Management's Discussion and Analysis
and Financial Statements
December 31, 2011 and 2010

Arbuckle Memorial Hospital Authority

CPAs & BUSINESS ADVISORS

Independent Auditor's Report

The Board of Directors
Arbuckle Memorial Hospital Authority
Sulphur, Oklahoma

We have audited the accompanying combined balance sheet of Arbuckle Memorial Hospital Authority (Authority) as of December 31, 2011 and the related combined statements of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Arbuckle Memorial Hospital Authority as of December 31, 2010 were audited by other auditors, whose report dated June 17, 2011 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our 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 Arbuckle Memorial Hospital Authority as of December 31, 2011 and the results of its operations, changes in net assets, and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 18, 2012 on our consideration of Arbuckle Memorial Hospital Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. 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 conjunction with this report in considering the results of our audits.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 7 be presented to supplement the basic combined financial statements. Such information, although not a part of the basic combined 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.

Eide Bailly LLP

Oklahoma City, Oklahoma
June 18, 2012

This discussion and analysis of the financial performance of Arbuckle Memorial Hospital Authority (Authority) provides an overall review of the Authority's financial activities and balances as of and for the years ended December 31, 2011 and 2010. The intent of this discussion and analysis is to provide further information on the Authority's performance as a whole; readers should also review the basic financial statements and the notes thereto to enhance their understanding of the Authority's financial status.

Financial Highlights – Financial Statements

- The Authority's net assets decreased by $487,452 or 6.9% in 2011 and by $403,168 or 5.4% in 2010.
- The Authority reported operating losses in 2011 of ($949,444) and 2010 ($905,686). Losses in 2011 increased by $43,758 or 4.8% over the loss reported in 2010. Operating losses reported in 2010 increased by $55,228 or 6.5% over the loss reported in 2009.
- Non-operating revenues decreased by $31,213 or 7.1% in 2011 compared to 2010. Non-operating revenues decreased by $637,731 or 59.2% in 2010 compared to 2009.

Organization Highlights

- The Authority continues to strategically plan for the replacement and upgrade of equipment.
- The Authority continues to recruit highly qualified employees and physicians.
- The Authority continues to strategically plan for the expansion of services.

Overview of the Financial Statements

The financial statements include the balance sheets, statements of revenues, expenses, and changes in net assets, and statements of cash flows.

The balance sheet at December 31, 2011 indicated total assets of $23,979,368, total liabilities of $17,397,165 and net assets of $6,582,203. Total current assets were $6,691,916 and total current liabilities were $2,111,666 for a current ratio of 3.2. The balance sheet at December 31, 2010 had current assets of $6,091,510 and current liabilities of $1,986,784 for a current ratio of 3.1.

The statements of revenues, expenses, and changes in net assets for the year ended December 31, 2011 indicated total operating revenues of $11,518,237 and operating expenses of $12,467,681, operating loss of $949,444, non-operating revenues (net) of $408,226, and capital contributions of $53,766. The net assets decreased by $487,452 from $7,069,655 at December 31, 2010 to $6,582,203 at December 31, 2011.

As reported in the statements of cash flows, cash and cash equivalents increased from $2,467,833 at December 31, 2010 to $3,698,222 at December 31, 2011.

Please review the notes to the financial statements included in the report.

The Authority's net assets are the difference between its assets and liabilities reported on the balance sheet. The Authority's net assets decreased by $487,452 or 6.9% in 2011 and by $403,168 or 5.4% in 2010.

Table 1 Assets, Liabilities, and Net Assets

	2011	2010	2009
Assets			
Current assets	$ 6,691,916	$ 6,091,510	$ 5,582,931
Capital assets	15,083,146	16,230,883	16,790,399
Other non-current assets	2,204,306	2,558,560	4,304,185
Total assets	$ 23,979,368	$ 24,880,953	$ 26,677,515
Liabilities			
Current liabilities	$ 2,111,666	$ 1,986,784	$ 2,951,874
Long-term debt, net of current portion	15,285,499	15,824,514	16,252,818
Total liabilities	17,397,165	17,811,298	19,204,692
Net Assets			
Invested in capital assets, net of related debt	(741,367)	(131,789)	1,725,810
Restricted	1,976,890	2,010,803	3,444,917
Unrestricted	5,346,680	5,190,641	2,302,096
Total net assets	6,582,203	7,069,655	7,472,823
Total liabilities and net assets	$ 23,979,368	$ 24,880,953	$ 26,677,515

A significant component of the change in the Authority's assets is the accumulated depreciation taken against the capital assets.

In 2011, the Authority's net assets decreased by $487,452 as shown in table 2. This decrease is made up of very different components and it represents a decline of 20.9% compared with the decrease in net assets for 2010 of $403,168.

