

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
Independent Auditor's Reports and Financial Statements  
September 30, 2015 and 2014





**Harper County Community Hospital**  
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**September 30, 2015 and 2014**

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## Independent Auditor's Report

Board of Control  
Harper County Community Hospital  
Buffalo, Oklahoma

### Report on the Financial Statements

We have audited the accompanying balance sheets of Harper County Community Hospital (the Hospital), a component unit of Harper County, Oklahoma, as of September 30, 2015 and 2014, 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 basic 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 Harper County Community Hospital as of September 30, 2015 and 2014, 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 Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated February 18, 2016, 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  
February 18, 2016

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Management's Discussion and Analysis**  
**Years Ended September 30, 2015 and 2014**

***Introduction***

This management's discussion and analysis of the financial performance of Harper County Community Hospital (the Hospital) provides an overview of the Hospital's financial activities for the years ended September 30, 2015 and 2014. It should be read in conjunction with the accompanying financial statements of the Hospital.

***Financial Highlights***

- Cash, cash equivalents and short-term certificates of deposit increased in 2015 by \$382,736 or 39% and in 2014 by \$11,986 or 1%.
- The Hospital's net position decreased in 2015 by \$208,568 or 9% and increased in 2014 by \$500,196 or 28%.
- The Hospital reported operating losses of \$832,078 in 2015 and \$30,569 in 2014.
- The Hospital's unrestricted appropriations from Harper County, Oklahoma, increased \$91,607 or 17% in 2015 compared to 2014 and decreased \$63,654 or 11% in 2014 compared to 2013.

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

***The Balance Sheet and Statement of Revenues, Expenses and Changes in Net 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 it. 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 \$208,568 or 9% in 2015 and increased by \$500,196 or 28% in 2014 as shown in Table 1.

**Table 1: Assets, Liabilities and Net Position**

	<b>2015</b>	<b>2014</b>	<b>2013</b>
<b>Assets</b>			
Cash, cash equivalents and short-term certificates of deposit	\$ 1,375,777	\$ 993,041	\$ 981,055
Patient accounts receivable, net	324,383	441,944	455,396
Other current assets	228,917	1,113,783	362,133
Capital assets, net	709,818	1,062,538	1,415,319
Other receivable – related party	95,000	-	-
	<u>\$ 2,733,895</u>	<u>\$ 3,611,306</u>	<u>\$ 3,213,903</u>
<b>Liabilities</b>			
Long-term debt (including current maturities)	\$ 155,331	\$ 234,242	\$ 325,849
Other current and noncurrent liabilities	530,531	1,120,463	1,131,649
	<u>685,862</u>	<u>1,354,705</u>	<u>1,457,498</u>
<b>Net Position</b>			
Net investment in capital assets	554,487	172,249	433,423
Unrestricted	1,493,546	2,084,352	1,322,982
	<u>2,048,033</u>	<u>2,256,601</u>	<u>1,756,405</u>
	<u>\$ 2,733,895</u>	<u>\$ 3,611,306</u>	<u>\$ 3,213,903</u>

A significant change in the Hospital's financial position in 2015 was a decrease in other current assets due to the receipt of approximately \$986,000 under the Electronic Health Records (EHR) Incentive Program during fiscal year 2015. Another significant change was a decrease in other current and noncurrent liabilities due to approximately \$690,000 of invoices paid during 2015 related to the implementation of the new EHR system.

A significant change in the Hospital's financial position in 2014 was an increase in other current assets due to approximately \$986,000 due from Medicare and Medicaid under the EHR Incentive Program at year-end.

## Operating Results and Changes in the Hospital's Net Position

In 2015, the Hospital's net position decreased by \$208,568 or 9% as shown in Table 2. This decrease is made up of several different components and represents a decrease of \$708,764 compared with the increase in net position for 2014 of \$500,196. The Hospital's change in net position increased from \$92,210 in 2013, an increase of \$592,406 or 642%.

