

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Auditor's Reports and Financial Statements
December 31, 2012 and 2011



Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
December 31, 2012 and 2011

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Independent Auditor's Report

Board of Trustees
Cleveland Area Hospital Trust Authority
Cleveland, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of Cleveland Area Hospital Trust Authority, a component unit of the City of Cleveland, Oklahoma, which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of revenues, expenses and changes in net position and cash flows for the years 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Cleveland Area Hospital Trust Authority as of December 31, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

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

Other Matters

Our audit was conducted for the purpose of forming an opinion on the basic financial statements as a whole. The combining schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 27, 2014, 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.

BKD, LLP

Tulsa, Oklahoma
January 27, 2014

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Management's Discussion and Analysis
Years Ended December 31, 2012 and 2011

Introduction

This management's discussion and analysis of the financial performance of Cleveland Area Hospital Trust Authority (the Authority) provides an overview of the Authority's financial activities for the years ended December 31, 2012 and 2011. It should be read in conjunction with the accompanying financial statements of the Authority.

Financial Highlights

- Cash increased in 2012 by \$480,042 (51%) and decreased in 2011 by \$294,348 (24%).
- Estimated amounts due to third-party payers increased in 2012 by \$1,335,562 (311%) and decreased in 2011 by \$1,940,000 (128%).
- Capital assets, net of depreciation expense decreased in 2012 by \$988,510 (17%) and increased in 2011 by \$1,498,833 (36%).
- Long-term debt decreased in 2012 by \$1,811,697 (29%) and increased in 2011 by \$2,805,210 (83%).
- The Authority's net position increased in 2012 by \$394,696 (40%) and decreased in 2011 by \$656,388 (40%).
- The Authority reported operating income in 2012 of \$268,646 and operating loss in 2011 of \$(791,217). The operating income in 2012 improved by \$1,059,863 (134%) over 2011 and the operating loss in 2011 increased by \$51,917 (7%) over the operating loss reported in 2010.

Using This Annual Report

The Authority's financial statements consist of three statements—a balance sheet; a statement of revenues, expenses and changes in net position; and a statement of cash flows. These statements provide information about the activities of the Authority, including resources held by the Authority but restricted for specific purposes by creditors, 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 Balance Sheet and Statement of Revenues, Expenses and Changes in Net Position

One of the most important questions asked about any organization's finances is, "Is the organization as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses and changes in net 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 all liabilities using the accrual basis of accounting. Using the accrual basis of accounting means that all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Authority's net position and changes therein. The Authority's total net position—the difference between assets and liabilities—is one measure of the Authority's financial health or financial position. Over time, increases or decreases in the Authority's net position is an indicator of whether its financial health is improving or deteriorating. Other nonfinancial factors, such as changes in the Authority's patient base, changes in legislation and regulations, measures of the quantity and quality of services provided to its patients and local economic factors, should also be considered to assess the overall financial health of the Authority.

The Statement of Cash Flows

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

The Authority's Net Position

The Authority's net position is the difference between its assets and liabilities reported in the accompanying balance sheets. The Authority's net position increased by \$394,696 (40%) in 2012 over 2011 and decreased by \$656,388 (40%) in 2011 over 2010 as shown in Table 1.

Table 1: Assets, Liabilities and Net Position

	2012	2011	2010
Assets			
Patient accounts receivable, net	\$ 1,106,897	\$ 1,277,795	\$ 1,328,928
Other current assets	1,748,740	1,699,329	1,598,194
Capital assets, net	4,685,742	5,674,252	4,175,419
Other noncurrent assets	219,092	176,732	198,203
Total assets	<u>\$ 7,760,471</u>	<u>\$ 8,828,108</u>	<u>\$ 7,300,744</u>
Liabilities			
Long-term debt, including current maturities	\$ 4,355,480	\$ 6,167,177	\$ 3,361,967
Other current and noncurrent liabilities	2,028,931	1,679,567	2,301,025
Total liabilities	<u>6,384,411</u>	<u>7,846,744</u>	<u>5,662,992</u>
Net Position			
Net investment in capital assets	2,380,424	3,208,412	1,866,402
Restricted – expendable for debt service	109,732	108,497	100,000
Unrestricted	(1,114,096)	(2,335,545)	(328,650)
Total net position	<u>1,376,060</u>	<u>981,364</u>	<u>1,637,752</u>
Total liabilities and net position	<u>\$ 7,760,471</u>	<u>\$ 8,828,108</u>	<u>\$ 7,300,744</u>

A significant change in the Authority's assets in 2012 is the decrease in capital assets, due to offsetting the Medicare electronic health record (EHR) incentive payment against the cost of the EHR software (see *Note 1*). Accounts payable and long-term debt both decreased from 2011 to 2012. Accounts payable decreased by \$625,233 (55%) due to paying off the liabilities associated with the EHR implementation while long-term debt decreased by \$1,811,697 (29%) due to paying off previous Medicare cost report liabilities. Another significant change in financial position relates to the estimated amounts due to or from third-party payers. At December 31, 2012, the estimated amount due to third-party payers was \$905,562 compared to an estimated amount due from third-party payers of \$430,000 at December 31, 2011. The cause of this change was primarily due to changes in interim payment rates from Medicare compared to changes in the Hospital's costs from higher inpatient and swing bed volumes.

A significant change in the Authority's assets in 2011 is the increase in capital assets, which increased by \$1,498,833 (36%) due to the implementation of the EHR system and construction of a medical office building. This activity also contributed to the increase in 2011 of long-term debt of \$2,805,210 (83%) compared to 2010. Another significant change in financial position relates to the estimated amounts due to or from third-party payers. In 2010, the Authority had an estimated amount due to third-party payers of \$1,510,000. This amount was converted to long-term debt in 2011. At December 31, 2011, the Authority had an estimated amount due from third-party payers of \$430,000, or a reduction of \$1,940,000 (128%), compared to 2010.

Operating Results and Changes in the Authority's Net Position

In 2012, the Authority's net position increased by \$394,696 (40%) as shown in Table 2. This increase is made up of several different components and represents an improvement of 168% compared with the decrease in net position for 2011 of \$656,388.

