performance provides an overview of the Authority's financial activities for the fiscal years ended June 30, 2017, 2016 and 2015. It should be read in conjunction with the accompanying financial statements of the Authority.

Financial Highlights

Current assets decreased in 2017 by $1,204,191 or 15% and increased in 2016 by $1,852,014 or 30%.

Total liabilities decreased in 2017 by $160,583 or 7% and decreased in 2016 by $477,118 or 18%.

The Authority's net position decreased in 2017 by $1,216,534 or 13% and decreased in 2016 by $448,045 or 5%.

The Authority reported an operating loss in 2017 of $2,139,445, an operating loss in 2016 of $1,318,916 and an operating loss in 2015 of $436,375. During 2017, the operating loss increased by $820,529 or 62%, and the operating loss increased by $882,541 or 202% during 2016.

Other operating revenue decreased by $328,265 in 2017, and decreased by $284,637 in 2016. The changes were primarily due to electronic health records incentive revenues.

Operating expenses increased in 2017 by $201,071 or 2% and decreased by $56,318 or 0.5% in 2016.

Using This Annual Report

The Authority's financial statements consist of three statements – Statement of Net Position, Statement of Revenues, Expenses and Changes in Net Position, and Statement of Cash Flows. These financial statements and related notes provide information about activities of the Authority, including resources held by the Authority but restricted for specific purposes by contributors, grantors, or enabling legislation. The Authority 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 Statement of Net Position and Statement of Revenues, Expenses and Changes in Net Position

One of the most important questions asked about the Authority's finances is "Is the Authority as a whole better or worse off as a result of the year's activities?" The Statement of Net Position and the Statement of Revenues, Expenses and Changes in Net Position report information about the Authority's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and liabilities using the accrual basis of accounting. 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 Authority's net position and changes in it. You can think of the Authority's net position - the difference between assets and liabilities - as one way to measure the Authority's financial health, or financial position. Over time, increases or decreases in the Authority's net position 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 Authority'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 Authority.

The Statement of Cash Flows

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

The Authority's Net Position

The Authority's net position is the difference between its assets and liabilities reported in the Statement of Net Position. The Authority's net position decreased by $1,216,534 or 13% in 2017 and decreased by $448,045 or 5% in 2016 as shown below.

	2017	2016	2015
Assets			
Current assets	$ 6,735,778	$ 7,939,969	$ 6,087,955
Capital assets, net	3,413,485	3,586,411	3,913,588
Other noncurrent assets	-	-	2,450,000
Total assets	$ 10,149,263	$ 11,526,380	$ 12,451,543
Liabilities			
Current liabilties	$ 1,874,374	$ 1,980,488	$ 2,360,376
Long-term debt, less current maturities	182,475	236,944	334,174
Total liabilities	2,056,849	2,217,432	2,694,550
Net Position			
Net investment in capital assets	1,989,003	1,934,782	1,986,010
Restricted, expendable for debt service	1,187,538	1,326,525	1,459,696
Unrestricted	4,915,873	6,047,641	6,311,287
Total net position	8,092,414	9,308,948	9,756,993
Total liabilities and net position	$ 10,149,263	$ 11,526,380	$ 12,451,543

Assets, Liabilities, and Net Position

A significant component of the change in the Authority's assets, liabilities, and net position is the change in current assets and other noncurrent assets. Current assets decreased $1,204,191 or 15% in 2017, which was due primarily to a decrease in cash as a result of the operating loss. Current assets increased $1,852,014 or 30% in 2016. Current liabilities decreased $106,114 or 5% in 2017 and decreased $379,888 or 16% in 2016. The decrease is a result of principal payments on outstanding debt obligations.