**Table 2: Operating Results and Changes in Net Position**

	<b>2015</b>	<b>2014</b>	<b>2013</b>
<b>Operating Revenues</b>			
Net patient service revenue	\$ 3,397,268	\$ 3,733,715	\$ 3,148,154
Other operating revenues	80,993	421,419	88,955
Total operating revenues	<u>3,478,261</u>	<u>4,155,134</u>	<u>3,237,109</u>
<b>Operating Expenses</b>			
Salaries and wages and employee benefits	2,615,949	2,548,673	2,682,287
Purchased services and professional fees	474,537	422,554	418,597
Depreciation	352,720	369,802	87,813
Other operating expenses	867,133	844,674	739,005
Total operating expenses	<u>4,310,339</u>	<u>4,185,703</u>	<u>3,927,702</u>
<b>Operating Loss</b>	<u>(832,078)</u>	<u>(30,569)</u>	<u>(690,593)</u>
<b>Nonoperating Revenues (Expenses)</b>			
County appropriations – unrestricted	624,429	532,822	596,476
Investment income	1,951	2,001	3,802
Interest expense	(11,001)	(13,038)	(10,087)
Noncapital gifts	8,131	8,980	8,192
Total nonoperating revenues (expenses)	<u>623,510</u>	<u>530,765</u>	<u>598,383</u>
<b>Increase (Decrease) in Net Position</b>	<u>\$ (208,568)</u>	<u>\$ 500,196</u>	<u>\$ (92,210)</u>

## Operating Losses

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

The operating loss increased by \$801,509 for 2015 as compared to 2014. The primary components of the changes in operating losses for 2015 are:

- A decrease in net patient service revenue of \$336,497 or 9% primarily due to the Hospital not receiving Medicare EHR Incentive Program revenue during 2015

- A decrease in other operating revenue of \$340,426 or 81% primarily due to the Hospital not receiving Medicaid EHR Incentive Program revenue during 2015
- An increase in purchased services and professional fees of \$51,983 or 12% primarily due to an increase in contract physician coverage

The operating loss improved by \$660,024 for 2014 as compared to 2013. The primary components of the improved operating loss for 2014 are:

- An increase in net patient service revenue of \$589,561 or 19% primarily due to recording revenue related to the Medicare EHR incentive payment earned in 2014
- An increase in other operating revenue of \$332,464 or 374% primarily due to recording revenue related to the Medicaid EHR incentive payment earned in 2014
- An increase in other operating expenses of \$105,669 or 14% primarily due to additional support costs for the new EHR system
- An increase in depreciation of \$281,989 or 321% primarily due to the first year of depreciation on the EHR system put in service late in 2013

### ***Nonoperating Revenues and Expenses***

Nonoperating revenues and expenses consist primarily of unrestricted county appropriations, noncapital gifts, investment income and interest expense. County appropriations from sales taxes increased by \$91,607 or 17% in 2015 compared to 2014 and decreased by \$63,654 or 11% in 2014 compared to 2013.

### ***The Hospital's Cash Flows***

Changes in the Hospital's cash flows are consistent with changes in operating results and nonoperating revenues and expenses for 2015 and 2014 as discussed earlier including the decrease in amounts due from third-party payers related to EHR incentive payments.

### ***Capital Asset and Debt Administration***

#### **Capital Assets**

In 2015, the Hospital did not acquire any new capital assets. In 2014, the Hospital acquired new capital assets costing \$17,021.

#### **Debt**

The Hospital issued no new debt during 2015 and 2014.

### ***Contacting the Hospital's Financial Management***

This financial report is designed to provide the Hospital's patients, suppliers, taxpayers and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Hospital's administration office by telephoning 580.735.2555.