Table 2: Operating Results and Changes in Net Assets

	2011	2010	2009
Operating Revenues			
Net patient service revenue	$ 11,308,833	$ 10,534,235	$ 7,669,680
Medicaid E.H.R Incentive Payment	150,000	-	-
Other revenue	59,404	17,706	16,979
Total operating revenue	11,518,237	10,551,941	7,686,659
Operating Expenses			
Salaries and wages	6,219,678	5,635,138	4,130,221
Supplies and other	4,819,358	4,446,084	4,148,206
Depreciation and amortization	1,428,645	1,376,405	258,690
Total operating expenses	12,467,681	11,457,627	8,537,117
Operating Income (Loss)	(949,444)	(905,686)	(850,458)
Non-operating Revenue (Expenses)			
Tax appropriations	1,492,687	1,528,322	1,237,062
Investment income	11,381	17,250	18,470
Interest expense	(1,097,404)	(1,113,331)	(98,716)
Contributions	1,562	-	-
Gain/(loss) on disposal of assets	-	7,198	(79,646)
Total non-operating revenue, net	408,226	439,439	1,077,170
Expenses in excess of Revenue Before Capital Contributions	(541,218)	(466,247)	226,712
Capital Contributions	53,766	63,079	648,403
(Decrease)/Increase in Net Assets	(487,452)	(403,168)	875,115
Net Assets, Beginning of Year	7,069,655	7,472,823	6,597,708
Net Assets, End of Year	$ 6,582,203	$ 7,069,655	$ 7,472,823

Operating Income

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

The operating loss for 2011 increased by $43,758 or 4.8% as compared to 2010 and increased in 2010 by $55,228 or 6.5% compared to 2009. The primary components of the increased operating loss are:

- An increase in salaries and wages of $584,540, or 10.3% as compared to an increase in 2010 of $1,504,917 or 36.4% as compared to 2009.
- An increase in supplies and other expenses of $373,274 or 8.4% as compared to an increase in 2010 of $297,878 or 7.2% as compared to 2009.

Non-operating Revenues and Expenses

Non-operating revenues consist primarily of sales tax proceeds, interest expense, investment earnings, and contributions. The non-operating revenues decreased in 2011 by $31,213 or 7.1% and decreased by $637,731 or 59.2% in 2010.

Capital Contributions

Capital contributions consist of contributions received for the purpose of purchasing capital assets or direct contributions of capital assets. The capital contributions decreased $9,313 or 14.8% in 2011 and decreased $585,324 or 90.3% in 2010.

The Authority's Cash Flows

Changes in the Authority's cash flows are consistent with changes in operating income and non-operating revenues and expenses, as discussed earlier.

Capital Assets

The Authority had capital assets and net accumulated depreciation at December 31, 2011 amounting to $15,083,146. This investment in capital assets includes land, buildings and improvements, equipment, and construction in progress.

Capital assets consisted of the following at December 31:

	2011	2010	2009
Land	$ 58,799	$ 58,799	$ 58,799
Buildings and fixed equipment	16,231,643	16,231,643	15,654,246
Major moveable equipment	3,710,208	3,452,735	3,148,747
Construction in progress	-	-	87,930
Accumulated depreciation	(4,917,504)	(3,512,294)	(2,159,323)
Total capital assets	$ 15,083,146	$ 16,230,883	$ 16,790,399

Debt

As of December 31, 2011 and 2010 the Authority had $1,214,513 and $1,572,672 in outstanding capital lease obligations as detailed in notes 6 and 7.

The Authority has bond obligations outstanding of $14,610,000 and $14,790,000 as of December 31, 2011 and 2010. These obligations require the Authority to maintain a debt service coverage ratio of 1.1 to 1. As of December 31, 2011 and 2010, the Authority was in compliance with this covenant.

Economic Factors

The Authority has increased rates during the current fiscal year, which should continue to increase revenues for the upcoming year. The Authority continues to monitor costs throughout the year. The Authority's continued mission is to be a health care leader in the area and to enhance services to customers in a fiscally responsible manner. The Authority strives to be conscientious, consumer oriented, and dedicated to teamwork, leadership, and education.

Requests for Information

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Authority's finances and to show the Authority's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Arbuckle Memorial Hospital Authority, 2011 W Broadway Ave., Sulphur, Oklahoma 73066.