Operating Results and Changes in Net Position

	2017	2016	2015
Operating Revenues			
Net patient service revenue	$ 9,832,205	$ 10,123,398	$ 10,777,620
Other operating revenue	131,788	460,053	744,690
Total operating revenue	9,963,993	10,583,451	11,522,310
Operating Expenses			
Salaries, wages, and employee benefits	6,426,932	6,327,323	6,484,645
Supplies and other	5,133,656	5,007,023	5,039,552
Depreciation and amortization	542,850	568,021	434,488
Total operating expenses	12,103,438	11,902,367	11,958,685
Operating Loss	(2,139,445)	(1,318,916)	(436,375)
Nonoperating Revenues (Expenses)			
Sales taxes	917,730	874,679	859,134
Investment income	36,091	41,250	46,505
Interest expense	(39,056)	(53,355)	(20,141)
Noncapital contributions and donations	8,146	8,297	7,956
Nonoperating revenues, net	922,911	870,871	893,454
Change in Net Position	$ (1,216,534)	$ (448,045)	$ 457,079

Operating Results

The first component of the overall change in the Authority's net position is its operating results. Generally, the operating income or loss is the difference between net patient service and other operating revenues and the expenses incurred to perform those services. The Authority had operating losses in 2017, 2016, and 2015.

The operating loss for 2017 increased by $820,529 or 62% as compared to the increase of $882,541 or 202% in 2016. The primary components of the increase in operating loss are:

- A decrease in net patient service of $291,193 in 2017 and $654,222 in 2016, which was due to a decrease in patient volumes.
- A decrease in other operating revenue of $328,265 in 2017 and $284,637 in 2016, primarily due to a decrease in electronic health records incentive revenues.
- An increase in supplies and other expenses of $126,633 in 2017, which was primarily due to increased repair costs compared to a decrease of $32,529 in 2016.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of city sales tax, interest income, and interest expense. The sales tax increased by $43,051 or 5% in 2017 and $15,545 or 2% in 2016.

The Authority's Cash Flows

The Authority's overall liquidity decreased during the year with a net decrease to cash and cash equivalents, of $1,124,884, or 89% when compared with 2016. Cash flows used for operating activities increased by $250,837 during 2017 when compared with 2016. This was due primarily to the decrease in payments from electronic health records incentive. Cash provided by non-capital financing activities increased by $62,270 compared with 2016. Cash used for capital and capital related financing activities increased by $65,979 when compared with 2016. Cash used for investing activities increased by $276,220 in 2017 compared to $91,571 in 2016.

Capital Assets

The Authority had $3,413,485 invested in capital assets at the end of 2017 and $3,586,411 at the end of 2016, net of accumulated depreciation, as detailed in Note 4 to the financial statements. The Authority purchased new capital assets totaling $369,924 in 2017 and $240,844 in 2016.

Note Payable and Capital Leases

The Authority had $1,424,482 in a note payable and capital leases at the end of 2017 and $1,651,629 at the end of 2016, as detailed in Notes 5 and 6 to the financial statements. The Authority made principal payments of $227,147 in 2017 and $275,949 in 2016.

Contacting the Authority's Financial Management

This financial report is designed to provide our patients, suppliers and creditors with a general overview of the Authority's finances and to show the Authority's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Authority administration by calling 580-317-9500.

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	2017	2016
Assets		
Current Assets		
Cash and cash equivalents	$ 1,283,255	$ 2,408,139
Certificates of deposit	62,462	1,415,475
Internally designated for specific operating purposes	1,763,061	-
Restricted by bank for debt service	1,187,538	1,326,525
Receivables		
Patient, net of estimated uncollectibles of $2,516,000 in 2017 and $1,869,000 in 2016	1,334,952	1,647,094
Estimated third-party payor settlements	106,463	85,000
Sales tax	412,086	456,688
Supplies	464,198	497,445
Prepaid expenses and other	121,763	103,603
Total current assets	6,735,778	7,939,969
Capital Assets		
Capital assets not being depreciated	15,512	15,512
Capital assets being depreciated, net	3,397,973	3,570,899
Total capital assets	3,413,485	3,586,411
Total assets	$ 10,149,263	$ 11,526,380

See Notes to Financial Statements

	2017	2016
Liabilities and Net Position		
Current Liabilities		
Note payable	$ 1,187,538	$ 1,326,525
Current maturities of long-term debt	54,469	88,160
Accounts payable	276,413	251,115
Accrued expenses	355,954	314,688
Total current liabilities	1,874,374	1,980,488
Long-Term Debt, Less Current Maturities	182,475	236,944
Total liabilities	2,056,849	2,217,432
Net Position		
Net investment in capital assets	1,989,003	1,934,782
Restricted, expendable for debt service	1,187,538	1,326,525
Unrestricted	4,915,873	6,047,641
Total net position	8,092,414	9,308,948
Total liabilities and net position	$ 10,149,263	$ 11,526,380

