

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Independent Auditor's Reports and Financial Statements
June 30, 2016



McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
June 30, 2016

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Independent Auditor's Report

Board of Trustees
McAlester Regional Health Center Authority
McAlester, Oklahoma

Report on the Financial Statements

We have audited the accompanying balance sheet of McAlester Regional Health Center Authority (the Authority), a component unit of the city of McAlester, Oklahoma, as of June 30, 2016, 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.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 the Authority as of June 30, 2016, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Prior Year Audited by Other Auditors

The 2015 financial statements were audited by other auditors and their report thereon, dated October 7, 2015, expressed an unmodified opinion.

Other Matters

Required Supplementary Information

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Information

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

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 21, 2016, on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

BKD, LLP

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Balance Sheet
June 30, 2016

Assets

Current Assets

Cash and cash equivalents	\$ 29,218,856
Short-term investments	979,257
Restricted cash	120,194
Restricted certificates of deposit for workers' compensation	473,746
Patient accounts receivable, net of allowance – \$14,683,252	11,457,956
Supplies	2,461,261
Prepaid expenses and other	<u>2,296,618</u>

Total current assets 47,007,888

Noncurrent Cash and Investments

Held by trustee for capital acquisitions	8,600,033
Other long-term investments	3,876,212
Investment in and advances to equity investees	<u>4,843,506</u>

Total noncurrent cash and investments 17,319,751

Capital Assets, Net

26,168,062

Total assets \$ 90,495,701

Liabilities and Net Position

Current Liabilities

Current maturities of long-term debt	\$ 709,511
Accounts payable	2,638,227
Accrued expenses	4,193,996
Estimated amounts due to third-party payers	<u>343,247</u>

Total current liabilities 7,884,981

Long-Term Debt

9,806,408

Total liabilities 17,691,389

Net Position

Net investment in capital assets	14,325,630
Restricted – expendable for	
Capital acquisitions and debt service	8,970,227
Workers' compensation claims	473,746
Specific operating activities	25,000
Unrestricted	<u>49,009,709</u>

Total net position 72,804,312

Total liabilities and net position \$ 90,495,701

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Statement of Revenues, Expenses and Changes in Net Position
Year Ended June 30, 2016

Operating Revenues	
Net patient service revenue, net of provision for uncollectible accounts – \$10,090,264	\$ 83,646,754
Other operating revenue	<u>5,143,815</u>
Total operating revenues	<u>88,790,569</u>
Operating Expenses	
Salaries and wages	35,165,454
Employee benefits	6,615,407
Purchased services and professional fees	13,834,458
Supplies and other expenses	24,684,741
Depreciation and amortization	<u>3,461,143</u>
Total operating expenses	<u>83,761,203</u>
Operating Income	<u>5,029,366</u>
Nonoperating Revenues (Expenses)	
Gain on investment in equity investee	715,498
Investment income	183,390
Noncapital grants and gifts	317,575
Interest expense	<u>(106,690)</u>
Total nonoperating revenues (expenses)	<u>1,109,773</u>
Excess of Revenues over Expenses Before Capital Gifts	6,139,139
Gifts to Purchase Capital Assets and Other Capital Gifts	<u>250,000</u>
Increase in Net Position	6,389,139
Net Position, Beginning of Year	<u>66,415,173</u>
Net Position, End of Year	<u><u>\$ 72,804,312</u></u>

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Statement of Cash Flows
Year Ended June 30, 2016

Operating Activities	
Receipts from and on behalf of patients	\$ 83,270,969
Payments to suppliers and contractors	(42,142,868)
Payments to employees	(41,780,861)
Other receipts, net	<u>5,135,550</u>
Net cash provided by operating activities	<u>4,482,790</u>
Noncapital Financing Activities	
Noncapital grants and gifts	<u>317,575</u>
Net cash provided by noncapital financing activities	<u>317,575</u>
Capital and Related Financing Activities	
Capital grants and gifts	250,000
Principal payments made on long-term debt	(436,276)
Proceeds from issuance of long-term debt	9,099,045
Interest payments on capital debt and leases	(106,690)
Purchase of capital assets	<u>(3,784,757)</u>
Net cash provided by capital and related financing activities	<u>5,021,322</u>
Investing Activities	
Purchases of investments	(10,536,210)
Proceeds from disposition of investments	1,761,405
Investment income	165,759
Change in restricted asset, net	(2,839)
Advances to equity investee	(71,588)
Distributions from equity investees	<u>425,000</u>
Net cash used in investing activities	<u>(8,258,473)</u>
Increase in Cash and Cash Equivalents	1,563,214
Cash and Cash Equivalents, Beginning of Year	<u>27,775,836</u>
Cash and Cash Equivalents, End of Year	<u>\$ 29,339,050</u>
Reconciliation of Cash and Cash Equivalents to the Balance Sheet	
Cash and cash equivalents in current assets	\$ 29,218,856
Cash and cash equivalents in restricted cash	<u>120,194</u>
Total cash and cash equivalents	<u>\$ 29,339,050</u>