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	2011	2010
Assets		
Current Assets		
Cash and cash equivalents	$ 3,154,376	$ 1,584,362
Held by trustee for debt service	727,715	754,068
Receivables		
Patients, net of provision for bad debts of approximately $1,439,000 in 2011 and $1,118,000 in 2010	2,118,630	1,921,411
Sales tax	359,931	361,852
Other receivables	56,754	263,905
Estimated third-party payor settlements	-	800,000
Supplies	202,142	326,274
Prepaid and other assets	72,368	79,638
Total current assets	6,691,916	6,091,510
Assets Limited as to Use		
By Board of Trustees for capital acquisitions	543,846	883,471
Held by trustee for debt service, net of current portion	1,249,175	1,256,735
Total assets limited as to use	1,793,021	2,140,206
Other Assets		
Investments	181	181
Other receivables, net of current portion	16,365	-
Other deferred financing costs, net	394,739	418,173
Total other assets	411,285	418,354
Capital Assets		
Land	58,799	58,799
Depreciable assets, net of accumulated depreciation	15,024,347	16,172,084
Total capital assets	15,083,146	16,230,883
Total assets	$ 23,979,368	$ 24,880,953

	2011	2010
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt	$ 539,014	$ 538,158
Accounts payable	164,653	252,847
Construction accounts payable	-	379,195
Estimated third-party payor settlements	566,257	-
Accrued expenses		
Salaries and wages	314,204	282,971
Interest	527,538	533,613
Total current liabilities	2,111,666	1,986,784
Long-term Debt, Net of Current Portion	15,285,499	15,824,514
Total liabilities	17,397,165	17,811,298
Net Assets		
Invested in capital assets, net of related debt	(741,367)	(131,789)
Restricted		
Expendable for debt service	1,976,890	2,010,803
Unrestricted	5,346,680	5,190,641
Total net assets	6,582,203	7,069,655
Total liabilities and net assets	$ 23,979,368	$ 24,880,953

	2011	2010
Operating Revenues		
Patient and resident service revenue, net of provision for bad debts of $2,689,283 in 2011 and $2,105,911 in 2010	$ 11,308,833	$ 10,534,235
Medicaid E.H.R Incentive Payment	150,000	-
Other revenue	59,404	17,706
Total operating revenues	11,518,237	10,551,941
Operating Expenses		
Salaries and wages	6,219,678	5,635,138
Supplies and other	4,819,358	4,446,084
Depreciation and amortization	1,428,645	1,376,405
Total operating expenses	12,467,681	11,457,627
Operating Loss	(949,444)	(905,686)
Nonoperating Revenue (Expenses)		
Tax appropriations	1,492,687	1,528,322
Investment income	11,381	17,250
Interest expense	(1,097,404)	(1,113,331)
Contributions	1,562	-
Gain on disposal of assets	-	7,198
Total nonoperating revenue, net	408,226	439,439
Expenses in Excess of Revenue Before Capital Contributions	(541,218)	(466,247)
Capital Contributions	53,766	63,079
Decrease in Net Assets	(487,452)	(403,168)
Net Assets, Beginning of Year	7,069,655	7,472,823
Net Assets, End of Year	$ 6,582,203	$ 7,069,655

	2011	2010
Operating Activities		
Cash received from patient services	$ 12,627,871	$ 9,714,376
Cash payments to suppliers for goods and services	(4,776,150)	(4,461,114)
Cash payments to employees for services	(6,188,445)	(5,799,863)
Other operating revenues	250,190	75,478
Net Cash from (used for) Operating Activities	1,913,466	(471,123)
Non-capital Related Financing Activity		
Grants and contributions	1,562	-
Sales tax proceeds for operations	1,494,608	1,467,045
Net Cash from Non-capital Financing	1,496,170	1,467,045
Capital and Capital Related Financing Activities		
Capital contributions	53,766	63,079
Principal paid on long-term debt	(538,159)	(330,923)
Interest paid	(1,103,479)	(1,122,524)
Purchase of property and equipment	(636,669)	(1,853,523)
Proceeds from issuance of debt	-	82,947
Proceeds from sale of equipment	-	7,198
Net Cash used for Capital and Capital Related Financing Activities	(2,224,541)	(3,153,746)
Investing Activities		
Purchase of investments	(1,252,480)	(181)
Proceeds from sale of investments	1,286,393	3,787,482
Investment income	11,381	17,250
Net Cash from Investing Activities	45,294	3,804,551
Net Increase in Cash and Cash Equivalents	1,230,389	1,646,727
Cash and Cash Equivalents, Beginning of Year	2,467,833	821,106
Cash and Cash Equivalents, End of Year	$ 3,698,222	$ 2,467,833
Reconciliation of Cash and Cash Equivalents to the Balance Sheet		
Cash and cash equivalents	$ 3,154,376	$ 1,584,362
Cash and cash equivalents included in assets limited as to use	543,846	883,471
	$ 3,698,222	$ 2,467,833

