

Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
A Component Unit of the Town of Okeene, Oklahoma
Accountants' Reports and Financial Statements
June 30, 2011 and 2010



Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
A Component Unit of the Town of Okeene, Oklahoma
June 30, 2011 and 2010

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Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Trustees
Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
Okeene, Oklahoma

We have audited the accompanying balance sheets of Okeene Municipal Hospital and Schallmo Authority d/b/a Okeene Municipal Hospital (the Hospital), a component unit of the Town of Okeene, Oklahoma, as of June 30, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As more fully described in *Note 8* to the financial statements, the Hospital has classified its Series 2006 Revenue Bonds, which are subject to acceleration, as long-term debt in the accompanying 2010 balance sheet, which practice, in our opinion, is not in accordance with accounting principles generally accepted in the United States of America. The effects on the 2010 balance of the aforementioned item are disclosed in *Note 8*.

In our opinion, except for the effects on the 2010 balance sheet of the matter described in the previous paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of Okeene Municipal Hospital and Schallmo Authority d/b/a Okeene Municipal Hospital as of June 30, 2011 and 2010, and its changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 17, 2011, 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* and should be considered in assessing the results of our audit.

Board of Trustees
Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
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The accompanying management's discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

BKD, LLP

November 17, 2011

**Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
A Component Unit of the Town of Okeene, Oklahoma
Management's Discussion and Analysis
Years Ended June 30, 2011 and 2010**

Introduction

This management's discussion and analysis of the financial performance of Okeene Municipal Hospital and Schallmo Authority d/b/a Okeene Municipal Hospital (the Hospital), a component unit of the Town of Okeene, Oklahoma, provides an overview of the Hospital's financial activities for the years ended June 30, 2011 and 2010. It should be read in conjunction with the accompanying financial statements of the Hospital.

Financial Highlights

- Cash and cash equivalents increased in 2011 by \$1,669,567 or 245.0% and decreased in 2010 by \$341,166 or 33.4%.
- The Hospital's net assets decreased by \$168,353 or 7.1% in 2011 and \$544,021 or 18.8% in 2010.
- The Hospital reported an operating income in 2011 of \$213,983 and an operating loss in 2010 of \$153,757. The operating income in 2011 is an increase compared to 2010 of \$367,740. The operating loss in 2010 is a decrease compared to 2009 of \$380,112.

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 assets; 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 Assets

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 assets 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 assets and changes in them. The Hospital's total net assets—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 assets 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 Assets

The Hospital's net assets are the difference between its assets and liabilities reported in the balance sheet. The Hospital's net assets decreased by \$168,353 (7.1%) in 2011 over 2010 and decreased by \$544,021 (18.8%) in 2010 over 2009 as shown in Table 1.

Table 1: Assets, Liabilities and Net Assets

	2011	2010	2009
Assets			
Cash and cash equivalents	\$ 2,351,037	\$ 681,470	\$ 1,022,636
Patient accounts receivable, net	932,212	783,868	931,044
Other current assets	515,279	774,261	579,468
Capital assets, net	6,541,694	6,933,045	7,369,251
Other noncurrent assets	1,025,819	1,039,152	1,053,883
Total assets	\$ 11,366,041	\$ 10,211,796	\$ 10,956,282
Liabilities			
Long-term debt (including current portion)	\$ 7,168,592	\$ 7,265,664	\$ 7,378,503
Other current liabilities	2,007,718	588,048	675,674
Total liabilities	9,176,310	7,853,712	8,054,177
Net Assets			
Invested in capital assets, net of related debt	398,921	706,533	690,003
Restricted – expendable for debt service	52,370	51,765	37,522
Unrestricted	1,738,440	1,599,786	2,174,580
Total net assets	2,189,731	2,358,084	2,902,105
Total liabilities and net assets	\$ 11,366,041	\$ 10,211,796	\$ 10,956,282

Significant changes that took place in 2011 relate to the increase in cash and cash equivalents and current liabilities. During the year, cash balances increased by \$1,669,567 (245.0%) in 2011 over 2010. This resulted from the Hospital being overpaid by Medicare during the year. In connection with the overpayment from Medicare during 2011, the Hospital had an increase at June 30, 2011, in its liability to Medicare in the amount of \$1,597,093 compared to June 30, 2010.