Reconciliation of Net Operating Revenues (Expenses) to Net Cash**Provided by Operating Activities**

Operating income	\$ 5,029,366
Depreciation and amortization	3,461,143
Accrued self-insurance costs	(230,145)
Provision for uncollectible accounts	10,090,264
Changes in operating assets and liabilities	
Patient accounts receivable	(11,152,423)
Estimated amounts due from and to third-party payers	686,374
Accounts payable and accrued expenses	(3,779,078)
Supplies and prepaid expenses	<u>377,289</u>
Net cash provided by operating activities	<u>\$ 4,482,790</u>

Supplemental Cash Flows Information

Capital lease obligations incurred for capital assets	\$ 293,025
Prepaid insurance included in accrued expenses	\$ 361,883
Capital asset acquisitions included in accounts payable	\$ 310,037

McAlester Regional Health Center Authority
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Notes to Financial Statements
June 30, 2016

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

Nature of Operations

The McAlester Regional Health Center Authority (the Authority) was created by a trust indenture dated August 11, 1969, as a public trust and an agency of the State of Oklahoma for the benefit of the City of McAlester, Oklahoma, and the surrounding area. The Authority operates, as its sole activity, McAlester Regional Health Center. Substantially all property and equipment used by the Authority is subject to a 50-year lease agreement with the City of McAlester commencing December 19, 1973. Effective May 1, 2016, the Authority amended the lease agreement for an additional 20 years until December 18, 2043.

The Authority primarily earns revenues by providing inpatient, outpatient and emergency services to patients in McAlester, Oklahoma, and surrounding communities. The Authority also operates physician clinics, a rehabilitation unit, a skilled nursing unit and provides home health services in the same geographic area.

Reporting Entity

The accompanying financial statements present the Authority and its blended component units, entities for which the Authority is considered to be financially accountable. Blended component units are, in substance, part of the primary government's operations, even though they are legally separate entities. Thus, blended component units are appropriately presented as funds of the primary government.

Blended Component Units

The McAlester Regional Health Center Foundation (the Foundation) is a legally separate, tax-exempt component unit of the Authority. The Foundation's primary purpose is to raise and hold funds to support the Authority and its programs. Although the Authority does not control the timing or amount of receipts from the Foundation, the majority of the Foundation's resources and related income are to be used for the benefit of the Authority. The Authority appoints the Board of Directors of the Foundation and, accordingly, is included as a component unit in the Authority's financial statements using the blended method. All significant intercompany accounts and transactions between the Authority and the Foundation have been eliminated in the accompanying financial statements.

The Auxiliary Volunteer Services of McAlester Regional Health Center (the Auxiliary) is a legally separate component unit of the Authority. The Auxiliary's primary function is to raise and hold funds to support the Authority and its programs. The board of the Auxiliary is self-perpetuating, but the director of the Auxiliary is appointed by the chief executive officer of the Authority. Because the Authority's Board of Trustees has final approval for the use of all assets of the Auxiliary, the Auxiliary is included as a component unit in the Authority's financial statements using the blended method. All significant intercompany accounts and transactions between the Authority and the Auxiliary have been eliminated in the accompanying financial statements.

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McAlester Medical Services, LLC (MMS) employs physicians and other health care providers. The Authority is the sole corporate member of MMS. MMS is included as a blended component unit of the Authority in the accompanying financial statements.

Separate financial statements for the blended component units can be obtained by contacting the Authority's administrative office.

Basis of Accounting and Presentation

The accompanying financial statements of the Authority have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally, federal and state grants) 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, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Authority first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets 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 Authority considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2016 and 2015, cash equivalents consisted primarily of money market accounts with brokers.

Risk Management

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

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The Authority is self-insured for a portion of its exposure to risk of loss from workers' compensation and employee health claims. Annual estimated provisions are accrued for the self-insured portion of workers' compensation and employee health 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 U.S. Treasury, agency and instrumentality obligations with a remaining maturity of one year or less at time of acquisition and in non-negotiable certificates of deposit are carried at amortized cost. The investment in equity investee is reported on the equity method of accounting. All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income, realized gains and losses on investments sold and the net change for the year in the fair value of investments carried at fair value.