	2011	2010
Reconciliation of Operating Income to Net		
Cash used for Operating Activities		
Operating Loss	$ (949,444)	$ (905,686)
Adjustments to reconcile change in net assets to net cash used for operating activities		
Depreciation and amortization	1,428,645	1,376,405
Provision for bad debts	2,689,283	2,105,911
Changes in assets and liabilities		
Accounts receivable	(2,886,502)	(2,209,921)
Supplies	124,132	(101,149)
Other receivables	190,786	57,772
Prepaid expenses	7,270	(2,449)
Accounts payable	(88,194)	88,568
Accrued liabilities	31,233	(164,725)
Estimated third-party payor settlements	1,366,257	(715,849)
Net cash from (used for) operating activities	$ 1,913,466	$ (471,123)
Supplemental Disclosure of Cash Flow Information		
Property and equipment purchased through capital leases	$ -	$ 82,947
Capital asset acquisitions included in accounts payable	$ -	$ 379,195
Cash paid on construction payable	$ 379,195	$ -

Note 1 - Organization and Significant Accounting Policies

Arbuckle Memorial Hospital Authority

Arbuckle Memorial Hospital Authority (Authority) is a public trust which was formed by Murray County, Oklahoma (Trustor) to facilitate the construction of a new hospital through the issuance of hospital and sales tax revenue bonds. The beneficiary of the trust is Murray County. The Authority's board is made up of members of Arbuckle Memorial Hospital's (Hospital) Board of Directors. The Authority is considered to be a component unit of Murray County.

The Hospital is owned by Murray County and governed by a Board of Directors. The Board of County Commissioners appoints the Board of Directors of the Hospital. The Hospital is a 25 bed facility that provides acute care services in Sulphur, Oklahoma and is a component unit of Murray County.

The Murray County Healthcare Foundation (Foundation) was formed as a non-profit 501(c)(3) organization, whose purpose is to receive contributions and help provide financial resources for the Hospital. As the Foundation exists for the exclusive benefit and support of the Hospital, it is included as a component in the Authority's financial statements using the blended method. All significant intercompany accounts and transactions have been eliminated in the combined financial statements.

Income Taxes

The Authority is exempt from income taxes under Internal Revenue Code Section 115 and a similar provision of state law as a political subdivision of the State of Oklahoma.

The Foundation is a not-for-profit corporation and has been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code.

The Foundation believes it has appropriate support for any tax positions taken affecting its annual filing requirements, and as such, does not have any uncertain tax positions that are material to the financial statements. The Foundation would recognize future accrued interest and penalties related to unrecognized tax benefits and liabilities in income tax expense if such interest and penalties are incurred. The Foundation has determined it is not subject to unrelated business income tax and has not filed an Exempt Organization Business Income Tax Return (Form 990T) with the IRS.

Proprietary Fund Accounting

The Authority uses proprietary fund accounting. Revenues and expenses are recognized on the accrual basis. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, the Authority has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

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 and 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 assets limited as to use.

Patient Receivables

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

Supplies

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

Assets Limited as to Use

Assets limited as to use include assets held by trustees under an indenture agreement. Assets limited as to use that are available for obligations classified as current liabilities are reported in current assets.

Deferred Financing Costs

Deferred financing costs are amortized over the period the related obligation is outstanding using the straight-line method.

Capital Assets

Capital asset acquisitions in excess of $1,000 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:

	Depreciable Life
Land improvements	2 - 40 years
Building, improvements, and fixed equipment	5 - 40 years
Major moveable equipment	3 - 20 years

Compensated Absences

The Authority's policies permit most employees to accumulate vacation leave 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 benefits 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 are presented in the following three components:

Net Assets Invested in Capital Assets, Net of Related Debt – Net assets invested in capital assets net of related debt consists of capital assets, net of accumulated depreciation and reduced by the current balances of any outstanding debt used to finance the purchase or construction of those assets.

Expendable Restricted Net Assets – Expendable restricted net assets are non-capital net assets that must be used for a particular purpose, as specified by creditor, grantors, or contributors external to the Authority.

Unrestricted Net Assets - Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets, net of related debt or restricted.

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 accrued 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 that 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 $258,000 and $162,000 for the years ended December 31, 2011 and 2010, calculated by multiplying the ratio of cost to gross charges for the Hospital by the gross uncompensated charges associated with providing charity care to its patients.

Advertising Costs

The Authority expenses advertising costs as incurred.

Operating Revenues and Expenses

The Authority's statement of revenues, expenses, and changes in net assets distinguishes between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, the Authority's principal activity. Non-exchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as non-operating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Grants and Contributions

From time to time, the Authority receives grants from individuals and private organizations. Revenues from grants and contributions 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 restricted or that are restricted to a specific operating purpose are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses as capital contributions.

Risk Management

The Authority 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.

Reclassification

Certain amounts in the 2010 financial statements have been reclassified to conform to the 2011 presentation. The reclassifications had no impact on previously reported changes in net assets.

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: The Authority is licensed as a Critical Access Hospital (CAH). The Authority is reimbursed for most acute care services at cost plus 1% with final settlement determined after submission of annual cost reports by the Authority and are subject to audits thereof by the Medicare intermediary. The Authority's Medicare cost reports have been audited by the Medicare fiscal intermediary through the year ended December 31, 2009. Clinical services are paid on a cost basis or fixed fee schedule.

