Memorial Hospital of Texas County

Auditor's Reports and Financial Statements

June 30, 2013 and 2012

BKD LLP
CPAs & Advisors

Memorial Hospital of Texas County
June 30, 2013 and 2012

Contents

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Independent Auditor's Report on Financial Statements

Board of Control
Memorial Hospital of Texas County
Guymon, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of Memorial Hospital of Texas County (the Hospital), which comprise the balance sheets as of June 30, 2013 and 2012, 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 respective financial position of the Hospital as of June 30, 2013 and 2012, 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.

Emphasis of Matter

The accompanying financial statements have been prepared assuming the Hospital will continue as a going concern. As discussed in *Note 16*, the Hospital has suffered recurring losses from operations and negative cash flows from operations, which raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in *Note 16*. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 31, 2014, on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control over financial reporting and compliance.

BKD, LLP

Tulsa, Oklahoma
March 31, 2014

Memorial Hospital of Texas County

Management's Discussion and Analysis

Years Ended June 30, 2013 and 2012

Introduction

This management's discussion and analysis of the financial performance of Memorial Hospital of Texas County (the Hospital) provides an overview of the Hospital's financial activities for the years ended June 30, 2013 and 2012. It should be read in conjunction with the accompanying financial statements of the Hospital.

Financial Highlights

- Cash and short-term deposits decreased in 2013 by $478,685 or 55% and decreased in 2012 by $2,098,819 or 71%.
- The Hospital's net position decreased in 2013 by $1,316,224 or 15% and decreased in 2012 by $3,046,505 or 26%.
- The Hospital reported an operating loss in 2013 of $3,481,051 and 2012 of $3,114,821. The operating loss in 2013 increased by $366,230 or 12% over the operating loss reported in 2012. The operating loss in 2012 increased by $1,245,365 or 67% over the operating loss reported in 2011.
- Net nonoperating revenues increased by $1,642,179 or 4,651% in 2013 compared to 2012 and decreased by $91,252 or 72% in 2012 compared to 2011.

Using This Annual Report

The Hospital's financial statements consist of three statements—a balance sheet; a statement of revenues, expenses and changes in net position; and a statement of cash flows. These statements provide information about the activities of the Hospital. The Hospital is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

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

One of the most important questions asked about any hospital's finances is, "Is the hospital as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses and changes in net position report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. Using the accrual basis of accounting means that all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

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

The Statement of Cash Flows

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

The Hospital's Net Position

The Hospital's net position is the difference between its assets and liabilities reported in the balance sheet. The Hospital's net position decreased by $1,316,224 or 15% in 2013 over 2012 and decreased by $3,046,505 or 26% in 2012 over 2011.

Table 1: Assets, Liabilities and Net Position

	2013	2012	2011
Assets			
Cash and short-term deposits	$ 398,532	$ 877,217	$ 2,976,036
Patient accounts receivable, net	2,521,159	2,838,723	2,548,111
Capital assets, net	6,278,320	6,882,984	7,655,581
Other current and noncurrent assets	1,476,611	1,511,082	1,630,945
Total assets	$ 10,674,622	$ 12,110,006	$ 14,810,673
Liabilities			
Long-term debt, including current maturities	$ -	$ 465,935	$ 736,732
Other current and noncurrent liabilities	3,250,637	2,903,862	2,287,227
Total liabilities	3,250,637	3,369,797	3,023,959
Net Position			
Net investment in capital assets	6,228,625	6,412,749	6,863,915
Unrestricted	1,195,360	2,327,460	4,922,799
Total net position	7,423,985	8,740,209	11,786,714
Total liabilities and net position	$ 10,674,622	$ 12,110,006	$ 14,810,673

Some significant changes in the Hospital's assets and liabilities in 2013 are:

- A decrease in cash and short-term deposits of $478,685 or 55% due to the Hospital utilizing cash reserves to fund operating losses
- A decrease in net patient accounts receivable of $317,564 or 11% due to a decrease in net patient service revenue and due to an increase in the overall aging of accounts receivable, which required a higher allowance for uncollectible accounts
- An increase in accounts payable of $764,659 or 44% as the Hospital has held invoices longer due to cash shortages
- A decrease in accrued expenses of $457,884 or 39% due to a decrease in accrued self-insured employee health claims

Some significant changes in the Hospital's assets and liabilities in 2012 were the decrease in cash and short-term deposits and the increase in accounts payable and other current liabilities. The decrease in cash and short-term deposits of $2,098,819 or 71% is due primarily as a result of funding operating losses and increased accounts receivable. The increase in accounts payable of $522,086 or 43% primarily relates to the Hospital changing its cash flow management policy on timing of payments to vendors.