Choctaw County – City of Hugo Hospital Authority

Statements of Revenues, Expenses and Changes in Net Position

Years Ended June 30, 2017 and 2016

	2017	2016
Operating Revenues		
Net patient service revenue (net of provision for bad debts of $4,608,985 in 2017 and $4,435,289 in 2016)	$ 9,832,205	$ 10,123,398
Other revenue	131,788	460,053
Total operating revenues	9,963,993	10,583,451
Operating Expenses		
Salaries and wages	5,526,639	5,421,685
Employee benefits	900,293	905,638
Professional fees and purchased services	2,630,966	2,808,014
Supplies and other	2,502,690	2,199,009
Depreciation and amortization	542,850	568,021
Total operating expenses	12,103,438	11,902,367
Operating Loss	(2,139,445)	(1,318,916)
Nonoperating Revenues (Expenses)		
Sales tax income	917,730	874,679
Investment income	36,091	41,250
Interest expense	(39,056)	(53,355)
Noncapital contributions	8,146	8,297
Net nonoperating revenues (expenses)	922,911	870,871
Change in Net Position	(1,216,534)	(448,045)
Net Position, Beginning of Year	9,308,948	9,756,993
Net Position, End of Year	$ 8,092,414	$ 9,308,948

	2017	2016
Operating Activities		
Receipts from and on behalf of patients	$ 10,122,884	$ 10,052,647
Payments to suppliers and contractors	(5,093,271)	(4,955,702)
Payments to and on behalf of employees	(6,385,666)	(6,530,426)
Other receipts and payments, net	131,788	460,053
Net Cash used for Operating Activities	(1,224,265)	(973,428)
Noncapital Financing Activities		
Noncapital contributions	8,146	8,297
Sales taxes received	962,332	899,911
Net Cash from Noncapital Financing Activities	970,478	908,208
Capital and Capital Related Financing Activities		
Principal payment for short-term notes payable	(138,987)	(133,171)
Principal payments on long-term debt	(88,160)	(142,778)
Interest paid	(39,056)	(53,355)
Purchase of capital assets	(369,924)	(240,844)
Net Cash used for Capital and Capital Related Financing Activities	(636,127)	(570,148)
Investing Activites		
Investment income	36,091	41,250
Sales and maturities of certificates of deposit	1,200,000	-
Purchases of certificates of deposit	(1,471,061)	-
Net Cash (used for) from Investing Activities	(234,970)	41,250
Net Change in Cash and Cash Equivalents	(1,124,884)	(594,118)
Cash and Cash Equivalents, Beginning of Year	2,408,139	3,002,257
Cash and Cash Equivalents, End of Year	$ 1,283,255	$ 2,408,139

	2017	2016
Reconciliation of Operating Loss to Net Cash used for Operating Activities		
Operating loss	$ (2,139,445)	$ (1,318,916)
Adjustments to reconcile operating loss to net cash used for operating activities		
Depreciation and amortization on capital assets	542,850	568,021
Provision for bad debts	4,608,985	4,435,289
Changes in assets and liabilities		
Patient receivables	(4,296,843)	(4,514,040)
Supplies	33,247	13,375
Prepaid expenses and other	(18,160)	36,012
Accounts payable	25,298	1,934
Accrued expenses	41,266	(203,103)
Estimated third-party payor settlements	(21,463)	8,000
Net Cash used for Operating Activities	$ (1,224,265)	$ (973,428)

Note 1 - Reporting Entity and Summary of Significant Accounting Policies

The financial statements of the Choctaw County – City of Hugo Hospital Authority (Authority) have been prepared in accordance with generally accepted accounting principles in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting and reporting policies and practices used by the Authority are described below.