Medicaid: Inpatient and outpatient services rendered to patients covered by the state Medicaid program are reimbursed on a prospectively determined per diem rate or established fee.

Other: 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.

Revenue from the Medicare and Medicaid programs accounts for approximately 68.8% and 6.5%, respectively, of the Authority's net patient service revenue for the year ended December 31, 2011 and 69.5% and 6.6%, respectively, for the year ended December 31, 2010. 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 Centers for Medicare and Medicaid Services (CMS) has implemented a Recovery Audit Contractor (RAC) program under which claims subsequent to October 1, 2007, are reviewed by contractors for validity, accuracy, and proper documentation. A demonstration project completed in several other states resulted in the identification of potential overpayments, some being significant. If selected for audit, the potential exists that the Authority may incur a liability for a claims overpayments at a future date. The Authority is unable to determine if it will be audited and, if so, the extent of the liability of overpayments, if any. As the outcome of such potential reviews is unknown and cannot be reasonably estimated, it is the Authority's policy to adjust revenue for deductions from overpayment amounts or additions from underpayment amounts determined under the RAC audits at the time a change in reimbursement is agreed upon between the Authority and CMS.

A summary of patient service revenue and contractual adjustments for the years ended December 31, 2011 and 2010 is as follows:

	2011	2010
Total patient and resident service revenue	$ 23,134,392	$ 19,822,059
Contractual adjustments		
Medicare and Medicaid	(6,778,076)	(5,457,853)
Other	(2,358,200)	(1,724,060)
Provisions for bad debt	(2,689,283)	(2,105,911)
Total contractual adjustments and provisions for bad debt	(11,825,559)	(9,287,824)
Net patient and resident service revenue	$ 11,308,833	$ 10,534,235

Note 3 - Cash and Deposits

Custodial Credit Risk – Exposure to custodial credit risk related to deposits exists when the Authority holds deposits that are uninsured and uncollateralized; collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the Authority's name; or collateralized without a written or approved collateral agreement. Exposure to custodial credit risk related to investments exists when the Authority holds investments that are uninsured and unregistered, with securities held by the counterparty or by its trust department or agent by not in the Authority's name**.** The Authority secures cash deposits in excess of $250,000 with U.S. Government or Federal Agency securities. State law requires all deposits of public funds to be collateralized.

	2011	2010
Insured (FDIC)	$ 968,249	$ 871,484
Collateralized by U.S. government securities held by the Authority's agents in the Authority's name	2,909,895	1,596,068
Uncollateralized	2,362	462
Total	$ 3,880,506	$ 2,468,014

The carrying amount of the Authority's deposites shown above are included in the balance sheets at December 31, 2011 and 2010 as follows:

	2011	2010
Carrying value		
Deposits	$ 3,154,376	$ 1,584,362
Deposits - assets limited to use	543,846	883,471
Total carrying value	$ 3,698,222	$ 2,467,833

Investment Credit Risk – Investment credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Authority's investment practices limits investments to the following types of securities: U.S. Treasury securities, Federal Agency securities, and certificates of deposits

Concentration of Investment Credit Risk – Exposure to concentration of credit risk is considered to exist when investments in any one issuer represent a significant percent of total investments. Investments issued or explicitly guaranteed by the U.S. government and investment in mutual funds, external investment pools, and other pooled investments are excluded from this consideration.

Note 4 - Assets Limited as to Use

The Authority's investments generally are reported at fair value. Assets limited as to use are held in the Authority's name by a custodial bank that is an agency of the Authority.

Investment income on assets limited as to use, cash equivalents, and other investments consists of interest income. Investment income was $11,381 and $17,250 for the years ended December 31, 2011 and 2010, respectively.

Assets Limited as to Use

Assets limited as to use are as follows:

	2011	2010
By Board of Trustees for capital acquisitions		
Cash and cash equivalents	$ 543,846	$ 883,471
Held by Trustee for Debt Service		
U.S. Treasury Obligations included in current assets	727,715	754,068
U.S. Treasury Obligations	1,249,175	1,256,735
Total assets limited as to use	$ 2,520,736	$ 2,894,274

Note 5 - Capital Assets

Capital assets additions, retirements, and balances for the year ended December 31, 2011 are as follows:

	Balance 2010	Additions	Deductions	Transfers	Balance 2011
Non-depreciable capital assets					
Land	$ 58,799	$ -	$ -	$ -	$ 58,799
Total non-depreciable capital assets	58,799	-	-	-	58,799
Depreciable capital assets					
Buildings and fixed equipment	16,231,643	-	-	-	16,231,643
Major moveable equipment	3,452,735	257,473	-	-	3,710,208
Total depreciable capital assets	19,684,378	257,473	-	-	19,941,851
Less accumulated depreciation for					
Building and fixed equipment	(1,941,778)	(897,394)	-	-	(2,839,172)
Major moveable equipment	(1,570,516)	(507,816)	-	-	(2,078,332)
Total accumulated depreciation	(3,512,294)	(1,405,210)	-	-	(4,917,504)
Net depreciable capital assets	16,172,084	(1,147,737)	-	-	15,024,347
Capital assets, net	$ 16,230,883	$ (1,147,737)	$ -	$ -	$ 15,083,146