Patient Accounts Receivable

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

Supplies

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

Capital Assets

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

Land improvements	15–20 years
Buildings and leasehold improvements	10–40 years
Equipment	3–20 years

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Compensated Absences

Authority policies permit most employees to accumulate paid time 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 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.

Restricted Cash

The Authority received appropriations related to excise taxes levied by two city ordinances to provide revenues for the purpose of financing and construction of a cancer treatment facility, total funds not to exceed \$1,750,000, and a wellness facility, total funds not to exceed \$6,000,000, in the City of McAlester, Oklahoma. The Authority reached the maximum funding levels from each excise tax during 2010. At June 30, 2016, approximately \$120,000 of the funds under the excise taxes remain unspent and are reflected on the accompanying balance sheet as restricted cash.

Restricted Certificates of Deposit

The Oklahoma Workers' Compensation Court requires the Authority to post collateral for self-insured claims in the form of a certificate of deposit in the event the Authority is unable to pay its claims. As of June 30, 2016, the pledged restricted certificates of deposit of approximately \$474,000 are reflected on the accompanying balance sheet as restricted certificates of deposit for workers' compensation.

Net Position

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

Net Patient Service Revenue

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

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Charity Care

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

Income Taxes

As an essential government function of the City, the Authority is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. The Authority's blended component units are generally exempt from income taxes under Section 501 of the Code and under a similar provision of Oklahoma statutes. However, the Authority is subject to federal income tax on any unrelated business taxable income.

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 and physicians that demonstrate meaningful use of certified electronic health records (EHR) technology. Payments under the Medicare program are generally made for up to four years based upon a statutory formula. 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). Payments under both programs are contingent on the Authority continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. Eligibility under the Medicaid program generally requires a minimum Medicaid payer mix threshold. The final amount for any payment year 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 Authority 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.

In 2016, the Authority completed the third-year requirements under the Medicare program and has recorded revenue of approximately \$1,170,000, which is included in other operating revenue within operating revenues in the accompanying statement of revenues, expenses and changes in net position.

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Supplemental Hospital Offset Payment Program

On January 17, 2012, CMS approved the State of Oklahoma’s Supplemental Hospital Offset Payment Program (SHOPP). The SHOPP is retroactive back to July 1, 2011, and is currently scheduled to sunset on December 31, 2020. The SHOPP is designed to assess Oklahoma hospitals a supplemental hospital offset fee which will be placed in pools after receiving federal matching funds. The total fees and matching funds will then be allocated to hospitals as directed by legislation.

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

During the year ended June 30, 2016, the Authority had the following activity related to the SHOPP:

SHOPP funds received	\$	5,250,000
SHOPP assessment fees paid		2,204,000
Net benefit under SHOPP	\$	3,046,000

Note 2: Net Patient Service Revenue

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

Medicare – Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient, outpatient, rehabilitation, skilled nursing and home health services are paid at prospectively determined rates that are based on the patients’ acuity. The Authority is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare administrative contractor.

Medicaid – Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under prospectively determined rates per discharge and fee schedules with no retroactive adjustment. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

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Approximately 43% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the year ended June 30, 2016. 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 Authority has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Authority under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Note 3: Deposits, Investments and Investment Income

Deposits

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

At June 30, 2016, approximately \$1,420,000 of the Authority's bank balances of \$32,122,000 were exposed to custodial credit risk as uninsured and uncollateralized.

Investments

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

At June 30, 2016, the Authority had the following investments and maturities:

Type	Fair Value	Maturities in Years			
		Less than 1	1-5	6-10	More than 10
Corporate bonds	\$ 1,347,955	\$ -	\$ 938,847	\$ 409,108	\$ -
U.S. Treasury obligations	1,138,203	183,420	659,788	294,995	-
U.S. agencies obligations	102,174	-	102,174	-	-
Money market mutual funds	8,930,283	8,930,283	-	-	-
	11,518,615	<u>\$ 9,113,703</u>	<u>\$ 1,700,809</u>	<u>\$ 704,103</u>	<u>\$ -</u>
Corporate stocks	741,101				
Accrued interest	10,051				
	<u>\$ 12,269,767</u>				

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Interest Rate Risk – The Authority’s investment policy does not specifically limit the maturity of investments as a means of limiting its exposure to fair value losses arising from rising interest rates. The money market mutual funds are presented as an investment with a maturity of less than one year because they are redeemable in full immediately.

Credit Risk – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The Authority’s investment policy does not specifically address management of credit risk. At June 30, 2016, the Authority’s investments not directly guaranteed by the U.S. government were rated as follows:

Investments	Moody’s	S & P
Corporate bonds	Baa3-Aaa	BBB-AA+
U.S. agencies obligations	Aaa	AA+
Money market mutual funds	Not rated to Aaa-mf	Not rated to AAAM

Custodial Credit Risk – For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty the Authority will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Authority’s investment policy does not address custodial credit risk.