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Balance Sheets**  
**September 30, 2015 and 2014**

**Assets**

	<b>2015</b>	<b>2014</b>
<b>Current Assets</b>		
Cash and cash equivalents	\$ 1,214,711	\$ 818,822
Short-term certificates of deposit	161,066	174,219
Patient accounts receivable, net of allowance; 2015 – \$318,000, 2014 – \$592,000	324,383	441,944
Estimated amounts due from third-party payers	-	870,000
Supplies and prepaid expenses	182,750	140,417
Other receivables	46,167	103,366
Total current assets	1,929,077	2,548,768
<b>Capital Assets, Net</b>	709,818	1,062,538
<b>Other Receivable – Related Party</b>	95,000	-
Total assets	<b>\$ 2,733,895</b>	<b>\$ 3,611,306</b>

**Liabilities and Net Position**

<b>Current Liabilities</b>		
Current maturities of long-term debt	\$ 70,418	\$ 78,530
Accounts payable	144,507	780,358
Accrued expenses	351,024	340,105
Estimated amounts due to third-party payers	35,000	-
Total current liabilities	600,949	1,198,993
<b>Long-Term Debt</b>	84,913	155,712
Total liabilities	685,862	1,354,705
<b>Net Position</b>		
Net investment in capital assets	554,487	172,249
Unrestricted	1,493,546	2,084,352
Total net position	2,048,033	2,256,601
Total liabilities and net position	<b>\$ 2,733,895</b>	<b>\$ 3,611,306</b>

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**Years Ended September 30, 2015 and 2014**

	<b>2015</b>	<b>2014</b>
<b>Operating Revenues</b>		
Net patient service revenue, net of provision for uncollectible accounts; 2015 – \$128,211, 2014 – \$222,438	\$ 3,397,268	\$ 3,733,715
Other	80,993	421,419
	<b>3,478,261</b>	<b>4,155,134</b>
<b>Operating Expenses</b>		
Salaries and wages	2,183,678	2,135,473
Employee benefits	432,271	413,200
Purchased services and professional fees	474,537	422,554
Medical supplies and drugs	116,666	108,980
Supplies and other	750,467	735,694
Depreciation	352,720	369,802
	<b>4,310,339</b>	<b>4,185,703</b>
	<b>(832,078)</b>	<b>(30,569)</b>
<b>Nonoperating Revenues (Expenses)</b>		
County appropriations – unrestricted	624,429	532,822
Investment income	1,951	2,001
Interest expense	(11,001)	(13,038)
Noncapital gifts	8,131	8,980
	<b>623,510</b>	<b>530,765</b>
	<b>(208,568)</b>	<b>500,196</b>
<b>Excess (Deficiency) of Revenues over Expenses and Increase (Decrease) in Net Position</b>	<b>(208,568)</b>	<b>500,196</b>
<b>Net Position, Beginning of Year</b>	<b>2,256,601</b>	<b>1,756,405</b>
<b>Net Position, End of Year</b>	<b>\$ 2,048,033</b>	<b>\$ 2,256,601</b>

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Statements of Cash Flows**  
**Years Ended September 30, 2015 and 2014**

	<b>2015</b>	<b>2014</b>
<b>Operating Activities</b>		
Receipts from and on behalf of patients	\$ 4,419,829	\$ 2,997,167
Payments to suppliers and contractors	(1,363,807)	(1,231,023)
Payments to and on behalf of employees	(2,605,030)	(2,552,332)
Other receipts and payments, net	80,993	421,419
Net cash provided by (used in) operating activities	531,985	(364,769)
<b>Noncapital Financing Activities</b>		
Noncapital appropriations – Harper County	681,628	487,440
Noncapital gifts	8,131	8,980
Net cash provided by noncapital financing activities	689,759	496,420
<b>Capital and Related Financing Activities</b>		
Principal paid on long-term debt	(78,911)	(91,607)
Interest paid on long-term debt	(11,001)	(13,038)
Purchase of capital assets	(656,047)	(17,021)
Net cash used in capital and related financing activities	(745,959)	(121,666)
<b>Investing Activities</b>		
Interest on investments	1,951	2,001
Net sales of certificates of deposit	13,153	24,790
Advances to related party	(95,000)	-
Net cash provided by (used in) investing activities	(79,896)	26,791
<b>Increase in Cash and Cash Equivalents</b>	395,889	36,776
<b>Cash and Cash Equivalents, Beginning of Year</b>	818,822	782,046
<b>Cash and Cash Equivalents, End of Year</b>	\$ 1,214,711	\$ 818,822