Capital assets additions, retirements, and balances for the year ended December 31, 2010 are as follows:

	Balance 2009	Additions	Deductions	Transfers	Balance 2010
Non-depreciable capital assets					
Land	$ 58,799	$ -	$ -	$ -	$ 58,799
Total non-depreciable capital assets	58,799	-	-	-	58,799
Depreciable capital assets					
Buildings and fixed equipment	15,654,246	38,497	-	538,900	16,231,643
Major moveable equipment	3,148,747	303,988	-	-	3,452,735
Construction in progress	87,930	450,970	-	(538,900)	-
Total depreciable capital assets	18,890,923	793,455	-	-	19,684,378
Less accumulated depreciation for					
Building and fixed equipment	(1,083,061)	(858,717)	-	-	(1,941,778)
Major moveable equipment	(1,076,262)	(494,254)	-	-	(1,570,516)
Total accumulated depreciation	(2,159,323)	(1,352,971)	-	-	(3,512,294)
Net depreciable capital assets	16,731,600	(559,516)	-	-	16,172,084
Capital assets, net	$ 16,790,399	$ (559,516)	$ -	$ -	$ 16,230,883

Note 6 - Leases

The Authority leases certain equipment under non-cancelable long-term lease agreements. Certain leases have been recorded as capitalized leases and others as operating leases. At December 31, 2011 and 2010, the capitalized leased assets consisted of:

	2011	2010
Major movable equipment	$ 1,766,546	$ 2,250,458
Less accumulated amortization (included as depreciation on the accompanying financial statements)	(822,358)	(428,730)
Total	$ 944,188	$ 1,821,728

Note 7 - Debt

At December 31, 2011 and 2010, long-term debt consisted of:

	Balance 12/31/10	Additions	Deductions	Balance 12/31/11	Amounts Due Within One Year
Series 2008 Revenue Bonds payable	$ 14,790,000	$ -	$ (180,000)	$ 14,610,000	$ 190,000
Capital lease obligation	1,572,672	-	(358,159)	1,214,513	349,014
Total notes	$ 16,362,672	$ -	$ (538,159)	$ 15,824,513	$ 539,014

	Balance 12/31/09	Additions	Deductions	Balance 12/31/10	Amounts Due Within One Year
Series 2008 Revenue Bonds payable	$ 14,890,000	$ -	$ (100,000)	$ 14,790,000	$ 180,000
Capital lease obligation	1,720,648	82,947	(230,923)	1,572,672	358,158
Total notes	$ 16,610,648	$ 82,947	$ (330,923)	$ 16,362,672	$ 538,158

The terms and due dates of the Authority's long-term debt, including capital lease obligations at December 31, 2011 and 2010 are as follows:

(1) 7.00% to 7.25% bond payable, due January 1, 2038, collateralized by the net revenues, accounts receivables, and assets included under the indenture.
(2) Capital lease obligations, at varying rates of imputed interest from 3% to 5%, collateralized by leased equipment with a cost of $1,766,546.

Under the terms of the Revenue Bond Indenture agreement, the Authority is required to maintain certain deposits with a trustee. Such deposits are included with assets limited as to use in the balance sheets. The Revenue Bond Indenture also places limits on the incurrence of additional borrowings and requires that the Authority satisfy certain measures of financial performance as long as the notes are outstanding. At December 31, 2011 and 2010, the Authority was in compliance with the covenants of the Revenue Bond.

At December 31, 2011 and 2010, scheduled principal and interest repayments on long-term debt and payments on capital lease obligations were as follows:

	Bonds Payable		Capital Lease Obligations	
Year Ending December 31:	Principal	Interest	Principal	Interest
2012	$ 190,000	$ 1,055,075	$ 349,014	$ 31,656
2013	205,000	1,041,775	359,630	21,041
2014	220,000	1,027,425	370,568	10,102
2015	235,000	1,012,025	135,301	986
2016	250,000	995,575	-	-
Thereafter	13,510,000	13,912,800	-	-
Total	$ 14,610,000	$ 19,044,675	$ 1,214,513	$ 63,785

Note 8 - Employee Benefit Plan

The Authority contributes to a defined contribution pension plan covering substantially all employees. Beginning in 1998, the Authority implemented an employer match which is determined by the Board annually. Pension expense is recorded for the amount of the Authority's contributions, determined in accordance with the terms of the plan. The plan is administered by a Board of Trustees appointed by the governing body of the Authority. The plan provides retirement benefits to plan members and their beneficiaries. Benefit provisions and contribution requirements are contained in the plan document and were established and can be amended by action of the Authority's governing body. For the years ended December 31, 2011 and 2010, all the Authority provided a 4% match totaling $49,089 and $51,626, respectively.