Table 2: Operating Results and Changes in Net Position

	2012	2011	2010
Operating Revenues			
Net patient service revenue	\$ 11,469,350	\$ 11,952,120	\$ 10,811,602
Other operating revenues	946,140	820,304	310,938
Total operating revenues	12,415,490	12,772,424	11,122,540
Operating Expenses			
Salaries and wages and employee benefits	7,502,339	8,256,416	7,136,989
Purchased services and professional fees	2,088,849	3,036,255	2,618,861
Other operating expenses	2,209,644	1,976,667	1,856,540
Depreciation	346,012	294,303	249,450
Total operating expenses	12,146,844	13,563,641	11,861,840
Operating Income (Loss)	268,646	(791,217)	(739,300)
Nonoperating Revenues (Expenses)			
City appropriations – unrestricted	494,648	450,261	417,652
Investment income (loss)	(42,477)	(19,078)	61,171
Noncapital gifts and grants	-	-	9,101
Interest expense	(326,121)	(296,354)	(197,157)
Total nonoperating revenues (expenses)	126,050	134,829	290,767
Excess (Deficiency) of Revenues over Expenses and Increase (Decrease) in Net Position	<u>\$ 394,696</u>	<u>\$ (656,388)</u>	<u>\$ (448,533)</u>

Operating Income (Loss)

The first component of the overall change in the Authority's net position is its operating income or loss—generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. Since acquiring Cleveland Area Hospital Holdings, Inc., and Pawnee Home Health Care, Inc., in January 2009, the Authority has reported operating losses until fiscal year 2012. This is consistent with the Authority's recent operating history as the Authority was formed and is operated primarily to serve residents of Cleveland, Oklahoma, and the surrounding area. The Authority receives sales tax appropriations levied by the City of Cleveland, Oklahoma (the City) to provide sufficient resources to enable the facility to serve lower income and other residents.

The operating income for 2012 improved by \$1,059,863 (134%) as compared to 2011. The primary components of the change in operating income are:

- A decrease in net patient service revenue of \$482,770 (4%)
- A decrease in salaries and wages and employee benefits of \$754,077 (9%)
- A decrease in purchased services and professional fees of \$947,406 (31%)

Net patient service revenue decreased in 2012 as compared to 2011 as a result of lower emergency room and outpatient volumes, reductions in home health volume and increased contractual discount rates. These discounts were partially offset by the recognition of approximately \$838,000 of revenue related to Oklahoma's Supplemental Hospital Offset Payment Program in 2012. Employee salaries and wages decreased in 2012 in connection with the elimination of certain key positions and a reduction in paid hours. The decrease in purchased services and professional fees primarily relates to the reduction in EHR conversion costs in 2012 compared to 2011.

The operating loss for 2011 worsened by \$51,917 (7%) as compared to 2010. The primary components of the change in operating loss are:

- An increase in net patient service revenue of \$1,140,518 (11%)
- An increase in salaries and wages and employee benefits of \$1,119,427 (16%)
- An increase in purchased services and professional fees of \$417,394 (16%)

Net patient service revenue increased in 2011 as compared to 2010 as a result of higher outpatient volumes and a significant decrease in provision for uncollectible accounts. Total inpatient days at the Hospital decreased by 375 days (22%) in 2011 compared to 2010. This decrease was offset by higher outpatient volumes at the Hospital and other business units. In 2010, the Authority began to more closely monitor the patient accounts receivable activity, and there has been a reduction in patient receivables of 25% since December 31, 2010. This increased monitoring contributed to fewer uncollectible accounts and the 43% decrease in provision for uncollectible accounts in 2011.

Employee salaries and wages increased in 2011 in connection with the Authority's retention and recruitment efforts. Employee benefits increased in 2011 due to an increase in employees and higher health insurance costs than in 2010.

The increase in purchased services and professional fees primarily relate to implementation costs for the new EHR system.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of sales tax appropriations levied by the City and investment income and interest expense. The nonoperating revenues and expenses in 2012 were consistent with the amounts in 2011.

The Authority's Cash Flows

Changes in the Authority's cash flows are consistent with changes in operating losses and nonoperating revenues and expenses for 2012 and 2011 with the exception of the changes in estimated amounts due from/to third-party payers and the reduction in accounts payable, discussed earlier.

Capital Assets and Debt Administration

Capital Assets

At the end of 2012 and 2011, the Authority had \$4,685,742 and \$5,674,252, respectively, invested in capital assets, net of accumulated depreciation, as detailed in *Note 5* to the financial statements. In 2012, the Authority purchased new equipment costing \$36,985 and disposed of assets totaling \$691,000 related to the EHR incentive program. In 2011, the Authority purchased new equipment costing \$942,339 and completed construction of a medical office building and other projects with additions of \$850,296.

Debt

At December 31, 2012 and 2011, the Authority had \$4,355,480 and \$6,167,177, respectively, in notes payable and capital lease obligations outstanding. In 2012, the Authority issued \$1,500,000 of new debt. In 2011, the Authority converted \$2,131,647 due to the Centers for Medicare and Medicaid Services related to the 2011 and 2010 Medicare cost reports to long-term debt. The Authority also entered into two notes payable to vendors for equipment, including EHR technology, totaling \$1,289,975.

Contacting the Authority's Financial Management

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. Questions about this report and requests for additional financial information should be directed to the Authority's administrative office by telephoning 918.358.9980.

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Balance Sheets
December 31, 2012 and 2011

Assets

	2012	2011
Current Assets		
Cash	\$ 1,422,657	\$ 942,615
Patient accounts receivable, net of allowance; 2012 – \$541,000, 2011 – \$505,000	1,106,897	1,277,795
Other receivables	100,663	98,436
Supplies	159,178	224,641
Estimated amounts due from third-party payers	-	430,000
Prepaid expenses and other	66,242	3,637
Total current assets	<u>2,855,637</u>	<u>2,977,124</u>
Noncurrent Cash and Investments		
Restricted under loan agreement	109,732	108,497
Other long-term investments	7,740	54,680
	<u>117,472</u>	<u>163,177</u>
Capital Assets, Net	<u>4,685,742</u>	<u>5,674,252</u>
Other Assets	<u>101,620</u>	<u>13,555</u>
Total assets	<u><u>\$ 7,760,471</u></u>	<u><u>\$ 8,828,108</u></u>