Concentration of Credit Risk – The Authority limits exposure of the portfolio to any one issuer, other than the U.S. government or its agencies, to 25% of the market value of the fund in one industry and 10% in any one company. At June 30, 2016, the Authority’s investment in one money market mutual fund of \$8,600,033 constituted 70% of its total investments.

McAlester Regional Health Center Authority
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Notes to Financial Statements
June 30, 2016

Summary of Carrying Values

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

Carrying value	
Deposits	\$ 30,998,531
Investments	<u>12,269,767</u>
	<u>\$ 43,268,298</u>
Included in the following balance sheet captions	
Cash and cash equivalents	\$ 29,218,856
Short-term investments	979,257
Restricted cash	120,194
Restricted certificates of deposit for workers' compensation	473,746
Held by trustee for capital acquisitions	8,600,033
Other long-term investments	<u>3,876,212</u>
	<u>\$ 43,268,298</u>

Investment Income

Investment income for the year ended June 30, 2016, consisted of:

Interest and dividend income	\$ 124,689
Net increase in fair value of investments	<u>58,701</u>
	<u>\$ 183,390</u>

McAlester Regional Health Center Authority
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June 30, 2016

Note 4: Patient Accounts Receivable

The Authority 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 June 30, 2016, consisted of:

Medicare	\$ 3,512,818
Medicaid	2,444,150
Other third-party payers	6,558,549
Patients	<u>13,625,691</u>
	26,141,208
Less allowance for uncollectible accounts	<u>14,683,252</u>
	<u><u>\$ 11,457,956</u></u>

McAlester Regional Health Center Authority
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Notes to Financial Statements
June 30, 2016

Note 5: Investments in Joint Ventures

The investments in joint ventures relate to a 33% ownership in Heartland Healthcare Reciprocal Risk Retention Group (Heartland); a 50% ownership in McAlester Ambulatory Surgery Center, LLC (the Surgery Center); a 50% ownership in McAlester Regional Dialysis Center, LLC (the Dialysis Center); and a 20% ownership in MSO Healthcare of Oklahoma, LLC (MSO). These investments in joint ventures are accounted for using the equity method. The financial position and results of operations from Heartland's fiscal year ended December 31, 2015, audited financial statements and the financial statements of the joint venture entities, the Surgery Center, the Dialysis Center and MSO, for the fiscal year ended June 30, 2016 (unaudited) are summarized below:

	December 31, 2015, Heartland	June 30, 2016		
		McAlester Ambulatory Surgery Center, LLC	McAlester Regional Dialysis Center, LLC	MSO Healthcare of Oklahoma, LLC
Current assets	\$ 13,832,346	\$ 3,769,444	\$ 904,767	\$ 47,641
Property and other long-term assets, net	-	379,975	739,766	408,708
Total assets	\$ 13,832,346	\$ 4,149,419	\$ 1,644,533	\$ 456,349
Total liabilities	\$ 5,967,744	\$ 272,857	\$ 371,620	\$ 61,922
Partners' equity	7,864,602	3,876,562	1,272,913	394,427
Total liabilities and partners' equity	\$ 13,832,346	\$ 4,149,419	\$ 1,644,533	\$ 456,349
Revenues	\$ 3,154,517	\$ 2,922,171	\$ 4,196,600	\$ 226,356
Excess (deficiency) of revenues over expenses	\$ 32,091	\$ 480,363	\$ 199,717	\$ (4,837)

Complete financial statements of the joint venture entities may be obtained by contacting the Authority's management.

The Authority purchases its professional liability (medical malpractice) and general liability insurance coverage from Heartland (see *Note 7*). For the year ended June 30, 2016, the Authority paid approximately \$815,000 to Heartland for the coverage. The Authority's investment in Heartland was approximately \$1,745,000 as of June 30, 2016.

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The Surgery Center is a joint venture with Warren Clinic, organized to operate an ambulatory surgery center in McAlester, Oklahoma. The Authority leases employees to the Surgery Center and provides insurance coverage and supplies on a limited basis. The Surgery Center paid the Authority approximately \$1,061,000 during the year ended June 30, 2016. At June 30, 2016, the Surgery Center owed the Authority approximately \$331,000. The Authority's investment in the Surgery Center was approximately \$1,950,000 as of June 30, 2016.

The Dialysis Center is a joint venture with a physician, organized to operate a dialysis facility in McAlester, Oklahoma. The Authority leases employees to the Dialysis Center and provides insurance coverage and supplies on a limited basis. The Dialysis Center paid the Authority approximately \$1,780,000 during the year ended June 30, 2016. At June 30, 2016, the Dialysis Center owed the Authority approximately \$344,000. The Authority's investment in the Dialysis Center was approximately \$1,076,000 as of June 30, 2016.