Operating Results and Changes in the Hospital's Net Position

In 2013, the Hospital's net position decreased by $1,316,224 or 15% as shown in Table 2. This decrease is made up of several different components and represents an increase of $1,730,281, compared with the decrease in net position for 2012 of $3,046,505.

Table 2: Operating Results and Changes in Net Position

	2013	2012	2011
Operating Revenues			
Net patient service revenue	$ 14,678,125	$ 17,878,434	$ 17,888,070
Other operating revenues	912,994	480,932	289,874
Total operating revenues	15,591,119	18,359,366	18,177,944
Operating Expenses			
Salaries and wages and employee benefits	9,073,808	11,453,515	10,640,937
Purchased services and professional fees	3,794,357	3,758,675	3,539,109
Other operating expenses	5,210,683	5,158,885	4,598,226
Depreciation	993,322	1,103,112	1,269,128
Total operating expenses	19,072,170	21,474,187	20,047,400
Operating Loss	(3,481,051)	(3,114,821)	(1,869,456)
Nonoperating Revenues (Expenses)			
Noncapital gifts	1,714,378	-	-
Gain on investment in joint venture	-	71,741	124,632
Investment income	3,942	15,827	49,468
Interest expense	(40,833)	(52,260)	(47,540)
Total nonoperating revenues (expenses)	1,677,487	35,308	126,560
Deficiency of Revenues over Expenses Before Capital Grants and Gifts	(1,803,564)	(3,079,513)	(1,742,896)
Capital Grants and Gifts	487,340	33,008	74,346
Decrease in Net Position	$ (1,316,224)	$ (3,046,505)	$ (1,668,550)

Operating Loss

The first component of the overall change in the Hospital'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. In each of the past three years, the Hospital has reported an operating loss. This is consistent with the Hospital's recent operating history as the Hospital was formed and is operated primarily to serve residents of Guymon, Oklahoma, and the surrounding area.

The operating loss for 2013 increased by $366,230 or 12% compared to 2012. The primary components of the increased operating loss are:

- A decrease in net patient service revenue of $3,200,309 or 18% due primarily to decreased patient volumes and as a result of the closure of the home health, physical therapy and High Plains internal medicine, and increased competition related to certain radiological services

- A decrease in salaries and wages and employee benefits for the Hospital's employees of $2,379,707 or 21% due to a decrease in total full-time equivalent number of employees, the termination of two employed physicians, a decrease in self-funded health insurance claims expense and due to severance payments made to the Hospital's former CEO during 2012

- An increase in other operating revenue of $432,062 or 90% due to the Hospital completing the first-year requirements under the Medicaid electronic health records stimulus funds program. See *Note 1* for further information

The operating loss for 2012 increased by $1,245,365 or 66% compared to 2011. The primary components of the increased operating loss are:

- An increase in salaries and wages and employee benefits for the Hospital's employees of $812,578 or 8% due to an increase in self-funded health insurance claims and due to severance payments made to the Hospital's former CEO

- An increase in purchased services and professional fees of $219,566 or 6% as the result of the Hospital's previous decision to outsource the business office functions as well as its decision to contract with a third-party management company

- An increase in supplies and other expenses of $562,710 or 12% primarily as a result of the Supplemental Hospital Offset Payment Program (SHOPP) assessment for 2012. See *Note 1*

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist of investment income, interest expense and noncapital gifts received from the county. During 2013, the Hospital received $1,714,378 in noncapital gifts and an additional $487,340 in capital gifts from Texas County, Oklahoma.

The Hospital's Cash Flows

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

Capital Assets

At June 30, 2013, the Hospital had $6,278,320 invested in capital assets, net of accumulated depreciation, as detailed in *Note 5* to the financial statements. In 2013, the Hospital purchased new capital assets costing $388,658.

At June 30, 2012, the Hospital had $6,882,984 invested in capital assets, net of accumulated depreciation, as detailed in *Note 5* to the financial statements. In 2012, the Hospital purchased new capital assets costing $330,659.