Reporting Entity

The Authority operates a 34-bed short-term acute care hospital located in Hugo, Oklahoma as Choctaw Memorial Hospital. The governing boards of Choctaw County and the City of Hugo appoint members to the Board of Trustees of the Authority on an alternating basis. The Board of Trustees exercises governing oversight responsibility for the Hospital which includes such duties as budget review, care of patients, and management of the facilities as set forth by the ordinance of the City of Hugo.

For financial reporting purposes, the Authority has included all funds, organizations, agencies, boards, commissions, and authorities. The Authority 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 Authority are such that the exclusion would cause the Authority's financial situation to be misleading or incomplete. The GASB 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 Authority 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 Authority. The Authority does not have a component unit which meets the GASB criteria.

Measurement Focus and Basis of Accounting

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

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

Basis of Presentation

The statement of net position displays the Authority's assets, deferred outflows, liabilities, and deferred inflows, with the difference reported as net position. Net position is reported in the following categories/components:

Net investment in capital assets consists of net capital assets reduced by the outstanding balances of any related debt obligations and deferred inflows of resources attributable to the acquisition, construction or improvement of those assets or the related debt obligations and increased by balances of deferred outflows of resources related to those assets or debt obligations.

Restricted net position:

Expendable - Expendable net position results when constraints placed on net position use are either externally imposed or imposed through enabling legislation.

Nonexpendable - Nonexpendable net position is subject to externally imposed stipulations which require them to be maintained permanently by the Authority.

Unrestricted net position consists of net position not meeting the definition of the preceding categories. Unrestricted net position often has constraints on resources imposed by management which can be removed or modified.

When an expense is incurred that can be paid using either restricted or unrestricted resources (net position), the Authority's policy is to first apply the expense toward the most restrictive resources and then toward unrestricted resources.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with an original maturity of three months or less, excluding internally designated or restricted cash and investments. For purposes of the statement of cash flows, the Authority considers all cash and investments with an original maturity of three months or less as cash and cash equivalents.

Short-Term Investments

Short-term investments include certificates of deposit with an original maturity of three to twelve months, excluding internally designated or restricted cash and investments.

Patient Receivables

Patient receivables are uncollateralized patient and third-party payor obligations. Patient receivables, excluding amounts due from third-party payors, are turned over to a collection agency if the receivables remain unpaid after the Authority's collections procedures. The Authority does not charge interest on the unpaid patient receivables. Payments of patient receivables are allocated to the specific claims 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 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.

Supplies

Supplies are stated at lower of cost (first-in, first-out) or market and are expensed when used.

Investment Income

Interest, dividends, gains and losses, both realized and unrealized, on investments and deposits are included in nonoperating revenues when earned.

Capital Assets

Property and equipment acquisitions in excess of $5,000 are capitalized and recorded at cost. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method. 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. Amortization is included in depreciation and amortization in the financial statements. The estimated useful lives of capital assets are as follows:

Land improvements	10-40 years
Buildings and improvements	5-40 years
Equipment	3-20 years

Gifts of long-lived assets such as land, buildings, or equipment are reported as additions to unrestricted net position, and are excluded from revenues in excess of (less than) expenses. 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 net position.

Compensated Absences

The Authority's employees earn paid time-off days at varying rates depending on years of service. Employees may accumulate paid time-off up to a specified maximum. Employees are paid for accumulated paid time-off upon termination. The liability for compensated absences is included with accrued expenses in the accompanying financial statements.

Operating Revenues and Expenses

The Authority's statement of revenues, expenses, and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues and expenses of the Authority result from exchange transactions associated with providing health care services - the Authority's principal activity, and the costs of providing those services, including depreciation and excluding interest cost. All other revenues and expenses are reported as nonoperating.

Net Patient Service Revenue

The Authority has agreements with third-party payors that provide for payments to the Authority at amounts different from its established rates. Payment arrangements include prospectively determined rates, 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 considered in the recognition of revenue on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity Care

The Authority provides health care services to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Since the Authority does not pursue collection of these amounts, they are not reported as patient service revenue. The estimated cost of providing these services was $120,000 and $48,000 for the years ended June 30, 2017 and 2016, calculated by multiplying the ratio of cost to gross charges for the Authority by the gross uncompensated charges associated with providing charity care to its patients.