The Authority is an approximate 20% ownership member of MSO. The Authority's investment in MSO amounted to approximately \$72,000 at June 30, 2016. MSO was formed in January 2014 for the purpose of providing high-quality, cost-effective management services to the health care providers of Oklahoma.

Note 6: Capital Assets

Capital assets activity for the year ended June 30, 2016, was:

	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 1,059,793	\$ -	\$ -	\$ -	\$ 1,059,793
Land improvements	1,458,936	-	-	136,468	1,595,404
Buildings and fixed equipment	42,405,551	372,247	-	4,093,251	46,871,049
Major moveable equipment	32,012,077	2,559,995	(5,885)	(2,974,206)	31,591,981
Construction in progress	1,333,020	1,455,577	-	(1,255,513)	1,533,084
	<u>78,269,377</u>	<u>4,387,819</u>	<u>(5,885)</u>	<u>-</u>	<u>82,651,311</u>
Less accumulated depreciation					
Land improvements	1,116,212	44,037	-	102,904	1,263,153
Buildings and fixed equipment	27,892,939	1,533,564	-	2,190,821	31,617,324
Major moveable equipment	24,108,639	1,793,743	(5,885)	(2,293,725)	23,602,772
	<u>53,117,790</u>	<u>3,371,344</u>	<u>(5,885)</u>	<u>-</u>	<u>56,483,249</u>
Capital assets, net	<u>\$ 25,151,587</u>	<u>\$ 1,016,475</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 26,168,062</u>

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Note 7: Medical Malpractice Claims

The Authority purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Authority's claims experience, an accrual of approximately \$219,000 has been made as of June 30, 2016. It is reasonably possible that this estimate could change materially in the near term.

The Authority is a subscriber (member) of Heartland, an entity approved by the State of Vermont to provide hospital professional and general liability coverage to its subscribers. Heartland was formed in order to stabilize the cost and availability of hospital professional and general liability insurance by taking advantage of the self-funding capabilities of a homogenous group of health care providers. Heartland members are provided hospital professional and general liability insurance under claims-made policies on a fixed premium basis. See *Note 5* for additional information about Heartland.

Note 8: Self-Insured Claims

Substantially all of the Authority's employees and their dependents are eligible to participate in the Authority's employee health insurance plan. The Authority is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$125,000 and any amounts over \$1,000,000. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount of \$125,000 up to \$1,000,000.

The Authority is self-insured for risks related to workers' compensation claims up to \$600,000 per occurrence with an annual liability limit of \$1,000,000 in the aggregate.

A provision is accrued for self-insured employee health claims and workers' compensation claims, including both claims reported and claims incurred but not yet reported. The accruals are 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 Authority's estimates will change by a material amount in the near term.

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Activity in the Authority's accrued employee health claims and workers' compensation liabilities during 2016 is summarized as follows:

	<u>Employee Health</u>	<u>Workers' Compensation</u>
Balance, beginning of year	\$ 669,418	\$ 470,001
Current year claims incurred and changes in estimates for claims incurred in prior years	3,193,835	(88,757)
Claims and expenses paid	<u>(3,423,980)</u>	<u>(232,064)</u>
Balance, end of year	<u>\$ 439,273</u>	<u>\$ 149,180</u>

Note 9: Long-Term Obligations

The following is a summary of long-term obligation transactions for the Authority for the year ended June 30, 2016:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>
Notes payable to banks	\$ 1,467,319	\$ 9,099,045	\$ (271,455)	\$ 10,294,909	\$ 611,926
Capital lease obligations	<u>92,806</u>	<u>293,025</u>	<u>(164,821)</u>	<u>221,010</u>	<u>97,585</u>
Total long-term debt	<u>\$ 1,560,125</u>	<u>\$ 9,392,070</u>	<u>\$ (436,276)</u>	<u>\$ 10,515,919</u>	<u>\$ 709,511</u>

Notes Payable to Banks

The notes payable to banks are due between December 2017 and June 2036, payable monthly, including interest at rates of 2.55% to 5.15%. The notes are secured by real estate and certain capital assets. The debt service requirements as of June 30, 2016, are as follows:

<u>Year Ending June 30,</u>	<u>Total to be Paid</u>	<u>Principal</u>	<u>Interest</u>
2017	\$ 898,007	\$ 611,926	\$ 286,081
2018	883,609	625,992	257,617
2019	759,402	519,310	240,092
2020	941,949	722,537	219,412
2021	705,240	505,520	199,720
2022–2026	3,240,953	2,459,457	781,496
2027–2031	2,749,605	2,270,467	479,138
2032–2036	<u>2,750,437</u>	<u>2,579,700</u>	<u>170,737</u>
	<u>\$ 12,929,202</u>	<u>\$ 10,294,909</u>	<u>\$ 2,634,293</u>