Liabilities and Net Position

Current Liabilities		
Current maturities of long-term debt	\$ 2,363,356	\$ 3,588,852
Accounts payable	516,633	1,141,866
Accrued expenses	606,736	537,701
Estimated amounts due to third-party payers	905,562	-
Total current liabilities	4,392,287	5,268,419
Long-Term Debt	<u>1,992,124</u>	<u>2,578,325</u>
Total liabilities	<u>6,384,411</u>	<u>7,846,744</u>
Net Position		
Net investment in capital assets	2,380,424	3,208,412
Restricted – expendable for debt service	109,732	108,497
Unrestricted	(1,114,096)	(2,335,545)
Total net position	<u>1,376,060</u>	<u>981,364</u>
Total liabilities and net position	<u><u>\$ 7,760,471</u></u>	<u><u>\$ 8,828,108</u></u>

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2012 – \$1,004,027, 2011 – \$1,027,641	\$ 11,469,350	\$ 11,952,120
Other	946,140	820,304
	<u>12,415,490</u>	<u>12,772,424</u>
Operating Expenses		
Salaries and wages	6,063,390	6,714,791
Employee benefits	1,438,949	1,541,625
Purchased services and professional fees	2,088,849	3,036,255
Supplies and other	2,209,644	1,976,667
Depreciation	346,012	294,303
	<u>12,146,844</u>	<u>13,563,641</u>
	<u>268,646</u>	<u>(791,217)</u>
Operating Income (Loss)		
Nonoperating Revenues (Expenses)		
City appropriations – unrestricted	494,648	450,261
Investment loss	(42,477)	(19,078)
Interest expense	(326,121)	(296,354)
	<u>126,050</u>	<u>134,829</u>
	<u>394,696</u>	<u>(656,388)</u>
Excess (Deficiency) of Revenues over Expenses and Increase (Decrease) in Net Position		
Net Position, Beginning of Year	<u>981,364</u>	<u>1,637,752</u>
Net Position, End of Year	<u><u>\$ 1,376,060</u></u>	<u><u>\$ 981,364</u></u>

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Statements of Cash Flows
Years Ended December 31, 2012 and 2011

	2012	2011
Operating Activities		
Receipts from and on behalf of patients	\$ 12,975,810	\$ 11,745,275
Payments to suppliers and contractors	(4,920,058)	(4,110,516)
Payments to and on behalf of employees	(7,433,304)	(8,221,431)
Other receipts and payments, net	946,140	820,786
	<u>1,568,588</u>	<u>234,114</u>
Investing Activities		
Purchase of investments	(1,235)	(8,497)
Investment income received	4,463	9,983
	<u>3,228</u>	<u>1,486</u>
Noncapital Financing Activities		
Interest paid on long-term debt	(180,537)	(153,523)
Proceeds from issuance of long-term debt	1,500,000	949,143
Principal paid on long-term debt	(2,267,739)	(1,057,330)
Deferred financing costs paid	(91,102)	-
City appropriations received	494,648	436,836
	<u>(544,730)</u>	<u>175,126</u>
Capital and Related Financing Activities		
Proceeds from issuance of long-term debt	-	1,289,975
Interest paid on long-term debt	(145,584)	(142,831)
Principal paid on long-term debt	(1,043,958)	(59,082)
Payments received related to disposal of capital assets	679,483	-
Purchase of capital assets	(36,985)	(1,793,136)
	<u>(547,044)</u>	<u>(705,074)</u>
Increase (Decrease) in Cash	480,042	(294,348)
Cash, Beginning of Year	<u>942,615</u>	<u>1,236,963</u>
Cash, End of Year	<u><u>\$ 1,422,657</u></u>	<u><u>\$ 942,615</u></u>

See Notes to Financial Statements

	2012	2011
Reconciliation of Net Operating Revenues (Expenses) to Net Cash		
Provided by Operating Activities		
Operating income (loss)	\$ 268,646	\$ (791,217)
Depreciation	346,012	294,303
Provision for uncollectible accounts	1,004,027	1,027,641
Changes in operating assets and liabilities		
Patient accounts receivable, net	(833,129)	(976,508)
Supplies, prepaid expenses and other	3,668	48,849
Estimated amounts due from/to third-party payers	1,335,562	(257,496)
Accounts payable and accrued expenses	(556,198)	888,542
	<u>\$ 1,568,588</u>	<u>\$ 234,114</u>
Supplemental Cash Flows Information		
Conversion of estimated amount due to third-party payers to long-term debt	\$ -	\$ 1,682,504

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Notes to Financial Statements
December 31, 2012 and 2011

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

Nature of Operations and Reporting Entity

Cleveland Area Hospital Trust Authority (the Authority) was created under a trust indenture dated November 22, 1976, as a public trust under provisions of Title 60 of the Oklahoma Statutes for the benefit of the citizens of Cleveland, Oklahoma. The Authority is a component unit of the City of Cleveland, Oklahoma (the City), and the Cleveland City Council appoints the board members of the Authority.

The Authority operates Cleveland Area Hospital Holdings, Inc. (the Hospital). The Hospital is a critical access hospital located in Cleveland, Oklahoma. The Hospital primarily earns revenue by providing inpatient, outpatient and emergency care services to patients in Cleveland, Oklahoma, and the surrounding area.

The Authority also operates Pawnee County Home Health Care, Inc. (PCHH), which earns revenue by providing home health services to the citizens of Cleveland, Oklahoma, and the surrounding area.

Both the Hospital and PCHH were incorporated in November 2008. On January 1, 2009, the Hospital and PCHH were acquired from the previous owner by the Authority. As the Authority is the sole corporate member of the Hospital and PCHH, both the Hospital and PCHH are included as blended component units in the accompanying financial statements of the Authority.

Basis of Accounting and Presentation

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

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and deferred inflows and outflows of resources 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.

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Notes to Financial Statements
December 31, 2012 and 2011

Cash and Cash Equivalents

The Authority considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2012 and 2011, the Authority had no cash equivalents.

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 did not exceed this commercial coverage in any of the three preceding years.

Investments and Investment Income

All investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes interest income and the net change for the year in the fair value of investments carried at fair value.

Patient Accounts Receivable

The Authority reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Authority provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Supplies

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

Capital Assets

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

Land improvements	5–40 years
Buildings and improvements	5–40 years
Equipment	3–20 years

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Notes to Financial Statements
December 31, 2012 and 2011

Deferred Financing Costs

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt using the straight-line method and are included in other assets on the accompanying balance sheets.