Significant changes in the Hospital's balance sheets from 2009 to 2010 include the decrease in cash and cash equivalents of \$341,166 (33.4%) and the decrease in patient accounts receivable of \$147,146 (15.8%). The decrease in cash and cash equivalents is primarily attributable to the Hospital's decrease in operating income. The patient accounts receivable decrease is due primarily to additional allowances for bad debts and commercial insurance claims caused by the current economic environment.

Operating Results and Changes in the Hospital's Net Assets

In 2011 and 2010, the Hospital's net assets decreased by \$168,353 (7.1%) and \$544,021 (18.8%) as shown in Table 2. The decrease in 2011 is made up of several different components and represents an improvement of 69.1% compared with the decrease in net assets for 2010.

Table 2: Operating Results and Changes in Net Assets

	2011	2010	2009
Operating Revenues			
Net patient service revenue	\$ 5,689,912	\$ 4,721,824	\$ 5,036,482
Other operating revenue	54,222	45,703	81,494
Total operating revenues	<u>5,744,134</u>	<u>4,767,527</u>	<u>5,117,976</u>
Operating Expenses			
Salaries and wages and employee benefits	2,992,990	2,721,668	2,629,069
Purchased services and professional fees	473,581	457,768	100,461
Depreciation and amortization	437,408	438,777	457,871
Other operating expenses	1,626,172	1,303,071	1,704,220
Total operating expenses	<u>5,530,151</u>	<u>4,921,284</u>	<u>4,891,621</u>
Operating Income (Loss)	<u>213,983</u>	<u>(153,757)</u>	<u>226,355</u>
Nonoperating Revenues (Expenses)			
Noncapital appropriations – Town of Okeene	85,254	84,513	89,734
Investment return	23,826	21,205	21,047
Noncapital grants and gifts	42,849	34,351	8,283
Abandonment loss	-	-	(96,638)
Interest expense	(534,265)	(530,333)	(559,951)
Total nonoperating revenues (expenses)	<u>(382,336)</u>	<u>(390,264)</u>	<u>(537,525)</u>
Capital Gifts	<u>-</u>	<u>-</u>	<u>4,000</u>
Decrease in Net Assets	<u>\$ (168,353)</u>	<u>\$ (544,021)</u>	<u>\$ (307,170)</u>

Operating Income (Loss)

The first component of the overall change in the Hospital's net assets is its operating income or loss—generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services. In 2011 and 2009, the Hospital reported operating income, and in 2010, the Hospital 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 Okeene, Oklahoma, Blaine County, Oklahoma, and the surrounding area. The Town of Okeene levies sales taxes and appropriates them to the Hospital to provide additional resources to enable the Hospital to serve lower income and other residents.

The operating income for 2011 increased by \$367,740 (239.2%) as compared to 2010. The primary component of the increased operating income is an increase in net patient service revenue of \$968,008 (20.1%). Net patient service revenue increased in 2011 as a result of an increase in patient census and utilization. Salaries and wages also increased in 2011 by \$258,443 (11.0%) due in large part to the increased census and volume.

The operating loss for 2010 increased by \$380,112 (167.9%) as compared to 2009. The primary component of the increased operating loss is a decrease in net patient service revenue of \$314,658 (6.3%). Net patient service revenue decreased because of increased reserves for bad debts and commercial insurance adjustments.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of appropriations from the Town of Okeene, investment income and interest expense, all of which remained relatively constant in 2011 as compared to 2010 and 2009.

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 2011 and 2010, discussed earlier, except for the increased cash flow from operations due to the overpayment by Medicare during 2011.

Capital Asset and Debt Administration

Capital Assets

At June 30, 2011, the Hospital had \$6,541,694 invested in capital assets, net of accumulated depreciation, as detailed in *Note 6* to the financial statements. In 2011, the Hospital purchased new equipment costing \$32,150.