Grants and Contributions

The Authority may receive grants as well as contributions from individuals and private organizations. Revenues 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 non-operating revenues. Amounts restricted to capital acquisitions are reported after revenues in excess of (less than) expenses.

Electronic Health Record Incentives

The American Recovery and Reinvestment Act of 2009 (ARRA) amended the Social Security Act to establish incentive payments under the Medicare and Medicaid programs for certain hospitals and professionals that demonstrate meaningful use of certified Electronic Health Records (EHR) technology.

To qualify for the EHR incentive payments, hospitals and physicians must meet designated EHR meaningful use criteria. In addition, hospitals must attest that they have used certified EHR technology, satisfied the meaningful use objectives, and specify the EHR reporting period. This attestation is subject to audit by the federal government or its designee. The EHR incentive payment to hospitals for each payment year is calculated as a product of (1) an initial amount; (2) the Medicare share; and (3) a transition factor applicable to that payment year.

The Authority recognizes EHR incentive payments as revenue when there is reasonable assurance that the Authority will comply with the conditions attached to the incentive payments. EHR incentive payments are included in other operating revenue in the accompanying financial statements. The amount of EHR incentive payments recognized are based on management's best estimate and those amounts are subject to change with such changes impacting the period in which they occur.

The Authority recognized revenue of $3,892 and $345,925 for the years ended June 30, 2017 and 2016 related to EHR incentive payments. These incentive payments are included in other revenue in the accompanying financial statements.

Supplemental Hospital Offset Payment Program

On January 17, 2012, CMS approved the State of Oklahoma's Supplemental Hospital Offset Payment Program (SHOPP). The SHOPP is retroactive back to July 1, 2011, and is currently scheduled to sunset on December 31, 2020. The SHOPP 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.

SHOPP revenue is recorded as part of net patient service revenue and SHOPP assessment fees are recorded as part of other expenses on the accompanying statements of revenues, expenses and changes in net position. The annual amounts to be received and paid by the Authority over the term of the SHOPP are subject to change annually based on various factors involved in determining the amount of federal matching funds. Based on the current information available, the annual net benefit to the Authority over the term of the SHOPP is not expected to be materially different than the net amounts received in 2017 and 2016. Net SHOPP benefit consisted of the following for the years ended June 30, 2017 and 2016.

	2017	2016
SHOPP funds received	$ 943,277	$ 844,000
SHOPP assessment fees paid	356,776	301,000
Net SHOPP benefit	$ 586,501	$ 543,000

Sales Tax Revenue

Effective April 1, 2009, the citizens of Choctaw County, Oklahoma, approved a 0.75% sales tax for furnishing, equipping, renovating and maintaining the Authority, including the payment of principal and interest on any indebtedness. The tax will continue until repealed by the voters. For the years ended June 30, 2017 and 2016, the Authority received approximately $918,000 and $875,000, or 8% and 8% of its revenue, from the tax appropriation. Revenue from tax appropriations is recognized in the year in which the sales taxes are earned.

Reclassifications

Reclassifications have been made to the June 30, 2016 financial information to make it conform to the current year presentation. The reclassifications had no effect on previously reported operating results or changes in net position.

Note 2 - Net Patient Service Revenue

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

Medicare: Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient skilled nursing services are paid at prospectively determined per diem rates that are based on the patients' acuity. The Authority is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare Administrative Contractor (MAC). The Authority's Medicare cost reports have been audited by the MAC through the year ended June 30, 2015.

Medicaid: The Authority 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.

Other carriers: The Authority has also entered into payment agreements with certain commercial insurance carriers and other organizations. The basis for payment to the Authority under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Concentration of gross revenues by major payor accounted for the following percentages of the Authority's patient service revenues for the years ended June 30, 2017 and 2016 is as follows:

	2017	2016
Medicare	47%	47%
Medicaid	17%	16%
Commercial and other payors	23%	24%
Self pay	13%	13%
	100%	100%

Laws and regulations governing the Medicare, Medicaid, and other programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The net patient service revenue for the year ended June 30, 2017 decreased approximately $327,000 due to adjustments of amounts previously estimated.