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Included in notes payable is the Series 2016 Hospital Revenue Note (the 2016 Note) in the original amount of \$8,600,000 dated May 1, 2016, which bears interest monthly at 2.55%. The 2016 Note is secured by the gross revenues of the Authority and requires certain funds be established with the trustee. Accordingly, these funds are included as assets held by trustee for capital acquisitions in the accompanying balance sheet. The 2016 Note also requires the Authority to comply with certain restrictive covenants, including maintaining a debt service coverage ratio of 1.20 to 1.00 and days cash on hand of 75 days.

Capital Lease Obligations

The Authority is obligated under various leases for equipment that are accounted for as capital leases. Assets under capital leases at June 30, 2016, totaled \$293,025, net of accumulated depreciation of \$59,004. The following is a schedule by year of future minimum lease payments under capital lease, including interest at a rate of 1.96% with the present value of the future minimum lease payments as of June 30, 2016:

Year Ending June 30,	
2017	\$ 100,487
2018	100,488
2019	25,119
Total minimum lease payments	226,094
Less amount representing interest	5,084
Present value of future minimum lease payments	\$ 221,010

Note 10: Charity Care

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

Charity allowances	\$ 619,000
State Medicaid and other public aid programs	6,797,000
	\$ 7,416,000

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The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges. In addition to uncompensated charges, the Authority also commits significant time and resources to endeavors and critical services, which meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screenings and assessments, prenatal education and care, community educational services and various support groups.

Note 11: Pension Plan

The Authority contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Authority's required contributions, determined in accordance with the terms of the plan. The plan is administered by the Authority's Board of Trustees. 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 Authority's governing body. Contribution rates for plan members and the Authority expressed as a percentage of covered payroll was approximately 3% and 2%, respectively, for 2016. Contributions actually made by plan members and the Authority aggregated approximately \$1,022,000 and \$555,000, respectively, during 2016.

Note 12: Risk and Uncertainties

Litigation

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

Investments

The Authority invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the accompanying balance sheet.

McAlester Regional Health Center Authority
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June 30, 2016

Note 13: Disclosures About Fair Value of Assets

Fair value is the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets
- Level 3** Unobservable inputs supported by little or no market activity and significant to the fair value of the assets

Recurring Measurements

The following table presents the fair value measurements of assets recognized in the accompanying financial statements measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2016:

Type	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by Fair Value Level				
Money market mutual funds	\$ 8,930,283	\$ 8,930,283	\$ -	\$ -
Corporate bonds	1,347,955	1,347,955	-	-
U.S. Treasury obligations	1,138,203	1,138,203	-	-
U.S. agencies obligations	102,174	102,174	-	-
Corporate stocks	741,101	741,101	-	-
Total investments by fair value level	<u>\$ 12,259,716</u>	<u>\$ 12,259,716</u>	<u>\$ -</u>	<u>\$ -</u>

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Investments

Where quoted market prices are available in an active market, investments are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of investments with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such investments are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, investments are classified within Level 3 of the hierarchy. The Authority had no Level 2 or Level 3 investments at June 30, 2016.

Note 14: Combining Component Unit Information

Component Units' Financial Statements

The following tables include combining balance sheet information for the Authority and its blended component units, the Foundation and the Auxiliary, as of June 30, 2016:

	McAlester Regional Health Center Authority	McAlester Regional Health Center Foundation	Auxiliary Volunteer Services of McAlester Regional Health Center	Total	Eliminations	Combined Balance
Assets						
Current Assets						
Cash and cash equivalents	\$ 28,765,000	\$ 336,410	\$ 117,446	\$ 29,218,856	\$ -	\$ 29,218,856
Short-term investments	637,615	341,642	-	979,257	-	979,257
Restricted cash	120,194	-	-	120,194	-	120,194
Restricted certificates of deposit for workers' compensation	473,746	-	-	473,746	-	473,746
Patient accounts receivable, net of allowance	11,457,956	-	-	11,457,956	-	11,457,956
Supplies	2,431,556	-	29,705	2,461,261	-	2,461,261
Prepaid expenses and other	2,285,851	8,050	2,717	2,296,618	-	2,296,618
Total current assets	<u>46,171,918</u>	<u>686,102</u>	<u>149,868</u>	<u>47,007,888</u>	<u>-</u>	<u>47,007,888</u>
Noncurrent Cash and Investments						
Held by trustee for capital acquisitions	8,600,033	-	-	8,600,033	-	8,600,033
Other long-term investments	3,876,212	-	-	3,876,212	-	3,876,212
Investment in and advances to equity investees	4,843,506	-	-	4,843,506	-	4,843,506
Total noncurrent cash and investments	<u>17,319,751</u>	<u>-</u>	<u>-</u>	<u>17,319,751</u>	<u>-</u>	<u>17,319,751</u>
Capital Assets, Net	<u>26,168,062</u>	<u>-</u>	<u>-</u>	<u>26,168,062</u>	<u>-</u>	<u>26,168,062</u>
Total assets	<u>\$ 89,659,731</u>	<u>\$ 686,102</u>	<u>\$ 149,868</u>	<u>\$ 90,495,701</u>	<u>\$ -</u>	<u>\$ 90,495,701</u>