Compensated Absences

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

Net Position

Net position of the Authority is classified in three components. Net investment in capital assets consists of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net position is made up of noncapital assets that must be used for a particular purpose, as specified by creditors, grantors or donors external to the Authority, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets or restricted net position.

Net Patient Service Revenue

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

Charity Care

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

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Notes to Financial Statements
December 31, 2012 and 2011

Income Taxes

As an essential government function of the City, the Authority is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Authority is subject to federal income tax on any unrelated business taxable income.

City Appropriations

Effective January 27, 1978, the citizens of the City approved a 1% sales tax with no expiration date to provide unrestricted appropriations to the Authority.

The Authority received approximately 4% and 3% of its financial support from city appropriations related to sales taxes during the years ended December 31, 2012 and 2011, respectively. These funds were used to support operations and make payments on long-term debt.

Electronic Health Records Incentive Program

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records (EHR) technology. Critical access hospitals (CAHs) are eligible to receive incentive payments in the cost reporting period beginning in the federal fiscal year in which meaningful use criteria have been met. The Medicare incentive payment is for qualifying costs of the purchase of certified EHR technology multiplied by the Hospital's Medicare share fraction, which includes a 20% incentive. This payment is an acceleration of amounts that would have been received in future periods based on reimbursable costs incurred, including depreciation. If meaningful use criteria are not met in future periods, the Hospital is subject to penalties that would reduce future payments for services. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services (CMS). The final amount for any payment year under both programs is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Authority believes CMS intended to pay CAHs a grant under the EHR incentive payment program specifically to purchase an asset that will be used in providing services to all patients. In 2012, the Authority accounted for the Medicare EHR incentive amount by deducting the incentive amount of approximately \$680,000 in calculating the carrying amount of the asset. This approach recognizes the incentive payment in the accompanying statements of revenues, expenses and changes in net position over the life of the depreciable asset as a reduction to depreciation expense.

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In 2011, the Hospital completed the first-year requirements under the Medicaid program and recorded revenue of approximately \$289,000, which is included in other revenue within operating revenues in the accompanying statements of revenues, expenses and changes in net position.

Supplemental Hospital Offset Payment Program

On January 17, 2012, CMS approved the State of Oklahoma's Supplemental Hospital Offset Payment Program (SHOPP). The SHOPP program is retroactive to July 1, 2011, and is currently scheduled to sunset on December 31, 2017. The SHOPP program is designed to assess certain 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.

Critical access hospitals are excluded from paying an assessment fee but are still eligible to receive SHOPP funds. During 2012, the Hospital recognized approximately \$838,000 of revenue related to the SHOPP program. The annual amounts to be received by the Hospital over the term of the SHOPP program are subject to change annually based on various factors involved in determining the amount of federal matching funds. The estimated annual amount to be received by the Hospital over the term of the SHOPP program is approximately \$588,000.

Reclassifications

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

Note 2: Net Patient Service Revenue

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

- **Medicare** – Inpatient services rendered to Medicare program beneficiaries are paid based on a cost reimbursement methodology. Certain outpatient services related to Medicare beneficiaries are paid based on a combination of fee schedules and a cost reimbursement methodology. 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. The Hospital's Medicare cost reports have been audited by the Medicare administrative contractor through December 31, 2010.
- **Medicaid** – The Authority is 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. Those payment rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

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Approximately 77% and 73% of the Authority's net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2012 and 2011, respectively. Laws and regulations governing Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Authority has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider 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.

Note 3: Deposits, Investments and Investment Income

Deposits

Custodial credit risk is the risk that in the event of a bank failure a government's deposits may not be returned to it. The Authority's deposit policy for custodial credit risk requires compliance with the provisions of state law, which requires collateralization of all deposits with federal depository insurance or other acceptable collateral in specific amounts.

At December 31, 2012 and 2011, approximately \$938,000 and \$239,000 of the Authority's bank balances of \$1,762,746 and \$1,215,263, respectively, were exposed to custodial credit risk as being uninsured and uncollateralized.

Investments

The Authority may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in corporate bonds and equity securities.

At December 31, 2012 and 2011, the Authority had \$7,740 and \$54,680, respectively, in a corporate stock.

- **Interest Rate Risk** – The Authority does not currently have an investment policy limiting its exposure to fair value losses arising from rising interest rates.
- **Credit Risk** – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The Authority does not currently have an investment policy addressing credit risk.

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- **Custodial Credit Risk** – For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty the Authority will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Authority does not currently have an investment policy addressing how securities are to be held.
- **Concentration of Credit Risk** – The Authority places no limit on the amount that may be invested in any one issuer. At December 31, 2012 and 2011, the Authority held investments in only one corporation.

Summary of Carrying Values

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

	<u>2012</u>	<u>2011</u>
Carrying value		
Deposits	\$ 1,532,389	\$ 1,051,112
Investments	<u>7,740</u>	<u>54,680</u>
	<u>\$ 1,540,129</u>	<u>\$ 1,105,792</u>
Included in the following balance sheet captions		
Cash	\$ 1,422,657	\$ 942,615
Noncurrent cash and investments		
Restricted under loan agreement	109,732	108,497
Other long-term investments	<u>7,740</u>	<u>54,680</u>
	<u>\$ 1,540,129</u>	<u>\$ 1,105,792</u>

Investment Income (Loss)

Investment income (loss) for the years ended December 31, 2012 and 2011, consisted of:

	<u>2012</u>	<u>2011</u>
Interest and dividend income	\$ 4,463	\$ 9,983
Net decrease in fair value of investments	<u>(46,940)</u>	<u>(29,061)</u>
	<u>\$ (42,477)</u>	<u>\$ (19,078)</u>

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Note 4: Patient Accounts Receivable

The Authority grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31, 2012 and 2011, consisted of:

	2012	2011
Medicare	\$ 609,858	\$ 916,812
Medicaid	63,352	61,248
Other third-party payers	296,990	353,443
Patients	<u>677,697</u>	<u>451,292</u>
	1,647,897	1,782,795
Less allowance for uncollectible amounts	<u>541,000</u>	<u>505,000</u>
	<u><u>\$ 1,106,897</u></u>	<u><u>\$ 1,277,795</u></u>

Note 5: Capital Assets

Capital assets activity for the years ended December 31, 2012 and 2011, were:

	2012			
	Beginning Balance	Additions	Disposals	Transfers
Land	\$ 79,717	\$ -	\$ -	\$ -
Land improvements	176,509	-	-	101,848
Buildings and improvements	5,519,394	-	-	(60,135)
Equipment	3,216,225	33,740	(691,000)	-
Construction in progress	<u>69,242</u>	<u>3,245</u>	<u>-</u>	<u>(41,713)</u>
	9,061,087	36,985	(691,000)	-
	<u>9,061,087</u>	<u>36,985</u>	<u>(691,000)</u>	<u>-</u>
Less accumulated depreciation				
Land improvements	1,816	6,052	-	-
Buildings and improvements	1,358,378	170,940	-	-
Equipment	<u>2,026,641</u>	<u>169,020</u>	<u>(11,517)</u>	<u>-</u>
	3,386,835	346,012	(11,517)	-
	<u>3,386,835</u>	<u>346,012</u>	<u>(11,517)</u>	<u>-</u>
Capital assets, net	<u><u>\$ 5,674,252</u></u>	<u><u>\$ (309,027)</u></u>	<u><u>\$ (679,483)</u></u>	<u><u>\$ -</u></u>

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	2011				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 79,717	\$ -	\$ -	\$ -	\$ 79,717
Land improvements	142,861	501	-	33,147	176,509
Buildings and improvements	4,707,899	-	-	811,495	5,519,394
Equipment	2,253,406	942,339	-	20,480	3,216,225
Construction in progress	84,068	850,296	-	(865,122)	69,242
	<u>7,267,951</u>	<u>1,793,136</u>	<u>-</u>	<u>-</u>	<u>9,061,087</u>
Less accumulated depreciation					
Land improvements	330	1,486	-	-	1,816
Buildings and improvements	1,213,008	145,370	-	-	1,358,378
Equipment	1,879,194	147,447	-	-	2,026,641
	<u>3,092,532</u>	<u>294,303</u>	<u>-</u>	<u>-</u>	<u>3,386,835</u>
Capital assets, net	<u>\$ 4,175,419</u>	<u>\$ 1,498,833</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 5,674,252</u>

The disposals during the year ended December 31, 2012, primarily related to the Medicare EHR incentive program discussed in *Note 1*.

Note 6: Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses included in current liabilities at December 31 consisted of:

	2012	2011
Payable to suppliers and contractors	\$ 516,633	\$ 1,141,866
Payable to employees (including payroll taxes and benefits)	597,575	528,540
Interest payable	<u>9,161</u>	<u>9,161</u>
Total	<u>\$ 1,123,369</u>	<u>\$ 1,679,567</u>

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Note 7: Long-Term Debt

The following is a summary of long-term obligation transactions for the Authority for the years ended December 31:

	2012				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Notes payable to bank	\$ 2,633,971	\$ 1,500,000	\$ (652,693)	\$ 3,481,278	\$ 2,055,998
Note payable to Central Oklahoma Economic Development District, Inc.	467,190	-	(41,216)	425,974	43,325
Note payable to vendor (A)	255,545	-	(76,268)	179,277	72,507
Note payable to vendor (B)	1,008,165	-	(1,008,165)	-	-
Notes payable to CMS	1,650,000	-	(1,497,562)	152,438	152,438
Capital lease obligations	152,306	-	(35,793)	116,513	39,088
	<u>\$ 6,167,177</u>	<u>\$ 1,500,000</u>	<u>\$ (3,311,697)</u>	<u>\$ 4,355,480</u>	<u>\$ 2,363,356</u>

	2011				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Notes payable to bank	\$ 2,813,978	\$ -	\$ (180,007)	\$ 2,633,971	\$ 2,633,971
Note payable to Central Oklahoma Economic Development District, Inc.	362,866	500,000	(395,676)	467,190	41,216
Note payable to vendor (A)	-	255,545	-	255,545	60,521
Note payable to vendor (B)	-	1,034,430	(26,265)	1,008,165	-
Notes payable to CMS	-	2,131,647	(481,647)	1,650,000	817,351
Capital lease obligations	185,123	-	(32,817)	152,306	35,793
	<u>\$ 3,361,967</u>	<u>\$ 3,921,622</u>	<u>\$ (1,116,412)</u>	<u>\$ 6,167,177</u>	<u>\$ 3,588,852</u>

Notes Payable to Bank

The first note payable to bank is due in full upon the bank's demand, but if no demand is made the note payable is due August 2016 with principal and interest payable monthly. Interest is payable at the New York prime rate plus 1.25% with a floor of 5% and a ceiling of 8%. The interest rate is 5% at December 31, 2011. The note is secured by all inventory and equipment of the Authority and an assignment of half of the Authority's city appropriation revenue. The outstanding principal amount on this note was \$0 and \$575,982 at December 31, 2012 and 2011, respectively. During 2012, this note was refinanced through a new loan (see paragraph regarding the third note payable to bank).

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The second note payable to bank is due in full upon the bank's demand, but if no demand is made then the note payable is due December 2018 with monthly payments of \$14,275, including interest at 6%. The note is secured by a certificate of deposit of approximately \$110,000 held at the lending institution, a mortgage on the medical office building owned by the Authority and an assignment of all rents related to the medical office building. This note payable includes a balloon payment in December 2018. The outstanding principal amount on this note was \$2,009,528 and \$2,057,989 at December 31, 2012 and 2011, respectively.

In April 2012, the Authority issued a third note payable to bank in the amount of \$1,500,000. This third note payable to bank is due April 2032 with monthly payments of \$9,875, including interest at the Farmer Mac 3-Month Cost of Funds Index Net Yield plus 3.5% (4.97% at December 31, 2012). The note is secured by certain real property and an assignment of one quarter of the Authority's city appropriation revenue. The outstanding principal amount on this note was \$1,471,750 at December 31, 2012.

Assuming no demand is made by the bank, the debt service requirements for these notes as of December 31, 2012, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2013	\$ 289,794	\$ 98,695	\$ 191,099
2014	287,311	104,279	183,032
2015	289,794	110,182	179,612
2016	289,794	116,422	173,372
2017	289,794	123,019	166,775
2018–2022	2,407,471	2,043,748	363,723
2023–2027	592,470	422,369	170,101
2028–2032	514,946	462,564	52,382
	<u>\$ 4,961,374</u>	<u>\$ 3,481,278</u>	<u>\$ 1,480,096</u>

Note Payable to Central Oklahoma Economic Development District, Inc.