At June 30, 2010, the Hospital had \$6,933,045 invested in capital assets, net of accumulated depreciation, as detailed in *Note 6* to the financial statements. In 2010, the Hospital purchased new equipment costing \$10,988.

Debt

At June 30, 2011 and 2010, the Hospital had \$7,168,592 and \$7,265,664, respectively, in revenue bonds and capital lease obligations outstanding as detailed in *Note 8* to the financial statements. The Hospital issued no new debt in 2011 or 2010.

Other Economic Factors

One large employer in the Hospital's geographic region, CCA Diamondback prison, ceased operations May 28, 2010. CCA Diamondback had more than 300 employees, many of whom were local.

In addition, another local employer, U.S. Gypsum, began a reduction in workforce in July 2009. Due to a declining construction market, the plant was reduced to two shifts resulting in layoffs of 10 employees. In April 2010, the construction market decline caused U.S. Gypsum to cease wallboard production resulting in a decrease from 240 to 180 employees.

Finally, the local school system reduced its workforce by six beginning with the 2010–2011 school year.

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 Business Administration by telephoning 580.822.4417.

**Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital**

A Component Unit of the Town of Okeene, Oklahoma

Balance Sheets

June 30, 2011 and 2010

Assets

	2011	2010
Current Assets		
Cash and cash equivalents	\$ 2,351,037	\$ 681,470
Restricted cash and investments – current	311,370	314,265
Patient accounts receivable, net of allowance; 2011 – \$735,000, 2010 – \$532,000	932,212	783,868
Town appropriations receivable	11,155	11,155
Estimated amounts due from third-party payers	-	210,000
Supplies	153,922	148,483
Prepaid expenses and other	38,832	90,358
Total current assets	3,798,528	2,239,599
Noncurrent Cash and Investments		
Held by trustee for debt service	1,010,374	1,012,695
Less amount required to meet current obligations	311,370	314,265
	699,004	698,430
Capital Assets, Net	6,541,694	6,933,045
Deferred Financing Costs, Net	326,815	340,722
Total assets	\$ 11,366,041	\$ 10,211,796

Liabilities and Net Assets

	<u>2011</u>	<u>2010</u>
Current Liabilities		
Current maturities of long-term debt	\$ 98,089	\$ 97,658
Accounts payable	117,742	115,570
Accrued expenses	243,883	209,978
Accrued interest payable	259,000	262,500
Estimated amounts due to third-party payers	<u>1,387,093</u>	<u>-</u>
Total current liabilities	2,105,807	685,706
Long-term Debt		
	<u>7,070,503</u>	<u>7,168,006</u>
Total liabilities	<u>9,176,310</u>	<u>7,853,712</u>
Net Assets		
Invested in capital assets, net of related debt	398,921	706,533
Restricted – expendable for debt service	52,370	51,765
Unrestricted	<u>1,738,440</u>	<u>1,599,786</u>
Total net assets	<u>2,189,731</u>	<u>2,358,084</u>
Total liabilities and net assets	<u><u>\$ 11,366,041</u></u>	<u><u>\$ 10,211,796</u></u>

Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
A Component Unit of the Town of Okeene, Oklahoma
Statements of Revenues, Expenses and Changes in Net Assets
Years Ended June 30, 2011 and 2010

	2011	2010
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2011 – \$601,695, 2010 – \$515,382	\$ 5,689,912	\$ 4,721,824
Other	54,222	45,703
	5,744,134	4,767,527
Operating Expenses		
Salaries and wages	2,615,839	2,357,396
Employee benefits	377,151	364,272
Purchased services and professional fees	473,581	457,768
Supplies and other	1,626,172	1,303,071
Depreciation and amortization	437,408	438,777
	5,530,151	4,921,284
	213,983	(153,757)
Operating Income (Loss)		
Nonoperating Revenues (Expenses)		
Noncapital appropriations – Town of Okeene	85,254	84,513
Investment income	23,826	21,205
Interest expense	(534,265)	(530,333)
Noncapital grants and gifts	42,849	34,351
	(382,336)	(390,264)
	(168,353)	(544,021)
Excess of Expenses over Revenues and Decrease in Net Assets		
	2,358,084	2,902,105
Net Assets, Beginning of Year		
	\$ 2,189,731	\$ 2,358,084
Net Assets, End of Year		
	\$ 2,189,731	\$ 2,358,084

Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
A Component Unit of the Town of Okeene, Oklahoma
Statements of Cash Flows
Years Ended June 30, 2011 and 2010

	2011	2010
Operating Activities		
Receipts from and on behalf of patients	\$ 7,138,661	\$ 4,628,000
Payments to suppliers and contractors	(2,051,494)	(1,802,842)
Payments to and on behalf of employees	(2,959,085)	(2,706,833)
Other receipts and payments, net	54,222	68,027
Net cash provided by operating activities	2,182,304	186,352
Noncapital Financing Activities		
Noncapital grants and gifts	42,849	34,351
Town appropriations supporting operations	85,254	84,513
Net cash provided by noncapital financing activities	128,103	118,864
Capital and Related Financing Activities		
Principal paid on long-term debt	(108,417)	(124,186)
Interest paid on long-term debt	(526,420)	(534,978)
Purchase of capital assets	(32,150)	(10,988)
Net cash used in capital and related financing activities	(666,987)	(670,152)
Investing Activities		
Purchase of investments	(699,000)	(695,000)
Proceeds from disposition of investments	709,789	695,825
Interest on investments	9,033	21,205
Net cash provided by investing activities	19,822	22,030
Increase (Decrease) in Cash and Cash Equivalents	1,663,242	(342,906)
Cash and Cash Equivalents, Beginning of Year	999,165	1,342,071
Cash and Cash Equivalents, End of Year	\$ 2,662,407	\$ 999,165
Reconciliation of Cash and Cash Equivalents to the Balance Sheets		
Cash and cash equivalents in current assets	\$ 2,351,037	\$ 681,470
Cash equivalents in noncurrent cash and investments held by trustee for debt service	311,370	317,695
	\$ 2,662,407	\$ 999,165

See Notes to Financial Statements

	<u>2011</u>	<u>2010</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided by Operating Activities		
Operating income (loss)	\$ 213,983	\$ (153,757)
Loss on sale of capital assets	-	22,324
Item not requiring cash		
Depreciation and amortization	437,408	438,777
Changes in operating assets and liabilities		
Patient accounts receivable, net	(148,344)	147,176
Supplies, prepaid expenses and other receivables	46,087	13,466
Estimated amounts due to/from third-party payers	1,597,093	(241,000)
Accounts payable and accrued expenses	36,077	(40,634)
	<u> </u>	<u> </u>
Net cash provided by operating activities	<u>\$ 2,182,304</u>	<u>\$ 186,352</u>

**Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital**

A Component Unit of the Town of Okeene, Oklahoma

Notes to Financial Statements

June 30, 2011 and 2010

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

Nature of Operations and Reporting Entity

Okeene Municipal Hospital (the Hospital) is operated under the Okeene Municipal Hospital and Schallmo Authority (the Authority), a public trust established for the benefit of the Town of Okeene in Blaine County, Oklahoma. The Authority is a component unit of the Town of Okeene, Oklahoma (the Town). The Town Board appoints the Board of Trustees of the Authority.

The Authority operates the Hospital under a bargain lease agreement with the Town. The initial term of the lease is from December 1, 2004 to November 30, 2014, and will remain in effect thereafter as long as any security interest in the Hospital facility has been given to a financial institution or creditor. The lease has been amended to extend the lease term by an additional 21 years until November 30, 2035. Upon termination of the lease, control of Hospital operations reverts back to the Town.

The Hospital, located in Okeene, Oklahoma, is a 17-bed critical access hospital and primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in the Okeene, Oklahoma, area.