Debt

At June 30, 2012, the Hospital had $465,935 in a capital lease obligation outstanding as detailed in *Note 8* to the financial statements. The capital lease was paid in full during 2013 with funds contributed by Texas County, Oklahoma. The Hospital issued no new debt in 2013 and 2012.

Contacting the Hospital's Financial Management

This financial report is designed to provide the Hospital's patients, suppliers, taxpayers and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to hospital administration by telephoning 580.338.6515.

Memorial Hospital of Texas County

Balance Sheets

June 30, 2013 and 2012

Assets

	2013	2012
Current Assets		
Cash	$ 284,458	$ 155,482
Short-term deposits	114,074	721,735
Patient accounts receivable, net of allowance; 2013 – $4,132,000, 2012 – $4,068,000	2,521,159	2,838,723
Estimated amounts due from third-party payer	-	60,000
Supplies	684,083	591,230
Prepaid expenses	141,720	182,395
Total current assets	3,745,494	4,549,565
Capital Assets	6,278,320	6,882,984
Investment in Joint Venture	501,834	501,834
Other Assets	148,974	175,623
Total assets	$ 10,674,622	$ 12,110,006

Liabilities and Net Position

	2013	2012
Current Liabilities		
Current maturities of long-term debt	$ -	$ 237,634
Estimated amounts due to third-party payer	40,000	-
Accounts payable	2,499,312	1,734,653
Accrued expenses	711,325	1,169,209
Total current liabilities	3,250,637	3,141,496
Long-Term Debt	-	228,301
Total liabilities	3,250,637	3,369,797
Net Position		
Net investment in capital assets	6,228,625	6,412,749
Unrestricted	1,195,360	2,327,460
Total net position	7,423,985	8,740,209
Total liabilities and net position	$ 10,674,622	$ 12,110,006

Memorial Hospital of Texas County

Statements of Revenues, Expenses and Changes in Net Position

Years Ended June 30, 2013 and 2012

	2013	2012
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2013 – $4,474,000, 2012 – $3,696,000	$ 14,678,125	$ 17,878,434
Other	912,994	480,932
Total operating revenues	15,591,119	18,359,366
Operating Expenses		
Salaries and wages	7,506,097	9,076,720
Employee benefits	1,567,711	2,376,795
Purchased services and professional fees	3,794,357	3,758,675
Supplies and other	5,210,683	5,158,741
Depreciation	993,322	1,103,112
Loss on sale of capital assets	-	144
Total operating expenses	19,072,170	21,474,187
Operating Loss	(3,481,051)	(3,114,821)
Nonoperating Revenues (Expenses)		
Noncapital gifts	1,714,378	-
Gain on investment in joint venture	-	71,741
Investment income	3,942	15,827
Interest expense	(40,833)	(52,260)
Total nonoperating revenues (expenses)	1,677,487	35,308
Deficiency of Revenues over Expenses Before Capital Grants and Gifts	(1,803,564)	(3,079,513)
Capital Grants and Gifts	487,340	33,008
Decrease in Net Position	(1,316,224)	(3,046,505)
Net Position, Beginning of Year	8,740,209	11,786,714
Net Position, End of Year	$ 7,423,985	$ 8,740,209

Memorial Hospital of Texas County

Statements of Cash Flows

Years Ended June 30, 2013 and 2012

	2013	2012
Operating Activities		
Receipts from and on behalf of patients	$ 15,095,689	$ 16,384,733
Payments to and on behalf of employees	(9,528,808)	(10,488,976)
Payments to suppliers and contractors	(8,340,838)	(8,113,638)
Other receipts (payments), net	939,643	702,836
Net cash used in operating activities	(1,834,314)	(1,515,045)
Capital and Related Financing Activities		
Principal paid on long-term debt	(465,935)	(270,797)
Interest paid on long-term debt	(40,833)	(52,260)
Purchase of capital assets	(343,263)	(381,293)
Contributions for retirement of capital debt	466,245	-
Contributions for purchase of capital assets	21,095	33,008
Net cash used in capital and related financing activities	(362,691)	(671,342)
Noncapital Financing Activities		
Noncapital gifts	1,714,378	-
Net cash provided by noncapital financing activities	1,714,378	-
Investing Activities		
Purchase of deposits	(2,573)	(14,938)
Proceeds from disposition of deposits	610,234	1,440,354
Dividends received from investment in joint venture	-	71,741
Interest on deposits	3,942	15,827
Net cash provided by investing activities	611,603	1,512,984
Increase (Decrease) in Cash	128,976	(673,403)
Cash, Beginning of Year	155,482	828,885
Cash, End of Year	$ 284,458	$ 155,482