During 2011, the Authority refinanced its note with the Central Oklahoma Economic Development District, Inc. The refinanced note is due February 2021, with principal and interest at 5%, payable monthly. The note is secured by an assignment of half of the Authority's city appropriation revenue.

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The debt service requirements for this note as of December 31, 2012, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2013	\$ 63,640	\$ 43,325	\$ 20,315
2014	63,639	45,541	18,098
2015	63,639	47,871	15,768
2016	63,639	50,320	13,319
2017	63,640	52,895	10,745
2018–2022	<u>201,525</u>	<u>186,022</u>	<u>15,503</u>
	<u>\$ 519,722</u>	<u>\$ 425,974</u>	<u>\$ 93,748</u>

Note Payable to Vendor (A)

During 2011, the Authority entered into a financing agreement with a vendor. The note is due by June 2016 and is payable at amounts ranging from \$3,200 to \$6,652 per month with interest imputed at 5%. The note is secured by certain major movable equipment.

The debt service requirements for this note as of December 31, 2012, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2013	\$ 79,824	\$ 72,507	\$ 7,317
2014	38,400	33,830	4,570
2015	38,400	35,561	2,839
2016	<u>38,399</u>	<u>37,379</u>	<u>1,020</u>
	<u>\$ 195,023</u>	<u>\$ 179,277</u>	<u>\$ 15,746</u>

Note Payable to Vendor (B)

During 2011, the Authority entered into a financing agreement with the vendor implementing its EHR technology. The note included interest of 1.25% per month. Monthly payments of \$12,415, which primarily represent interest only payments, are required plus supplemental principal payments as funds related to the Medicare and Medicaid EHR Incentive Program (see *Note 1*) are received by the Authority. This note was paid off during 2012.

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Notes Payable to CMS

During 2011, the Authority entered into two notes payable with CMS related to amounts owed on the 2010 final cost report and the 2011 interim cost report. These notes are unsecured, originally due in 2012 and 2014, and are being paid on a monthly basis, including interest between 11.0% and 11.5% per annum. In addition to the regularly scheduled principal payments, CMS can withhold any cost report settlement amounts to be applied against the outstanding balances.

During 2012, the note related to the 2011 interim cost report was paid off.

As of December 31, 2012, the outstanding balance on the note related to the 2010 final cost report was \$152,438 and is included in current maturities of long-term debt.

Capital Lease Obligations

The Authority is obligated under leases for equipment that are accounted for as capital leases. Assets under capital leases at December 31, 2012 and 2011, totaled \$193,215, net of accumulated depreciation of \$93,387 and \$48,346, respectively. The following is a schedule by year of future minimum lease payments under the capital lease including interest at 12.7% together with the present value of the future minimum lease payments as of December 31, 2012:

Year Ending December 31,	
2013	\$ 48,030
2014	48,030
2015	<u>36,023</u>
Total minimum lease payments	132,083
Less amount representing interest	<u>15,570</u>
Present value of future minimum lease payments	<u><u>\$ 116,513</u></u>

Note 8: Charity Care and Other Community Benefits

In support of its mission, the Authority voluntarily provides free care to patients who lack financial resources and are deemed to be medically indigent. Because the Authority does not pursue collection of amounts determined to qualify as charity care, they are not reported in net patient service revenue. In addition, the Authority provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts which are less than established charges for the services provided to the recipients, and many times the payments are less than the cost of rendering the services provided.

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Uncompensated costs related to these services are approximately as follows:

	2012	2011
Charity care allowances	\$ 22,100	\$ 27,300
Medicaid contractual adjustments	<u>1,222,300</u>	<u>1,658,400</u>
Total	<u><u>\$ 1,244,400</u></u>	<u><u>\$ 1,685,700</u></u>

The cost of uncompensated care is estimated by applying the ratio of costs to gross charges from the 2012 Medicare cost report to the uncompensated care charges.

In addition to uncompensated charges, the Authority also commits significant time and resources to endeavors and critical services which meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screening and assessments and community educational services.

Note 9: Medical Malpractice Claims

The Authority purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Authority's claims experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

Note 10: Contingencies

Litigation

In the normal course of business, the Authority is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Authority evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

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Note 11: Retirement Plan

Effective January 1, 2009, the Authority created a 401(k) defined contribution plan covering substantially all employees. Effective June 7, 2010, the Board of Trustees for the Authority voted to terminate the 401(k) plan and establish separate 403(b) plans for the Hospital and PCHH.

Pension expense is recorded for the amount of the Authority's required contributions determined in accordance with the terms of the plans. The plans are administered by the Authority's Board of Trustees. The plans provide retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan documents and were established and can be amended by action of the Authority's governing body. Contributions actually made by plan members and the Authority aggregated approximately \$170,000 and \$90,000, respectively, for 2012 and \$123,000 and \$87,000, respectively, for 2011.

Note 12: Operating Leases

The Authority has noncancellable operating leases for medical equipment which expire in 2013. Future minimum lease payments at December 31, 2012, were approximately \$171,000.

Rental expense for the years ended December 31, 2012 and 2011, was approximately \$470,000 and \$434,000, respectively.

Note 13: Current Economic Conditions

The current economic environment presents hospitals with unprecedented circumstances and challenges, which in some cases have resulted in large declines in the fair value of investments and other assets, large declines in contributions, constraints on liquidity and difficulty obtaining financing. The accompanying financial statements have been prepared using values and information currently available to the Authority.

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

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

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Note 14: Patient Protection and Affordable Care Act

The *Patient Protection and Affordable Care Act* (PPACA) will substantially reform the United States health care system. The legislation impacts multiple aspects of the health care system, including many provisions that change payments from Medicare, Medicaid and insurance companies. Starting in 2014, the legislation requires the establishment of health insurance exchanges, which will provide individuals without employer-provided health care coverage the opportunity to purchase insurance. It is anticipated that some employers currently offering insurance to employees will opt to have employees seek insurance coverage through the insurance exchanges. It is possible the reimbursement rates paid by insurers participating in the insurance exchanges may be substantially different than rates paid under current health insurance products. Another significant component of the PPACA is the expansion of the Medicaid program to a wide range of newly eligible individuals. In anticipation of this expansion, payments under certain existing programs, such as Medicare disproportionate share, will be substantially decreased. Each state's participation in an expanded Medicaid program is optional.