	<u>2015</u>	<u>2014</u>
<b>Reconciliation of Operating Loss to Net Cash Provided by (Used in)</b>		
<b>Operating Activities</b>		
Operating loss	\$ (832,078)	\$ (30,569)
Depreciation	352,720	369,802
Provision for uncollectible accounts	128,211	222,438
Changes in operating assets and liabilities		
Patient accounts receivable, net	(10,650)	(208,986)
Estimated amounts due from or to third-party payers	905,000	(750,000)
Accounts payable and accrued expenses	31,115	(11,186)
Supplies and prepaid expenses	(42,333)	43,732
	<u>\$ 531,985</u>	<u>\$ (364,769)</u>
<b>Supplemental Cash Flows Information</b>		
Capital asset acquisitions included in accounts payable	\$ -	\$ 656,047

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Notes to Financial Statements**  
**September 30, 2015 and 2014**

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

***Nature of Operations and Reporting Entity***

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

***Basis of Accounting and Presentation***

The accompanying financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally, unrestricted county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program-specific (such as unrestricted county appropriations), investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net 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 September 30, 2015 and 2014, cash equivalents consisted of certificates of deposit.

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
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**September 30, 2015 and 2014**

***Risk Management***

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

***Investments and Investment Income***

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

***Patient Accounts Receivable***

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

***Supplies***

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

***Capital Assets***

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

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

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Notes to Financial Statements**  
**September 30, 2015 and 2014**

***Compensated Absences***

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

***Net 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.

***County Appropriations***

Effective May 1, 1990, the citizens of the County approved a 1% sales tax for the operations and capital improvements of county health care facilities. The previous tax expired April 30, 2013. On May 6, 2012, the voters of the County approved an extension of the sales tax beginning May 1, 2013 and expiring April 30, 2018. The County appropriates these amounts monthly to the Hospital. The Hospital received approximately 15% and 11% in 2015 and 2014, respectively, of its financial support from county appropriations related to the sales tax. Revenue from county appropriations is recognized in the year in which the sales taxes are earned.

**Harper County Community Hospital**  
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**Notes to Financial Statements**  
**September 30, 2015 and 2014**

***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.

***Electronic Health Records Incentive Programs***

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records (EHR) technology. Critical access hospitals (CAH) 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 administrative contractor. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Hospital recognized the incentive payment revenue received for qualified EHR technology expenditures during 2014, which was the period during which management was reasonably assured meaningful use was achieved and the earning process was complete. Management believes the incentive payments reflect a change in how "allowable costs" are determined in paying CAHs for providing services to Medicare beneficiaries. The Hospital recorded revenue of approximately \$716,000, which is included in net patient service revenue in the accompanying statements of revenues, expenses and changes in net position for the year ended September 30, 2014. The Hospital had not yet attested for the second year under Medicare as of September 30, 2015.

**Harper County Community Hospital**  
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**Notes to Financial Statements**  
**September 30, 2015 and 2014**

In 2014, the Hospital also met criteria for the second year of the Medicaid program and recorded revenue of approximately \$270,000, which is included in other revenue in the accompanying statements of revenues, expenses and changes in net position for the year ended September 30, 2014. The Hospital had not yet attested for the third year of the Medicaid program as of September 30, 2015.

***Supplemental Hospital Offset Payment Program***

On January 17, 2012, CMS approved the State of Oklahoma's Supplemental Hospital Offset Payment Program (SHOPP). The SHOPP is retroactive back to July 1, 2011, and is currently scheduled to sunset on December 31, 2017. The SHOPP is designed to assess Oklahoma hospitals a supplemental hospital offset fee which will be placed in pools after receiving federal matching funds. The total fees and matching funds will then be allocated to hospitals as directed by legislation.