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
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June 30, 2016

	McAlester Regional Health Center Authority	McAlester Regional Health Center Foundation	Auxiliary Volunteer Services of McAlester Regional Health Center	Total	Eliminations	Combined Balance
Liabilities and Net Position						
Current Liabilities						
Current maturities of long-term debt	\$ 709,511	\$ -	\$ -	\$ 709,511	\$ -	\$ 709,511
Accounts payable	2,603,921	27,160	7,146	2,638,227	-	2,638,227
Accrued expenses	4,193,996	-	-	4,193,996	-	4,193,996
Estimated amounts due to third-party payers	343,247	-	-	343,247	-	343,247
Total current liabilities	7,850,675	27,160	7,146	7,884,981	-	7,884,981
Long-Term Debt	9,806,408	-	-	9,806,408	-	9,806,408
Total liabilities	17,657,083	27,160	7,146	17,691,389	-	17,691,389
Net Position						
Net investment in capital assets	14,325,630	-	-	14,325,630	-	14,325,630
Restricted – expendable for						
Capital acquisitions and debt service	8,720,227	250,000	-	8,970,227	-	8,970,227
Workers' compensation claims	473,746	-	-	473,746	-	473,746
Specific operating activities	-	25,000	-	25,000	-	25,000
Unrestricted	48,483,045	383,942	142,722	49,009,709	-	49,009,709
Total net position	72,002,648	658,942	142,722	72,804,312	-	72,804,312
Total liabilities and net position	<u>\$ 89,659,731</u>	<u>\$ 686,102</u>	<u>\$ 149,868</u>	<u>\$ 90,495,701</u>	<u>\$ -</u>	<u>\$ 90,495,701</u>

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Notes to Financial Statements
June 30, 2016

The following table includes combining statement of revenues, expenses and changes in net position information for the Authority and its blended component units, the Foundation and the Auxiliary, for the year ended June 30, 2016:

	McAlester Regional Health Center Authority	McAlester Regional Health Center Foundation	Auxiliary Volunteer Services of McAlester Regional Health Center	Total	Eliminations	Combined Balance
Operating Revenues						
Net patient service revenue, net of provision for uncollectible accounts	\$ 83,646,754	\$ -	\$ -	\$ 83,646,754	\$ -	\$ 83,646,754
Other	4,995,082	-	148,733	5,143,815	-	5,143,815
Total operating revenues	<u>88,641,836</u>	<u>-</u>	<u>148,733</u>	<u>88,790,569</u>	<u>-</u>	<u>88,790,569</u>
Operating Expenses						
Salaries and wages	35,165,454	-	-	35,165,454	-	35,165,454
Employee benefits	6,615,407	-	-	6,615,407	-	6,615,407
Purchased services and professional fees	13,834,458	-	-	13,834,458	-	13,834,458
Supplies and other expenses	24,246,220	285,950	152,571	24,684,741	-	24,684,741
Depreciation and amortization	3,461,143	-	-	3,461,143	-	3,461,143
Total operating expenses	<u>83,322,682</u>	<u>285,950</u>	<u>152,571</u>	<u>83,761,203</u>	<u>-</u>	<u>83,761,203</u>
Operating Income (Loss)	<u>5,319,154</u>	<u>(285,950)</u>	<u>(3,838)</u>	<u>5,029,366</u>	<u>-</u>	<u>5,029,366</u>
Nonoperating Revenues (Expenses)						
Gain on investment in equity investee	715,498	-	-	715,498	-	715,498
Investment income	180,757	2,633	-	183,390	-	183,390
Noncapital grants and gifts	-	317,575	-	317,575	-	317,575
Interest expense	(106,690)	-	-	(106,690)	-	(106,690)
Total nonoperating revenues (expenses)	<u>789,565</u>	<u>320,208</u>	<u>-</u>	<u>1,109,773</u>	<u>-</u>	<u>1,109,773</u>
Excess (Deficiency) of Revenues over Expenses Before Capital Gifts	<u>6,108,719</u>	<u>34,258</u>	<u>(3,838)</u>	<u>6,139,139</u>	<u>-</u>	<u>6,139,139</u>
Gifts to Purchase Capital Assets and Other Capital Gifts	<u>-</u>	<u>250,000</u>	<u>-</u>	<u>250,000</u>	<u>-</u>	<u>250,000</u>
Change in Net Position	<u>6,108,719</u>	<u>284,258</u>	<u>(3,838)</u>	<u>6,389,139</u>	<u>-</u>	<u>6,389,139</u>
Net Position, Beginning of Year	<u>65,893,929</u>	<u>374,684</u>	<u>146,560</u>	<u>66,415,173</u>	<u>-</u>	<u>66,415,173</u>
Net Position, End of Year	<u>\$ 72,002,648</u>	<u>\$ 658,942</u>	<u>\$ 142,722</u>	<u>\$ 72,804,312</u>	<u>\$ -</u>	<u>\$ 72,804,312</u>