Note 3 - Deposits and Investments

The carrying amounts of deposits and investments as of June 30, 2017 and 2016 are as follows:

	2017	2016
Carrying Amount		
Cash	$ 1,283,255	$ 2,408,139
Short-term certificates of deposit	3,013,061	2,742,000
	$ 4,296,316	$ 5,150,139

Deposits and investments are reported in the following statement of net position captions:

	2017	2016
Cash and cash equivalents	$ 1,283,255	$ 2,408,139
Short-term investments	62,462	1,415,475
Internally designated for specific operating purposes	1,763,061	-
Restricted by bank for debt service	1,187,538	1,326,525
	$ 4,296,316	$ 5,150,139

Deposits – Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank or investment company failure, the Authority's deposits may not be returned to it. The Authority's deposit policy does not further restrict bank deposits or limit investment deposits.

The Authority's deposits in banks at June 30, 2017 and 2016 were entirely covered by federal depository insurance or by collateral held by the Authority's custodian bank in the Authority's name.

Investments

Under state law, investments are limited to full faith and credit obligations of the federal government, obligations of certain federal agencies or instrumentalities, repurchase agreements collateralized by those securities, collateralized or insured certificates of deposit and other evidences of deposit, negotiable certificates of deposit, Bankers' acceptances, limited top-rated commercial paper, certain money market mutual funds, obligations of state and local governments, including obligations of Oklahoma state public trusts and bond notes, debentures or other similar obligations of a foreign government that meet specific requirements.

The Authority had the following investments and maturities at June 30, 2017 and 2016:

	Maturities	2017	2016
Certificates of deposit	Less than 1 year	$ 3,013,061	$ 2,742,000

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The Authority does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. State statutes require that investments be made in compliance with state law. The Authority's investment policy does not further limit its investment options.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The Authority does not have a formally adopted investment policy for managing concentration of credit risk.

Note 4 - Capital Assets

Capital assets additions, retirements, transfers and balances for the year ended June 30, 2017 are as follows:

	Balance June 30, 2016	Additions	Transfers and Retirements	Balance June 30, 2017
Capital assets not being depreciated				
Land	$ 15,512	$ -	$ -	$ 15,512
Capital assets being depreciated				
Building and improvements	$ 6,151,041	$ 132,841	$ -	$ 6,283,882
Equipment	5,411,262	237,083	(8,853)	5,639,492
Total capital assets being depreciated	11,562,303	$ 369,924	$ (8,853)	11,923,374
Less accumulated depreciation for				
Building and improvements	(3,393,936)	$ (240,913)	$ -	(3,634,849)
Equipment	(4,597,468)	(301,937)	8,853	(4,890,552)
Total accumulated depreciation	(7,991,404)	$ (542,850)	$ 8,853	(8,525,401)
Net capital assets being depreciated	$ 3,570,899			$ 3,397,973
Capital assets, net	$ 3,586,411			$ 3,413,485

Capital assets additions, retirements, transfers and balances for the year ended June 30, 2016 are as follows:

	Balance June 30, 2015	Additions	Transfers and Retirements	Balance June 30, 2016
Capital assets not being depreciated				
Land	$ 15,512	$ -	$ -	$ 15,512
Construction in progress	2,377,479	-	(2,377,479)	-
Total capital assets not being depreciated	$ 2,392,991	$ -	$ (2,377,479)	$ 15,512
Capital assets being depreciated				
Building and improvements	$ 3,940,014	$ 57,524	$ 2,153,503	$ 6,151,041
Equipment	5,075,528	183,320	152,414	5,411,262
Total capital assets being depreciated	9,015,542	$ 240,844	$ 2,305,917	11,562,303
Less accumulated depreciation for				
Building and improvements	(3,194,349)	$ (240,987)	$ 41,400	(3,393,936)
Equipment	(4,300,596)	(327,034)	30,162	(4,597,468)
Total accumulated depreciation	(7,494,945)	$ (568,021)	$ 71,562	(7,991,404)
Net capital assets being depreciated	$ 1,520,597			$ 3,570,899
Capital assets, net	$ 3,913,588			$ 3,586,411