Note 9 - Concentrations of Credit Risk

The Authority grants credit without collateral to its patients, most of who are insured under third-party payor agreements. The mix of receivables from third-party payors and patients at December 31, 2011 and 2010 was as follows:

	2011	2010
Medicare	29%	30%
Medicaid	6%	8%
Other third-party payors	22%	15%
Patients	43%	47%
Total	100%	100%

Note 10 - 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 $2 million. An additional umbrella policy provides protection against losses on a claims-made basis subject to a limit of $1 million per claim and an annual aggregate of $3 million. Should the claims-made policies not be renewed or replaced with equivalent insurance, claims based on occurrences during the term, but reported subsequently, would be uninsured.

Note 11 - Related Party Transactions

On June 1, 1998, the Authority entered into a management agreement with Preferred Management Corporation, and Mercy Memorial Health Center, whereby Mercy Memorial Health Center agreed to provide Hospital-physician liaison services and information systems and Preferred Management Corporation agreed to administer the operations of the Authority and provide shared services for a predetermined fee. Fees incurred under the management agreement were $260,445 and $216,408 for the years ended December 31, 2011 and 2010, respectively.

The Murray County Healthcare Foundation raises funds on behalf of the Hospital, which are contributed to the Hospital based on availability and need. During the years ended December 31, 2011 and 2010 the Foundation made contributions to the Hospital of $377,985 and $506,391, respectively. These amounts are eliminated in the combined financial statements.

Note 12 - Medicaid Electronic Health Record (EHR)

During the year ended December 31, 2011, the Authority received incentive payments of $150,000 from Medicaid to implement electronic health record technology. At the time this report was issued, no authoritative guidance had been provided regarding the accounting treatment of Medicaid EHR. payments. In the absence of authoritative guidance, management had recorded this transaction in other operating income similar in nature to an exchange transaction.

Note 13 - Subsequent Events

The Authority evaluated events and transactions occurring subsequent to December 31, 2011 and through June 18, 2012, the date of issuance of the financial statements. During this period, there were no subsequent events requiring recognition in the combined financial statements.

Supplementary Information
December 31, 2011 and 2010

Arbuckle Memorial Hospital Authority

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Independent Auditor's Report on Supplementary Information

The Board of Directors
Arbuckle Memorial Hospital Authority
Sulphur, Oklahoma

We have audited the financial statements of Arbuckle Memorial Hospital Authority as of and for the year ended December 31, 2011 and our report thereon dated June 18, 2012, which expresses an unqualified opinion on those financial statements, appears on page 1. Our audit was conducted for the purpose of forming an opinion on the combined financial statements as a whole. The schedules of net patient service revenue – hospital only, schedules of other revenue – hospital only, and schedules of expenses – hospital only on page 24, are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Eide Bailly LLP

Oklahoma City, Oklahoma
June 18, 2012

	2011			2010		
	Inpatient	Outpatient	Total	Inpatient	Outpatient	Total
Routine Services						
Adults and pediatrics	$ 700,313	$ 1,058,850	$ 1,759,163	$ 610,146	$ 690,000	$ 1,300,146
Ancillary Services						
Operating room	5,729	234,746	240,475	16,581	236,466	253,047
Radiology	257,314	3,727,278	3,984,592	209,789	3,095,402	3,305,191
Laboratory	514,318	2,794,889	3,309,207	415,037	2,644,953	3,059,990
Respiratory therapy	680,624	218,278	898,902	586,116	159,994	746,110
Physical therapy	546,327	431,854	978,181	394,385	142,200	536,585
Electrocardiology	180,937	506,509	687,446	184,674	488,045	672,719
Medical supplies	2,103,188	893,287	2,996,475	1,801,833	950,273	2,752,106
Pharmacy	1,205,251	911,983	2,117,234	1,097,072	1,019,775	2,116,847
Clinic	-	1,156,688	1,156,688	-	843,458	843,458
Emergency	12,199	2,267,948	2,280,147	11,381	2,039,362	2,050,743
Physician fees	334,907	2,049,577	2,384,484	369,784	1,004,538	1,374,322
Special care	23,326	766,472	789,798	5,335	1,071,637	1,076,972
Total ancillary services	5,864,120	15,959,509	21,823,629	5,091,987	13,696,103	18,788,090
Charity Care	(448,400)	-	(448,400)	(266,177)	-	(266,177)
Gross Patient Service Revenue	$ 6,116,033	$ 17,018,359	23,134,392	$ 5,435,956	$ 14,386,103	19,822,059
Contractual adjustments and Provision for Bad Debts						
Medicare and Medicaid			(6,778,076)			(5,457,853)
Other			(2,358,200)			(1,724,060)
Provision for bad debts			(2,689,283)			(2,105,911)
Total contractual adjustments and provision for bad debts			(11,825,559)			(9,287,824)
Net patient service revenue			$ 11,308,833			$ 10,534,235