The state of Oklahoma has currently indicated it will not expand the Medicaid program, which may result in revenues from newly covered individuals not offsetting the Authority's reduced revenue from other Medicare/Medicaid programs.

The PPACA is extremely complex and may be difficult for the federal government and each state to implement. While the overall impact of the PPACA cannot currently be estimated, it is possible it will have a negative impact on the Authority's net patient service revenue. In addition, it is possible the Authority will experience payment delays and other operational challenges during PPACA's implementation.

Supplementary Information

Cleveland Area Hospital Trust Authority
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Combining Schedule – Balance Sheet Information
December 31, 2012

	Cleveland Area Hospital Trust Authority	Cleveland Area Hospital Holdings, Inc.	Pawnee County Home Health Care, Inc.	Subtotal	Eliminations	Total
Assets						
Current Assets						
Cash	\$ 314,253	\$ 1,056,213	\$ 52,191	\$ 1,422,657	\$ -	\$ 1,422,657
Patient accounts receivable, net of allowance of \$541,000	63,661	928,211	115,025	1,106,897	-	1,106,897
Other receivables	90,623	-	10,040	100,663	-	100,663
Supplies	12,064	128,455	18,659	159,178	-	159,178
Prepaid expenses and other	27,780	38,462	-	66,242	-	66,242
Total current assets	508,381	2,151,341	195,915	2,855,637	-	2,855,637
Noncurrent Cash and Investments						
Restricted under loan agreement	109,732	-	-	109,732	-	109,732
Other long-term investments	7,740	-	-	7,740	-	7,740
	117,472	-	-	117,472	-	117,472
Capital Assets, Net	4,320,897	364,845	-	4,685,742	-	4,685,742
Other Assets	88,065	13,285	270	101,620	-	101,620
Total assets	\$ 5,034,815	\$ 2,529,471	\$ 196,185	\$ 7,760,471	\$ -	\$ 7,760,471
Liabilities and Net Position						
Current Liabilities						
Current maturities of long-term debt	\$ 2,077,071	\$ 286,285	\$ -	\$ 2,363,356	\$ -	\$ 2,363,356
Accounts payable	86,527	419,284	10,822	516,633	-	516,633
Accrued expenses	118,325	423,563	64,848	606,736	-	606,736
Estimated amounts due to third-party payers	-	905,562	-	905,562	-	905,562
Total current liabilities	2,281,923	2,034,694	75,670	4,392,287	-	4,392,287
Long-Term Debt	1,465,135	526,989	-	1,992,124	-	1,992,124
Total liabilities	3,747,058	2,561,683	75,670	6,384,411	-	6,384,411
Net Position						
Net investment in capital assets	2,250,441	129,983	-	2,380,424	-	2,380,424
Restricted – expendable for debt service	109,732	-	-	109,732	-	109,732
Unrestricted	(1,072,416)	(162,195)	120,515	(1,114,096)	-	(1,114,096)
Total net position	1,287,757	(32,212)	120,515	1,376,060	-	1,376,060
Total liabilities and net position	\$ 5,034,815	\$ 2,529,471	\$ 196,185	\$ 7,760,471	\$ -	\$ 7,760,471

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Combining Schedule – Balance Sheet Information
December 31, 2011

	Cleveland Area Hospital Trust Authority	Cleveland Area Hospital Holdings, Inc.	Pawnee County Home Health Care, Inc.	Subtotal	Eliminations	Total
Assets						
Current Assets						
Cash	\$ 517,256	\$ 339,182	\$ 86,177	\$ 942,615	\$ -	\$ 942,615
Patient accounts receivable, net of allowance of \$505,000	58,615	1,069,764	149,416	1,277,795	-	1,277,795
Other receivables	78,973	-	19,463	98,436	-	98,436
Supplies	8,983	197,379	18,279	224,641	-	224,641
Estimated amounts due from third-party payers	-	430,000	-	430,000	-	430,000
Prepaid expenses and other	3,637	-	-	3,637	-	3,637
Total current assets	667,464	2,036,325	273,335	2,977,124	-	2,977,124
Noncurrent Cash and Investments						
Restricted under loan agreement	108,497	-	-	108,497	-	108,497
Other long-term investments	54,680	-	-	54,680	-	54,680
	163,177	-	-	163,177	-	163,177
Capital Assets, Net	4,551,800	1,122,452	-	5,674,252	-	5,674,252
Other Assets	-	13,285	270	13,555	-	13,555
Total assets	\$ 5,382,441	\$ 3,172,062	\$ 273,605	\$ 8,828,108	\$ -	\$ 8,828,108
Liabilities and Net Position						
Current Liabilities						
Current maturities of long-term debt	\$ 2,653,891	\$ 934,961	\$ -	\$ 3,588,852	\$ -	\$ 3,588,852
Accounts payable	259,278	872,101	10,487	1,141,866	-	1,141,866
Accrued expenses	164,387	290,177	83,137	537,701	-	537,701
Total current liabilities	3,077,556	2,097,239	93,624	5,268,419	-	5,268,419
Long-Term Debt	60,928	2,517,397	-	2,578,325	-	2,578,325
Total liabilities	3,138,484	4,614,636	93,624	7,846,744	-	7,846,744
Net Position						
Net investment in capital assets	2,412,963	795,449	-	3,208,412	-	3,208,412
Restricted – expendable for debt service	108,497	-	-	108,497	-	108,497
Unrestricted	(277,503)	(2,238,023)	179,981	(2,335,545)	-	(2,335,545)
Total net position	2,243,957	(1,442,574)	179,981	981,364	-	981,364
Total liabilities and net position	\$ 5,382,441	\$ 3,172,062	\$ 273,605	\$ 8,828,108	\$ -	\$ 8,828,108

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Combining Schedule – Statement of Revenues, Expenses and
Changes in Net Position Information
Year Ended December 31, 2012