Basis of Accounting and Presentation

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally, Town 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 Town appropriations, investment income and interest on capital assets-related debt, are included in nonoperating revenues and expenses. The Hospital first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

The Hospital prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
A Component Unit of the Town of Okeene, Oklahoma
Notes to Financial Statements
June 30, 2011 and 2010

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 and Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2011 and 2010, cash equivalents consisted primarily of money market accounts with brokers and a certificate of deposit.

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to \$250,000. Pursuant to legislation enacted in 2010, the FDIC will fully insure all noninterest-bearing transaction accounts beginning December 31, 2010 through December 31, 2012, at all FDIC-insured institutions.

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 in U.S. Treasury, agency and instrumentality obligations with a remaining maturity of one year or less at time of acquisition and in nonnegotiable certificates of deposit are carried at amortized cost. 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 carried at other than fair value and the net change for the year in the fair value of investments carried at fair value.

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.

**Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital**

A Component Unit of the Town of Okeene, Oklahoma

Notes to Financial Statements

June 30, 2011 and 2010

Supplies

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

Capital Assets

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

Land improvements, buildings and leasehold improvements	5–50 years
Equipment	3–25 years

Deferred Financing Costs

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt using the straight-line method.

Compensated Absences

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

Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets, net of related debt, 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 assets are noncapital assets that must be used for a particular purpose, as specified by creditors, grantors or donors external to the Hospital, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the definition of invested in capital assets, net of related debt or restricted expendable.

**Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital**

A Component Unit of the Town of Okeene, Oklahoma

Notes to Financial Statements

June 30, 2011 and 2010

Net Patient Service Revenue

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

Charity Care

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

Income Taxes

As an essential government function of the Town, 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.

Note 2: Net Patient Service Revenue

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

Medicare – Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid based on a cost reimbursement methodology. Certain outpatient services related to Medicare beneficiaries are paid based on a combination of fee schedules and a cost reimbursement methodology. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare administrative contractor. The Hospital's Medicare cost reports have been audited by the Medicare administrative contractor through June 30, 2009.

Medicaid – The Hospital is reimbursed for services rendered to patients covered by the state Medicaid program on a prospective per discharge or fee schedule method with no retroactive adjustments. These payment rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

**Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital**

A Component Unit of the Town of Okeene, Oklahoma

Notes to Financial Statements

June 30, 2011 and 2010

Approximately 82% and 81% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended June 30, 2011 and 2010, 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: Unrestricted Town Appropriations

Effective October 1, 1999, the citizens of Okeene, Oklahoma, approved a 1% sales tax to be appropriated to the Hospital to support its operations. The tax is to remain in effect so long as the Hospital is in operation or until the sales tax is repealed. The Town collects the sales tax and remits it to the Hospital monthly. The Hospital received approximately 1% and 2% of its financial support from Town appropriations related to sales tax during 2011 and 2010, respectively. Revenue from Town appropriations is recognized in the year in which the sales tax is earned.

Note 4: 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 Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law. State law requires that all deposits for public trusts be insured or collateralized.

At June 30, 2011 and 2010, \$387,156 and \$0 of the Hospital's bank balances of \$3,098,209 and \$731,484, respectively, were exposed to custodial credit risk as follows:

	<u>2011</u>	<u>2010</u>
Uninsured and uncollateralized	<u>\$ 387,156</u>	<u>\$ -</u>

**Okeene Municipal Hospital and Schallmo Authority
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Investments

At June 30, 2011 and 2010, the Hospital had the following investments and maturities:

	June 30, 2011				
	Maturities in Years				
	Fair Value	Less than 1	1-5	6-10	More than 10
Money market mutual fund	\$ 311,370	\$ 311,370	\$ -	\$ -	\$ -
	<u>\$ 311,370</u>	<u>\$ 311,370</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
	June 30, 2010				
	Maturities in Years				
	Fair Value	Less than 1	1-5	6-10	More than 10
U.S. agency obligations	\$ 695,000	\$ -	\$ 695,000	\$ -	\$ -
Money market mutual funds	317,695	317,695	-	-	-
	<u>\$ 1,012,695</u>	<u>\$ 317,695</u>	<u>\$ 695,000</u>	<u>\$ -</u>	<u>\$ -</u>