Note 5 - Lease Obligations

The Authority leases certain equipment under noncancelable long-term lease agreements. Certain leases have been recorded as capitalized leases and others as operating leases. Total lease expense for the years ended June 30, 2017 and 2016 for all operating leases was $225,843 and $285,940. The capitalized leased assets consist of:

	2017	2016
Major moveable equipment	$ 384,411	$ 752,169
Less accumulated amortization	(211,426)	(465,735)
	$ 172,985	$ 286,434

Minimum future lease payments for the capital and operating leases are as follows:

Years Ending June 30,	Capital Leases	Operating Leases
2018	$ 60,302	$ 75,336
2019	60,180	72,283
2020	60,180	40,014
2021	60,180	37,152
2022	10,449	22,094
Total minimum lease payments	251,291	$ 246,879
Less interest	(14,347)	
Present value of minimum lease payments - Note 6	$ 236,944	

Note 6 - Note Payable and Long-Term Debt

A schedule of changes in the Authority's long-term debt for 2017 and 2016 is as follows:

	Balance June 30, 2016	Additions	Payments	Balance June 30, 2017	Due Within One Year
Note Payable	$ 1,326,525	$ -	$ 138,987	$ 1,187,538	$ 1,187,538
Capital Lease Obligations (Note 5)	325,104	-	88,160	236,944	54,469
Total long-term debt	$ 1,651,629	$ -	$ 227,147	$ 1,424,482	$ 1,242,007

	Balance June 30, 2015	Additions	Payments	Balance June 30, 2016	Due Within One Year
Note Payable	$ 1,459,696	$ -	$ 133,171	$ 1,326,525	$ 1,326,525
Capital Lease Obligations (Note 5)	467,882	-	142,778	325,104	88,160
Total long-term debt	$ 1,927,578	$ -	$ 275,949	$ 1,651,629	$ 1,414,685

In March 2015, the Authority obtained a $1,494,000 short-term note payable to a bank which includes interest at 2.5% and is due on demand. The note matures annually and was extended for an additional year in February 2017. If no demand is made, the note matures February 2018. The note is collateralized by one of the Authority's certificates of deposit. Under an agreement with the bank, the Authority is making monthly payments on the note based on a 120 month amortization schedule.

Capital lease obligations, including imputed interest at 2.7%, are due in monthly installments maturing March 2022, and are collateralized by associated equipment.

Note 7 - Concentrations of Credit Risk

The Authority grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. The mix of receivables from third-party payors and patients at June 30, 2017 and 2016 was as follows:

	2017	2016
Medicare	31%	37%
Medicaid	9%	10%
Other third-party payors and patients	20%	19%
Self-pay	40%	34%
	100%	100%

Note 8 - Pension Plan

The Authority has a defined contribution pension plan under which employees can become participants upon hiring. Employer contributions are made on a discretionary basis. The Authority did not make any contributions for the years ended June 30, 2017, 2016 and 2015.

Note 9 - Contingencies

Risk Management

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

Malpractice Insurance

The Authority has malpractice insurance coverage to provide protection for professional liability losses on a claims-made basis subject to a limit of $1 million per claim and an annual aggregate limit of $3 million. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term, but reported subsequently, would be uninsured.

Litigations, Claims, and Disputes

The Authority is subject to the usual contingencies in the normal course of operations relating to the performance of its tasks under its various programs. In the opinion of management, the ultimate settlement of any litigation, claims, and disputes in process will not be material to the financial position, operations, or cash flows of the Authority.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Federal government activity has increased with respect to investigations and allegations concerning possible violations by health care providers of regulations, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenues from patient services.

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CPAs & BUSINESS ADVISORS

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

Board of Trustees
Choctaw County – City of Hugo Hospital Authority
Hugo, Oklahoma

We have audited, 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, the financial statements of Choctaw County – City of Hugo Hospital Authority (Authority) as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements and have issued our report thereon dated January 23, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority'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 Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying *Schedule of Findings and Responses*, we identified certain deficiencies in internal control that we consider to be material weaknesses.

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 Authority's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the following deficiencies described as items 2017-A through 2017-C in the accompanying *Schedule of Findings and Responses* to be material weaknesses.