CAHs are excluded from paying the supplemental hospital offset fee but are still eligible to receive SHOPP funds. During 2015 and 2014, the Hospital received approximately \$42,000 and \$32,000, respectively, in SHOPP funds. The SHOPP revenue is recorded as part of net patient service revenue in the accompanying statements of revenues, expenses and changes in net position.

The annual amounts to be received by the Hospital over the term of the SHOPP are subject to change annually based on various factors involved in determining the amount of federal matching funds. Based on the current information available, the annual net benefit to the Hospital over the term of the SHOPP is not expected to be materially different than the amounts received in 2015.

**Note 2: Net Patient Service Revenue**

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

- **Medicare** – The Hospital is reimbursed based on a cost reimbursement methodology for inpatient and outpatient services provided to Medicare program beneficiaries as a CAH. The Hospital is reimbursed at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare administrative contractor. The Hospital's Medicare cost reports have been audited by the Medicare administrative contractor through the year ended September 30, 2013.
- **Medicaid** – The Hospital has also been reimbursed for services rendered to patients covered by the state Medicaid program at prospectively determined rates per discharge and fee schedules with no retroactive adjustments. The payment rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

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Approximately 59% and 42% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended September 30, 2015 and 2014, 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**

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

At September 30, 2015 and 2014, none of the Hospital's bank balances of approximately \$1,430,000 and \$1,058,000, respectively, were exposed to custodial credit risk.

**Summary of Carrying Values**

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

	<b>2015</b>	<b>2014</b>
Cash and cash equivalents	\$ 1,214,711	\$ 818,822
Short-term certificates of deposit	161,066	174,219
	<b>\$ 1,375,777</b>	<b>\$ 993,041</b>

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**Note 4: Patient Accounts Receivable**

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

	<b>2015</b>	<b>2014</b>
Medicare	\$ 106,445	\$ 190,628
Medicaid	4,918	17,348
Other third-party payers	125,751	171,474
Patients	405,269	654,494
	642,383	1,033,944
Less allowance for uncollectible accounts	318,000	592,000
	\$ 324,383	\$ 441,944

**Note 5: Capital Assets**

Capital assets activity for the years ended September 30 was:

	<b>2015</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Land	\$ 8,875	\$ -	\$ -	\$ -	\$ 8,875
Land improvements	38,373	-	-	-	38,373
Buildings	557,383	-	(1,081)	-	556,302
Equipment	2,176,694	-	(28,622)	-	2,148,072
	2,781,325	-	(29,703)	-	2,751,622
Less accumulated depreciation					
Land improvements	31,854	1,422	-	-	33,276
Buildings	382,923	15,616	(1,081)	-	397,458
Equipment	1,304,010	335,682	(28,622)	-	1,611,070
	1,718,787	352,720	(29,703)	-	2,041,804
Capital assets, net	\$ 1,062,538	\$ (352,720)	\$ -	\$ -	\$ 709,818

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	2014				Ending Balance
	Beginning Balance	Additions	Disposals	Transfers	
Land	\$ 8,875	\$ -	\$ -	\$ -	\$ 8,875
Land improvements	38,373	-	-	-	38,373
Buildings	557,383	-	-	-	557,383
Equipment	2,159,673	17,021	-	-	2,176,694
	<u>2,764,304</u>	<u>17,021</u>	<u>-</u>	<u>-</u>	<u>2,781,325</u>
Less accumulated depreciation					
Land improvements	29,381	2,473	-	-	31,854
Buildings	365,414	17,509	-	-	382,923
Equipment	954,190	349,820	-	-	1,304,010
	<u>1,348,985</u>	<u>369,802</u>	<u>-</u>	<u>-</u>	<u>1,718,787</u>
Capital assets, net	<u>\$ 1,415,319</u>	<u>\$ (352,781)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,062,538</u>