	Cleveland Area Hospital Trust Authority	Cleveland Area Hospital Holdings, Inc.	Pawnee County Home Health Care, Inc.	Subtotal	Eliminations	Total
Operating Revenues						
Net patient service revenue, net of provision for uncollectible accounts of \$1,004,027	\$ 928,891	\$ 9,239,845	\$ 1,300,614	\$ 11,469,350	\$ -	\$ 11,469,350
Other	297,232	644,933	3,975	946,140	-	946,140
Total operating revenues	1,226,123	9,884,778	1,304,589	12,415,490	-	12,415,490
Operating Expenses						
Salaries and wages	1,407,524	3,635,701	1,020,165	6,063,390	-	6,063,390
Employee benefits	619,270	626,160	193,519	1,438,949	-	1,438,949
Purchased services and professional fees	71,674	1,981,227	35,948	2,088,849	-	2,088,849
Supplies and other	401,981	1,590,617	217,046	2,209,644	-	2,209,644
Depreciation	234,148	111,864	-	346,012	-	346,012
Overhead allocation	(1,845,841)	1,787,188	58,653	-	-	-
Total operating expenses	888,756	9,732,757	1,525,331	12,146,844	-	12,146,844
Operating Income (Loss)	337,367	152,021	(220,742)	268,646	-	268,646
Nonoperating Revenues (Expenses)						
City appropriations – unrestricted	494,648	-	-	494,648	-	494,648
Investment income (loss)	(45,343)	2,861	5	(42,477)	-	(42,477)
Interest expense	(184,667)	(141,454)	-	(326,121)	-	(326,121)
Total nonoperating revenues (expenses)	264,638	(138,593)	5	126,050	-	126,050
Excess (Deficiency) of Revenues over Expenses Before Transfers	602,005	13,428	(220,737)	394,696	-	394,696
Transfers	(1,558,205)	1,396,934	161,271	-	-	-
Increase (Decrease) in Net Position	(956,200)	1,410,362	(59,466)	394,696	-	394,696
Net Position, Beginning of Year	2,243,957	(1,442,574)	179,981	981,364	-	981,364
Net Position, End of Year	\$ 1,287,757	\$ (32,212)	\$ 120,515	\$ 1,376,060	\$ -	\$ 1,376,060

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Combining Schedule – Statement of Revenues, Expenses and
Changes in Net Position Information
Year Ended December 31, 2011

	Cleveland Area Hospital Trust Authority	Cleveland Area Hospital Holdings, Inc.	Pawnee County Home Health Care, Inc.	Subtotal	Eliminations	Total
Operating Revenues						
Net patient service revenue, net of provision for uncollectible accounts of \$1,027,641	\$ 648,804	\$ 9,468,142	\$ 1,835,174	\$ 11,952,120	\$ -	\$ 11,952,120
Other income	440,263	379,904	137	820,304	-	820,304
Total operating revenues	1,089,067	9,848,046	1,835,311	12,772,424	-	12,772,424
Operating Expenses						
Salaries and wages	1,380,506	4,188,976	1,145,309	6,714,791	-	6,714,791
Employee benefits	1,146,717	329,919	64,989	1,541,625	-	1,541,625
Purchased services and professional fees	160,622	2,830,891	44,742	3,036,255	-	3,036,255
Supplies and other	316,135	1,525,445	135,087	1,976,667	-	1,976,667
Depreciation	224,891	69,412	-	294,303	-	294,303
Overhead allocation	(1,977,105)	1,917,483	59,622	-	-	-
Total operating expenses	1,251,766	10,862,126	1,449,749	13,563,641	-	13,563,641
Operating Income (Loss)	(162,699)	(1,014,080)	385,562	(791,217)	-	(791,217)
Nonoperating Revenues (Expenses)						
City appropriations – unrestricted	450,261	-	-	450,261	-	450,261
Investment income (loss)	(20,196)	788	330	(19,078)	-	(19,078)
Interest expense	(159,298)	(137,056)	-	(296,354)	-	(296,354)
Total nonoperating revenues (expenses)	270,767	(136,268)	330	134,829	-	134,829
Excess (Deficiency) of Revenues over Expenses Before Transfers	108,068	(1,150,348)	385,892	(656,388)	-	(656,388)
Transfers	382,281	275,743	(658,024)	-	-	-
Increase (Decrease) in Net Position	490,349	(874,605)	(272,132)	(656,388)	-	(656,388)
Net Position, Beginning of Year	1,753,608	(567,969)	452,113	1,637,752	-	1,637,752
Net Position, End of Year	\$ 2,243,957	\$ (1,442,574)	\$ 179,981	\$ 981,364	\$ -	\$ 981,364

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

Board of Trustees
Cleveland Area Hospital Trust Authority
Cleveland, 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 Cleveland Area Hospital Trust Authority (the Authority), which comprise the balance sheet as of December 31, 2012, 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, and have issued our report thereon dated January 27, 2014.

Internal Control over Financial Reporting

Management of the Authority is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit, we considered the Authority's 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 that might be material weaknesses or significant deficiencies and, therefore, there can be no assurance that all material weaknesses or significant deficiencies have been identified. However, as discussed in the accompanying schedule of findings and responses, we identified a certain deficiency in internal control that we consider to be a material weakness.

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 deficiency described in the accompanying schedule of findings and responses as item 2012-1 to be a material weakness.

Board of Trustees
Cleveland Area Hospital Trust Authority

Compliance

As part of obtaining reasonable assurance about whether the 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, 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 the Finding

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

Other Matters

We also noted certain matters that we reported to the Authority's management in a separate letter dated January 27, 2014.

The purpose of this communication 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 compliance. This communication 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.

BKD, LLP

Tulsa, Oklahoma
January 27, 2014

Cleveland Area Hospital Trust Authority
A Component Unit of the City of Cleveland, Oklahoma
Schedule of Findings and Responses
Year Ended December 31, 2012

Reference Number	Finding
2012-1	<p>Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting.</p> <p>Condition – Management’s procedures for reconciling balance sheet accounts were not sufficient or not performed timely enough to identify necessary adjustments.</p> <p>Context – Errors existed in several balance sheet accounts related to reconciliations and control accounts were not reconciled to supporting documentation causing the need to record adjusting entries during the audit.</p> <p>Effect – Potentially material misstatements in the financial statements could occur.</p> <p>Cause – The reconciliation processes in place were not sufficient to properly state balances, including capital assets and accrued liabilities. In addition, the process of preparing estimates of allowances for contractual adjustments and bad debts and estimated amounts due from or to third-party payers were inadequate.</p> <p>Recommendation – Management should evaluate the procedures in place related to reconciling material balance sheet accounts to supporting schedules and the methodologies used to estimate significant allowances and estimates in the financial statements.</p> <p>Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will take steps to periodically review the material balance sheet account reconciliations and periodically evaluate the methodologies used in accurately estimating allowances and estimates.</p>