	2013	2012
Reconciliation of Operating Loss to Net Cash Used in Operating Activities		
Operating loss	$ (3,481,051)	$ (3,114,821)
Depreciation	993,322	1,103,112
Accrued self-insurance costs	(455,000)	266,000
Provision for uncollectible accounts	4,474,000	3,696,000
Loss on sale of capital assets	-	144
Changes in operating assets and liabilities		
Patient accounts receivable, net	(4,156,436)	(3,986,612)
Other assets and liabilities	8,597	182,704
Estimated amount due from and to third-party payer	100,000	(165,000)
Accounts payable and accrued expenses	682,254	503,428
Net cash used in operating activities	$ (1,834,314)	$ (1,515,045)
Supplemental Cash Flows Information		
Capital asset acquisitions included in accounts payable	$ 49,695	$ 4,300
Prepaid assets included in accounts payable	$ 90,914	$ 56,788

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

Nature of Operations and Reporting Entity

Memorial Hospital of Texas County (the Hospital) is an acute care hospital located in Guymon, Oklahoma. The Hospital primarily earns revenue by providing inpatient, outpatient and emergency care services to patients in and around the Guymon, Oklahoma, area. The Hospital also operates a home health agency and physician clinics in the same geographic area.

Basis of Accounting and Presentation

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place. Operating revenues and expenses include exchange transactions. Investment income and interest on capital asset-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position 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 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 Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2013 and 2012, the Hospital had no cash equivalents.

Risk Management

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

The Hospital is self-insured for a portion of its exposure to risk of loss from employee health claims. Annual estimated provisions are accrued for the self-insured portion of these claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Investments and Investment Income

Investments in non-negotiable certificates of deposit are carried at amortized cost. Investment income includes interest income.

Patient Accounts Receivable

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

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 and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital:

Land improvements	15–20 years
Buildings, improvements and fixed equipment	20–40 years
Major moveable equipment	3–7 years

Investment in Joint Venture

The Hospital has an ownership (equity) interest in a joint venture – Heartland Healthcare Reciprocal Risk Retention Group (Heartland). The investment in Heartland is recorded using the equity method of accounting (cost plus equity of Heartland's undistributed net income or loss since acquisition).

The Hospital has an approximate 7% equity interest in Heartland. Heartland was formed as an unincorporated association approved by the State of Vermont to provide hospital professional liability and general liability coverage to its subscribers. Until June 30, 2012, the Hospital purchased its professional liability (medical malpractice) and general liability insurance coverages from Heartland.

Effective June 30, 2012, the Hospital terminated its participation in Heartland. Heartland's subscriber agreement provides that a withdrawing member's undistributed SSA balance will be paid to the member three years after the termination date and the member's PSA balance will be paid to the member, at the discretion of Heartland's Subscribers' Advisory Committee, over a three-year period in annual installments after the termination date.

Complete financial statements of Heartland may be obtained by contacting hospital administration at 580.338.6515.

Compensated Absences

Hospital policies permit most employees to accumulate paid days off 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 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 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 Hospital is classified in two 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. Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets.

Net Patient Service Revenue

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

Charity Care

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

Income Taxes

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

Supplemental Hospital Offset Payment Program

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

During the years ended June 30, 2013 and 2012, the Hospital received approximately $1,171,000 and $1,070,000 in SHOPP funds and paid SHOPP assessment fees of approximately $524,000 and $515,000, respectively. The annual amounts to be received and paid 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. Based on current information available, the annual net benefit to the Hospital over the term of the SHOPP program is not expected to be materially different than the net amounts received in 2013 and 2012. The SHOPP revenue is recorded as part of net patient service revenue and the SHOPP assessment fees are recorded as part of other expenses on the accompanying statements of revenues, expenses and changes in net position.

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 technology (EHR). Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to four years based on a statutory formula, as determined by the state, which is approved by CMS. Payments under both programs are contingent on the Hospital continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the Medicare administrative contractor. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

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

During 2013, the Hospital completed the first-year requirements under the Medicaid program and has recorded revenue of approximately $625,000, which is included in other revenue within operating revenues in the accompanying statements of revenues, expenses and changes in net position.