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Notes to Financial Statements
June 30, 2016

The following table includes condensed combining statement of cash flows information for the Authority and its blended component units, the Foundation and the Auxiliary, for the year ended June 30, 2016.

	McAlester Regional Health Center Authority	McAlester Regional Health Center Foundation	Auxiliary Volunteer Services of McAlester Regional Health Center	Total	Eliminations	Combined Balance
Net Cash Provided by (Used in) Operating Activities	\$ 4,742,986	\$ (266,840)	\$ 6,644	\$ 4,482,790	\$ -	\$ 4,482,790
Net Cash Provided by Noncapital Financing Activities	-	317,575	-	317,575	-	317,575
Net Cash Provided by Capital and Related Financing Activities	4,771,322	250,000	-	5,021,322	-	5,021,322
Net Cash Used in Investing Activities	<u>(8,186,243)</u>	<u>(72,230)</u>	<u>-</u>	<u>(8,258,473)</u>	<u>-</u>	<u>(8,258,473)</u>
Increase in Cash and Cash Equivalents	1,328,065	228,505	6,644	1,563,214	-	1,563,214
Cash and Cash Equivalents, Beginning of Year	<u>27,557,129</u>	<u>107,905</u>	<u>110,802</u>	<u>27,775,836</u>	<u>-</u>	<u>27,775,836</u>
Cash and Cash Equivalents, End of Year	<u>\$ 28,885,194</u>	<u>\$ 336,410</u>	<u>\$ 117,446</u>	<u>\$ 29,339,050</u>	<u>\$ -</u>	<u>\$ 29,339,050</u>

Supplementary Information – Financial Ratios

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Days Cash on Hand
Year Ended June 30, 2016

Unrestricted cash	\$ 34,548,071
Operating expenses	\$ 83,761,203
Less depreciation and amortization	<u>(3,461,143)</u>
Adjusted expenses	80,300,060
	<u>365</u>
Average daily operating expense	<u>\$ 220,000</u>
Days cash on hand	<u>157.04</u>

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Debt Service Coverage Ratio
Year Ended June 30, 2016

Operating income	\$ 5,029,366
Plus depreciation and amortization	<u>3,461,143</u>
Net income available for debt service	<u>\$ 8,490,509</u>
Principal payments on long-term debt	\$ 436,276
Interest payments on long-term debt	<u>106,690</u>
	<u>\$ 542,966</u>
Debt service coverage ratio	15.64

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
EBIDA Calculation
Year Ended June 30, 2016

Operating income	\$ 5,029,366
Plus depreciation and amortization	<u>3,461,143</u>
EBIDA	<u><u>\$ 8,490,509</u></u>

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

Board of Trustees
McAlester Regional Health Center Authority
McAlester, 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 McAlester Regional Health Center Authority (the Authority), which comprise the balance sheet as of June 30, 2016, 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 October 21, 2016, which contained an *Other Matters* paragraph regarding omission of required supplementary information.

Internal Control over Financial Reporting

Management of the Authority is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered the Authority's internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Authority's financial statements will not be prevented or detected and corrected on a timely basis. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Board of Trustees
McAlester Regional Health Center Authority

Compliance and Other Matters

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

We noted certain matters that we reported to the Authority's management in a separate letter dated October 21, 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 entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Tulsa, Oklahoma
October 21, 2016

McAlester Regional Health Center Authority
A Component Unit of the City of McAlester, Oklahoma
Schedule of Findings and Responses
Year Ended June 30, 2016

Reference Number	Finding
	No matters are reportable.