	2011	2010
Other Revenues		
Medical records	$ 1,902	$ 2,184
Miscellaneous	22,161	14,587
Total other revenues	$ 24,063	$ 16,771

	2011			2010		
	Salaries	Other	Total	Salaries	Other	Total
Nursing Services						
Adults and pediatrics	$ 1,446,427	$ 90,376	$ 1,536,803	$ 1,334,113	$ 66,461	$ 1,400,574
Other Professional Services						
Operating room	-	74,068	74,068	-	89,494	89,494
Radiology	246,582	206,849	453,431	243,489	170,897	414,386
Laboratory	280,620	427,996	708,616	271,387	422,564	693,951
Respiratory therapy	120,298	73,378	193,676	111,120	66,671	177,791
Physical therapy	130,699	508,150	638,849	-	607,423	607,423
Medical supplies	-	202,759	202,759	-	89,356	89,356
Pharmacy	52,757	363,732	416,489	53,166	365,250	418,416
Clinic	773,169	159,323	932,492	574,170	146,023	720,193
Emergency	1,821,352	19,397	1,840,749	1,760,341	12,037	1,772,378
Total other professional services	3,425,477	2,035,652	5,461,129	3,013,673	1,969,715	4,983,388
General Services						
Dietary	103,969	75,126	179,095	96,718	58,988	155,706
Plant operations and maintenance	82,117	283,027	365,144	92,797	274,689	367,486
Housekeeping	132,327	26,234	158,561	129,082	28,670	157,752
Laundry	-	72,667	72,667	-	60,561	60,561
Medical records	87,735	72,112	159,847	75,852	28,852	104,704
Total general services	406,148	529,166	935,314	394,449	451,760	846,209
Administrative Services						
Administration and general	631,879	1,140,057	1,771,936	591,179	1,047,627	1,638,806
Nursing administration	309,747	8,385	318,132	301,724	12,079	313,803
Employee health and welfare	-	979,018	979,018	-	917,853	917,853
Total administrative services	941,626	2,127,460	3,069,086	892,903	1,977,559	2,870,462
Depreciation and Amortization	-	1,428,645	1,428,645	-	1,376,405	1,376,405
Total expenses	$ 6,219,678	$ 6,211,299	$ 12,430,977	$ 5,635,138	$ 5,841,900	$ 11,477,038

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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*

The Board of Directors
Arbuckle Memorial Hospital Authority
Sulphur, Oklahoma

We have audited the combined financial statements of Arbuckle Memorial Hospital Authority, as of and for the year ended December 31, 2011, and have issued our report thereon dated June 18, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit of the combined financial statements of Arbuckle Memorial Hospital Authority as of and for the year ended December 31, 2011, in accordance with auditing standards generally accepted in the United States of America, we considered Arbuckle Memorial Hospital Authority's internal control over financial reporting (internal control) 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 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 first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses and therefore, no assurance that all deficiencies, significant deficiencies and material weakness have been identified. However described in the schedule of findings we identified a deficiency in internal over financial reporting that we consider to be a material weakness.

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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 entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency 2011-01 in the accompanying schedule of findings to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Arbuckle Memorial Hospital Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, non-compliance with which could have a direct 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.

We noted certain other matters that were reported to management and the Board of Directors in a separate letter dated June 18, 2012.

Arbuckle Memorial Hospital Authority's response to the findings identified in our audit is described in the accompanying schedule of findings. We did not audit Arbuckle Memorial Hospital Authority's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Board of Directors, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Eide Bailly LLP

Oklahoma City, Oklahoma
June 18, 2012

2011-01 – Provision for Uncollectible Accounts

Condition and Criteria: Accounts receivable should be presented net of estimated allowances. Allowances should be made for all payor types to properly reflect the expected cash payments to be received. The estimate should be based on historical trends for each payor class.

Effect: We noted that while a calculation is performed for each payor class, it is not based on historical information that can be supported. This resulted in a material audit adjustment for private pay patients with balances aged less than 120 days.

Cause: Management has not tracked the historical activity for private pay patients in a fashion that allows for an appropriate estimate of future cash collections.

Auditor's Recommendation: We recommend that management review and establish effective procedures for evaluating contractual adjustments and allowances for bad debts. These procedures should incorporate methods for tracking information based on payor class and should be evaluated on a periodic basis.

Corrective Action Plan: Management will develop a method to determine allowances that is based on historical trends.