Subsequent to year-end, the Hospital completed the first-year requirements under the Medicare program and filed the certification application to receive the incentive payments. The Hospital will recognize approximately $690,000 of revenue in fiscal year 2014 related to meeting the first-year requirements under the Medicare program.

Change in Accounting Principle

In 2013, the Hospital adopted the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 61, *The Financial Reporting Entity: Omnibus, an amendment of GASB Statements No. 14 and No. 34*, which became effective for reporting periods beginning after June 15, 2012. Due to the change in accounting principle, the Hospital no longer meets the criteria to be considered as a blended component unit of the Texas County, Oklahoma. These changes have no impact on the financial statements of the Hospital.

Reclassifications

Certain reclassifications have been made to the 2012 financial statements to conform to the 2013 financial statement presentation. These reclassifications had no effect on the changes in net position.

Note 2: Net Patient Service Revenue

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

- **Medicare –** Substantially all inpatient acute care and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. Those rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient skilled nursing services are paid at prospectively determined per diem rates based on the patients' acuity and expected resource utilization. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare administrative contractor. The Medicare administrative contractor has audited the Hospital's cost reports through June 30, 2010.

- **Medicaid –** The Hospital is reimbursed for services rendered to patients covered by the state Medicaid program at prospectively determined rates per discharge and fee schedule with no retroactive adjustment. Those payment rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Approximately 46% and 40% of net patient service revenue are from participation in the Medicare and state-sponsored Medicaid programs for the years ended June 30, 2013 and 2012, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

Note 3: Deposits, Investments and Investment Income

Deposits

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

At June 30, 2013 and 2012, none of the Hospital's bank balances of $638,636 and $1,380,641, respectively, were exposed to custodial credit risk.

The Hospital's investment policy is to invest operating and excess funds in interest-bearing checking accounts and certificates of deposit with financial institutions. These investments are included as deposits.

Summary of Carrying Values

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

	2013	2012
Carrying values		
Deposits	$ 396,653	$ 875,310
Accrued interest income	75	579
Petty cash	1,804	1,328
	$ 398,532	$ 877,217
Included in the following balance sheet captions		
Cash	$ 284,458	$ 155,482
Short-term deposits	114,074	721,735
	$ 398,532	$ 877,217

Note 4: Patient Accounts Receivable

The Hospital 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 June 30 consisted of:

	2013	2012
Medicare	$ 890,895	$ 566,599
Medicaid	298,292	404,828
Other third-party payers	1,244,649	1,512,255
Patients	4,219,323	4,423,041
	6,653,159	6,906,723
Less allowance for uncollectible amounts	4,132,000	4,068,000
	$ 2,521,159	$ 2,838,723

Note 5: Capital Assets

Capital assets activity for the years ended June 30 was:

	2013				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	$ 335,035	$ -	$ -	$ -	$ 335,035
Land improvements	180,665	-	-	-	180,665
Buildings, improvements and fixed equipment	16,037,992	28,568	-	25,739	16,092,299
Major moveable equipment	10,927,988	49,695	(50,219)	315,578	11,243,042
Construction in progress	30,922	310,395		(341,317)	-
	27,512,602	388,658	(50,219)	-	27,851,041
Less accumulated depreciation					
Land improvements	171,908	1,289	-	-	173,197
Buildings, improvements and fixed equipment	10,841,943	557,277	-	-	11,399,220
Major moveable equipment	9,615,767	434,756	(50,219)	-	10,000,304
	20,629,618	993,322	(50,219)	-	21,572,721
Capital assets, net	$ 6,882,984	$ (604,664)	$ -	$ -	$ 6,278,320

	2012				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	$ 335,035	$ -	$ -	$ -	$ 335,035
Land improvements	180,665	-	-	-	180,665
Buildings, improvements and fixed equipment	15,939,903	67,123	-	30,966	16,037,992
Major moveable equipment	10,682,775	227,926	(5,628)	22,915	10,927,988
Construction in progress	49,193	35,610	-	(53,881)	30,922
	27,187,571	330,659	(5,628)	-	27,512,602
Less accumulated depreciation					
Land improvements	169,998	1,910	-	-	171,908
Buildings, improvements and fixed equipment	10,235,617	606,326	-	-	10,841,943
Major moveable equipment	9,126,375	494,876	(5,484)	-	9,615,767
	19,531,990	1,103,112	(5,484)	-	20,629,618
Capital assets, net	$ 7,655,581	$ (772,453)	$ (144)	$ -	$ 6,882,984