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.

Compliance and Other Matters
As part of obtaining reasonable assurance about whether the Authority's financial statements are free from 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*.

Authority's Response to Findings
The Authority's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The Authority's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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 Authority'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 Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Eide Bailly LLP

Oklahoma City, Oklahoma
January 23, 2018

Findings Related To Financial Statements – Internal Controls over Financial Reporting

Material Weaknesses:

2017-A Preparation of Financial Statements

Criteria: A properly designed system of internal control over financial reporting includes the preparation of an entity's financial statements and accompanying notes to the financial statements by internal personnel of the entity. Management is responsible for establishing and maintaining internal control over financial reporting and procedures related to the fair presentation of the financial statements in accordance with standards established by the U.S. generally accepted accounting principles (GAAP) and Governmental Accounting Standards Board (GASB).

Condition: The Authority does not have an internal control system designed to provide for the preparation of the financial statements, including the accompanying footnotes and statement of cash flows, as required by GAAP and GASB. As auditors, we were requested to draft the financial statements and accompanying notes to the financial statements.

Effect: The preparation of financial statements as part of the audit engagement may result in financial statements and related information not being available for management purposes as timely as it would be if prepared by Authority personnel.

Cause: This condition was caused by the Board of Trustees' and management's determination that it would take undue expense and effort to provide for a system that prepares the financial statements in accordance with GAAP.

Auditor's Recommendation: While the preparation of financial statements by an outside party is not unusual for an organization of your size, the need for material adjustments should require consideration of the controls and processes over the areas identified. It is the responsibility of management and those charged with governance to determine whether to accept the risk associated with a deficiency in preparation of financial statements because of cost or other considerations.

Management Response: Management agrees with the finding. The Board of Trustees has taken into consideration the expense of hiring additional accounting personnel for the accurate reporting of the financial statements and feels that the cost does not justify the benefit.

2017-B Segregation of Duties and Review of Manual Journal Entries

Criteria: A properly designed system of internal control segregates the initiation, record keeping, and authorization of transactions.

Condition: The Authority has a limited number of individuals available to segregate these duties. Incompatible duties were noted in the recording and approval of accounts receivable allowance entries.

Findings Related to Financial Statements: (continued)

Effect: Inadequate segregation of duties could adversely affect the Authority's ability to detect and correct unintentional or intentional misstatements in a timely manner by employees in the normal course of performing their assigned functions. The lack of review and approval process for recorded journal entries by the appropriate individual increases the risk of misstatement in the financial statements, either due to fraud or error.

Cause: The Authority's size and budget constraints limit the number of personnel and does not facilitate the segregation of duties necessary to adequately separate procedures.

Auditor's Recommendation: It is the responsibility of management and those charged with governance to make the decisions whether to accept the degree of risk associated with this condition because of cost or other considerations. While having limited resources available to perform all functions is often present in organizations of your size, it is important to consider the significance of certain controls, such as review of manual journal entries, in detecting and correcting potential misstatements on a timely basis. We recommend that management review current policies and assigned functions and separate the responsibilities of posting and reviewing manual journal entries to appropriate individuals. In addition, we recommend additional controls be added to the review and posting of changes to the chargemaster.

Management Response: Management agrees with the finding.

2017-C Cost Report Settlement Estimate

Criteria: A properly designed system of internal control over financial reporting allows entities to initiate, record, process and report financial report data reliably in accordance with generally accepted accounting principles.

Condition: During the current year, the Authority did not estimate the financial effect of the Medicare cost report settlement for the current year correctly. The Authority should record adjustments for current year activity to the estimated third party payor settlement account. Accounting standards require an entity to estimate the Medicare cost report settlement in order to fairly state the financial position as of year-end.

Effect: Interim financial statements may not be properly stated. A material audit adjustment was made to the cost report settlement accounts.

Cause: The current year cost report settlement was not properly estimated at year end which resulted in a material journal entry to the financial statements.

Auditor's Recommendation: It is recommended the Hospital implement a system that provides adequate controls over estimating cost report settlements.

Management Response: Management agrees with the finding.