**Note 6: Related-Party Receivable**

The Hospital loaned \$95,000 to the Harper County Community Hospital Authority (the Authority) in September 2015 for the purchase of a house in Buffalo, Oklahoma, for use in physician recruitment. The Authority is a component unit of the County and its board of trustees is appointed by the county commissioners. As of September 30, 2015, and through the date the financial statements were available to be issued, no signed agreement exists for this receivable between the Hospital and the Authority. It is the Hospital's intent that this receivable will be due at the earlier of five years or when the house is sold and bears no interest. As such, the receivable is classified as long term on the accompanying balance sheets as of September 30, 2015.

**Note 7: 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.

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**Note 8: Long-Term Debt**

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

	<b>2015</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Deductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Note payable to bank (A)	\$ 968	\$ -	\$ (968)	\$ -	\$ -
Note payable to bank (B)	37,308	-	(11,519)	25,789	11,730
Financing arrangement (C)	1,329	-	(1,329)	-	-
Note payable to bank (D)	29,281	-	(17,379)	11,902	11,902
Note payable to bank (E)	22,700	-	(7,864)	14,836	8,281
Note payable to bank (F)	14,283	-	(3,729)	10,554	3,926
Capital lease obligations	128,373	-	(36,123)	92,250	34,579
	<u>\$ 234,242</u>	<u>\$ -</u>	<u>\$ (78,911)</u>	<u>\$ 155,331</u>	<u>\$ 70,418</u>

  

	<b>2014</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Deductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Note payable to bank (A)	\$ 12,260	\$ -	\$ (11,292)	\$ 968	\$ 968
Note payable to bank (B)	48,199	-	(10,891)	37,308	11,160
Financing arrangement (C)	6,646	-	(5,317)	1,329	1,329
Note payable to bank (D)	46,105	-	(16,824)	29,281	17,306
Note payable to bank (E)	30,223	-	(7,523)	22,700	7,917
Note payable to bank (F)	17,839	-	(3,556)	14,283	3,745
Capital lease obligations	164,577	-	(36,204)	128,373	36,105
	<u>\$ 325,849</u>	<u>\$ -</u>	<u>\$ (91,607)</u>	<u>\$ 234,242</u>	<u>\$ 78,530</u>

**Notes Payable to Banks and Financing Arrangement**

- (A) Bank note payable dated November 11, 2010, in the original amount of \$42,442, has monthly payments of \$968, including interest at 4.5%, and was paid in full during 2015. The note was unsecured.
- (B) Bank note payable dated June 30, 2011, in the original amount of \$48,955, was refinanced on January 7, 2013, for an additional \$21,197 with monthly payments of \$1,073, including interest at 5.00%, and matures in 2018. The note is secured by certain equipment.
- (C) Financing arrangement with vendor dated November 18, 2011, payable quarterly beginning January 15, 2012, in the amount of \$2,060, which includes \$731 of warranty expense, principal and imputed interest at 3.25%, and was paid in full during 2015. The arrangement was secured by certain equipment.

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- (D) Bank note payable dated June 8, 2012, in the original amount of \$67,625, has monthly payments of \$1,506, including interest at 3.25%, and matures in 2016. The note is secured by certain equipment.
- (E) Bank note payable dated July 10, 2013, in the original amount of \$32,060, has monthly payments of \$731, including interest at 4.50%, and matures in 2017. The note is secured by certain equipment.
- (F) Bank note payable dated May 14, 2013, in the original amount of \$19,275, has monthly payments of \$362, including interest at 4.75%, and matures in 2018. The note is secured by certain equipment.