Note 6: Medical Malpractice Claims

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

Note 7: Employee Health Claims

Substantially all of the Hospital’s employees and their dependents are eligible to participate in the Hospital’s employee health insurance program. The Hospital is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of $75,000. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured claims, including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Hospital’s estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability during 2013 and 2012 is summarized as follows:

	2013	2012
Balance, beginning of year	$ 525,000	$ 259,000
Current year claims incurred and changes in estimates for claims incurred in prior years	653,409	1,600,497
Claims and expenses paid	(1,108,409)	(1,334,497)
Balance, end of year	$ 70,000	$ 525,000

Note 8: Long-Term Debt

The Hospital was obligated under a lease for medical equipment that was previously accounted for as a capital lease. Lease payments, including interest at 4.5%, were due monthly in the amount of $23,134 through April 2014. Principal payments totaled $270,797 during 2012. During 2013, the outstanding balance of $465,935 was paid in full with funds contributed to the Hospital by Texas County, Oklahoma.

Note 9: Designated Net Position

At June 30, 2013 and 2012, unrestricted net position has been designated by the Hospital's Board of Control for use in capital asset acquisition and payment of self-insured health claims in the amount of $1,863 and $181,603, respectively. Designated net position remains under the control of the Board of Control which may, at its discretion, later use this net position for other purposes.

Note 10: Charity Care

In support of its mission, the Hospital voluntarily provides free care to patients who lack financial resources and are deemed to be medically indigent. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported in net patient service revenue. In addition, the Hospital provides services to other medically indigent patients under the state Medicaid welfare program. The state Medicaid welfare program pays 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.

Uncompensated charges relating to these services are as follows:

	2013	2012
Charity allowances	$ 501,000	$ 292,000
State Medicaid welfare program	5,493,000	5,863,000
	$ 5,994,000	$ 6,155,000

In addition to uncompensated charges, the Hospital 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 screenings and assessments, prenatal education and care, community educational services and various support groups.

Note 11: Retirement Plan

The Hospital contributes to a defined contribution annuity plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's required contributions determined in accordance with the terms of the plan. The plan is administered by the Hospital's Board of Control. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Board of Control. Contribution rates for plan members and the Hospital expressed as a percentage of covered payroll were 4.1% and 1.6% for 2013 and 3.1% and 1.5% for 2012, respectively. Contributions actually made by plan members and the Hospital aggregated $224,000 and $87,000 during 2013 and $203,000 and $96,000 during 2012, respectively.

Note 12: Contract Management Services

Effective April 18, 2012, the Hospital is operated by NewLight Healthcare (NewLight) under a management contract. The contract is for an initial term of three years and automatically renews for additional successive three-year terms unless terminated in accordance with the contract by either party at least 90 days prior to the end of the current term. Services provided by NewLight under the management contract include items such as management advisory services, revenue cycle management and administrative salary costs. Fees paid to NewLight for management services were approximately $310,000 and $97,000 for the years ended June 30, 2013 and 2012, respectively. The Hospital terminated the management contract effective July 2013.

Note 13: Contingencies

Litigation

In the normal course of business, the Hospital 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 Hospital 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.

Note 14: Risks and Uncertainties

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 Hospital.

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

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

Note 15: 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 Hospital'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 Hospital's net patient service revenue. In addition, it is possible the Hospital will experience payment delays and other operational challenges during PPACA's implementation.

Note 16: Management's Consideration of Going Concern Matters

The Hospital has incurred significant losses for several years and currently has minimal working capital due to recurring negative cash flows. The accompanying financial statements have been prepared assuming the Hospital will continue as a going concern, realizing assets and liquidating liabilities in the ordinary course of business. Management is considering several alternatives for mitigating these conditions during the next year. These include evaluating contract nonrenewal of certain employed physicians where overhead costs significantly exceed revenue generated, evaluating the financial viability of current service lines and implementation of cost containment strategies. In addition, management is in the process of undergoing a review of its business office operations by an outside consulting firm to generate recommendations that will lead to improved charge capture, billing and collections processes that are expected to yield additional cash flow for the Hospital. Although not currently planned, realization of assets in other than the ordinary course of business in order to meet liquidity needs could incur losses not reflected in these financial statements.