The debt service requirements as of September 30, 2015, are as follows:

Year Ending September 30,	Total to be Paid	Principal	Interest
2016	\$ 38,068	\$ 35,839	\$ 2,229
2017	23,889	23,003	886
2018	4,319	4,239	80
	<u>\$ 66,276</u>	<u>\$ 63,081</u>	<u>\$ 3,195</u>

**Capital Lease Obligations**

The Hospital is obligated under two leases for equipment items that are accounted for as capital leases. Assets under capital lease at September 30, 2015 and 2014, totaled \$188,590, net of accumulated depreciation of \$90,057 and \$53,573, respectively. The following is a schedule by year of future minimum lease payments under the capital leases, including interest at rates of 5.16% to 8.00% together with the present value of the future minimum lease payments as of September 30, 2015:

Year Ending September 30,	
2016	\$ 39,403
2017	37,968
2018	22,977
Total minimum lease payments	<u>100,348</u>
Less amount representing interest	<u>8,098</u>
Present value of future minimum lease payments	<u>\$ 92,250</u>

**Harper County Community Hospital**  
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**September 30, 2015 and 2014**

**Note 9: Operating Leases**

Rental expense under month-to-month and other operating lease agreements totaled approximately \$57,000 for the years ended September 30, 2015 and 2014.

**Note 10: Pension Plan**

The Hospital contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's contributions determined in accordance with the terms of the plan. The plan is administered by a third-party administrator. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Hospital's governing body. Contribution rates for plan members and the Hospital expressed as a percentage of covered payroll were 7% and 3% for 2015 and 6% and 3% for 2014, respectively. Contributions actually made by plan members and the Hospital aggregated approximately \$91,000 and \$39,000 during 2015 and \$87,000 and \$42,000 during 2014, respectively.

**Note 11: 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 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.

Uncompensated costs related to these services are as follows:

	<b>2015</b>	<b>2014</b>
Charity allowances	\$ -	\$ 31,000
Medicaid	38,000	53,000
	<b>\$ 38,000</b>	<b>\$ 84,000</b>

The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges based on the most recently filed Medicare cost report. In addition to uncompensated costs, 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.

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**Note 12: 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.

**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  
Harper County Community Hospital  
Buffalo, 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 basic financial statements of Harper County Community Hospital (the Hospital), a component unit of Harper County, Oklahoma, which comprise the balance sheet as of September 30, 2015, 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 basic financial statements, and have issued our report thereon dated February 18, 2016.

***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 of the financial statements, 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 or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not 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 significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. 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 deficiency described in the accompanying schedule of findings and responses as item 2015-1 to be a material weakness.

Board of Control  
Harper County Community Hospital

### ***Compliance and Other Matters***

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

### ***The Hospital's Response to the Finding***

The Hospital's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. The Hospital'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.

We also noted certain matters that we reported to the Hospital's management in a separate letter dated February 18, 2016.

### ***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Hospital's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

**BKD, LLP**

Tulsa, Oklahoma  
February 18, 2016

**Harper County Community Hospital**  
**A Component Unit of Harper County, Oklahoma**  
**Schedule of Findings and Responses**  
**Year Ended September 30, 2015**

<b>Reference Number</b>	<b>Finding</b>
2015-1	<p>Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting.</p> <p>Condition – One employee’s duties are not adequately segregated among access, recording and monitoring functions in the purchases, cash disbursements and accounts payable transactions cycle (outflows); revenue, cash receipts and accounts receivable transactions cycle (inflows); and the payroll transactions cycle.</p> <p>Context – The chief executive officer has access rights allowing this individual to perform nearly all user activities in the accounting system and also has access to assets and reconciling responsibilities in the outflows, inflows and payroll transactions cycles.</p> <p>Effect – Potentially 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.</p> <p>Cause – Duties in the outflows, inflows and payroll transactions cycles are not adequately segregated and monitoring or other compensating controls are insufficient.</p> <p>Recommendation – Management should periodically evaluate the costs versus the benefits of further segregation of duties or addition of monitoring or other compensating controls and implement those changes it deems appropriate for which benefits are determined to exceed costs.</p> <p>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.</p>