Note 17: Subsequent Events

In August 2013, the Hospital received a $1,000,000 contribution from Texas County, Oklahoma, to be used for operating activities.

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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 the Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Control
Memorial Hospital of Texas County
Guymon, 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 Memorial Hospital of Texas County (the Hospital), which comprise the balance sheet as of June 30, 2013, 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 March 31, 2014, which contained an "Emphasis of Matter" paragraph regarding substantial doubt about the Hospital's ability to continue as a going concern for a reasonable period of time.

Internal Control over Financial Reporting

Management of the Hospital is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit, we considered the Hospital'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 Hospital's internal control. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control.

Our consideration of internal control 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 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 certain deficiencies in internal control that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention to those charged with governance. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Hospital's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2013-1 through 2013-3 to be material weaknesses.

Board of Control
Memorial Hospital of Texas County

Compliance

As part of obtaining reasonable assurance about whether the Hospital's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Hospital's Responses to the Findings

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

Other Matters

We also noted certain matters that we reported to the Hospital's management in a separate letter dated March 31, 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 entity's internal control or compliance. This communication is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Tulsa, Oklahoma
March 31, 2014

Memorial Hospital of Texas County

Schedule of Findings and Responses

Year Ended June 30, 2013

Reference Number	Finding
2013-1	Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal controls to promote accurate recording and classification of accounting transactions. Condition – Management’s procedures for recording and classifying accounting transactions and procedures for preparing general ledger reconciliations did not always prevent inaccurate recording of transactions. Context – Potential material misstatements in the financial statements or material misappropriation of assets due to error or fraud could occur and not be prevented or detected in a timely manner. Effect – Material journal entries were made to numerous general ledger accounts during the audit to correct misstatements not identified by management. Cause – Recording and monitoring procedures in the internal control over financial reporting process were not performed accurately. Recommendation – Management should ensure that controls are adequate to properly record accounting entries. Management should also ensure that monthly general ledger reconciliations are completed timely and accurately and all reconciling items are researched and resolved on a timely basis. Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will take steps to evaluate the current internal controls over the recording and classification of accounting transactions and prepare accurate monthly reconciliations, including resolving any variances.

Reference Number	Finding
2013-2	Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal controls to promote accurate recording and classification of accounting transactions.

Condition – Management has established various internal control policies and procedures for recording and classifying accounting transactions. These policies and procedures were not followed consistently throughout the year.

Context – Potential material misstatements in the financial statements or material misappropriation of assets due to error or fraud could occur and not be prevented or detected in a timely manner.

Effect – Various established internal control procedures were not completed routinely on a monthly basis during the year, including:

- Management review of pending checks prior to them being processed and released for payment
- Management review of monthly bank reconciliations
- CEO and CFO review of monthly financial statements
- CFO review of journal entries prepared by controller

Cause – Turnover in senior management resulted in established internal control policies and procedures not being performed routinely during the year.

Recommendation – Management should ensure all established internal controls are performed throughout the year.

Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will take steps to follow all established internal control policies and procedures.

Memorial Hospital of Texas County

Schedule of Findings and Responses

Year Ended June 30, 2013

Reference Number	Finding
2013-3	Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting. Condition – The controller has incompatible duties in the purchases, cash disbursements and accounts payable transactions cycle. Context – The controller has the ability to generate purchase orders and payments, record checks issued, add or make changes to vendor profiles in the computer system, record journal entries and prepare account reconciliations. Effect – Potentially material misstatements in the financial statements or material misappropriations of assets due to error or fraud could occur and not be prevented or detected in a timely manner. Cause – Duties in the purchases, cash disbursements and accounts payable transactions cycle are not adequately segregated and monitored. In addition, other compensating controls within the internal control environment designed to reduce the risk of error or fraud were not performed on a consistent basis throughout the year. Recommendation – Management should periodically evaluate the costs versus the benefits of further segregation of duties and implement those changes it deems appropriate for which benefits are determined to exceed costs. In addition, management should consistently follow established internal control procedures to help mitigate the risk of errors or fraud occurring as a result of segregation of duties weaknesses. Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will perform the suggested evaluation and make any changes deemed appropriate that are cost beneficial within the next year.