Interest Rate Risk – Interest rate risk is the exposure to fair value losses arising from rising interest rates. The Hospital’s policy does not address interest rate risk; however, all the Hospital’s investments are held by a trustee for debt service. 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. At June 30, 2011 and 2010, the Hospital’s investments in U.S. agency obligations not directly guaranteed by the U.S. government were rated AAA by Standard & Poor’s and Aaa by Moody’s Investors Service and its investments in money market mutual funds were not rated.

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

Concentration of Credit Risk – The Hospital places no limit on the amount that may be invested in any one issuer. At June 30, 2010, the Hospital’s investment in Federal Home Loan Mortgage Corporation bonds constituted 69% of its total investments.

Foreign Currency Risk – This risk relates to adverse effects on the fair value of an investment from changes in exchange rates. The Hospital had no investments denominated in foreign currency at June 30, 2011 and 2010.

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Summary of Carrying Values

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

	2011	2010
Carrying value		
Deposits	\$ 3,050,041	\$ 681,470
Investments	311,370	1,012,695
	\$ 3,361,411	\$ 1,694,165
Included in the following balance sheet captions		
Cash and cash equivalents	\$ 2,351,037	\$ 681,470
Restricted cash and investments – current	311,370	314,265
Noncurrent cash and investments	699,004	698,430
	\$ 3,361,411	\$ 1,694,165

Investment Income

Investment income for the years ended June 30, 2011 and 2010, consisted of interest income of \$23,826 and \$21,205, respectively.

Note 5: 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 June 30, 2011 and 2010, consisted of:

	2011	2010
Patients	\$ 795,450	\$ 714,454
Insurance carriers	148,739	204,155
Medicare	715,645	392,912
Medicaid	7,378	4,347
	1,667,212	1,315,868
Less allowance for uncollectible accounts	735,000	532,000
	\$ 932,212	\$ 783,868
Patient accounts receivable, net		

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Note 6: Capital Assets

Capital assets activity for the years ended June 30, 2011 and 2010, was:

	2011				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 151,601	\$ -	\$ -	\$ -	\$ 151,601
Land improvements	72,694	-	-	-	72,694
Buildings, improvements and fixed equipment	8,620,355	-	-	-	8,620,355
Major moveable equipment	<u>761,060</u>	<u>32,150</u>	<u>(37,522)</u>	-	<u>755,688</u>
	<u>9,605,710</u>	<u>32,150</u>	<u>(37,522)</u>	-	<u>9,600,338</u>
Less accumulated depreciation					
Land improvements	24,931	5,244	-	-	30,175
Buildings, improvements and fixed equipment	2,034,269	380,826	-	-	2,415,095
Major moveable equipment	<u>613,465</u>	<u>37,431</u>	<u>(37,522)</u>	-	<u>613,374</u>
	<u>2,672,665</u>	<u>423,501</u>	<u>(37,522)</u>	-	<u>3,058,644</u>
Capital assets, net	<u>\$ 6,933,045</u>	<u>\$ (391,351)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 6,541,694</u>
	2010				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 151,601	\$ -	\$ -	\$ -	\$ 151,601
Land improvements	72,694	-	-	-	72,694
Buildings, improvements and fixed equipment	8,620,355	-	-	-	8,620,355
Major moveable equipment	<u>836,396</u>	<u>10,988</u>	<u>(86,324)</u>	-	<u>761,060</u>
	<u>9,681,046</u>	<u>10,988</u>	<u>(86,324)</u>	-	<u>9,605,710</u>
Less accumulated depreciation					
Land improvements	19,690	5,241	-	-	24,931
Buildings, improvements and fixed equipment	1,653,448	380,821	-	-	2,034,269
Major moveable equipment	<u>638,657</u>	<u>38,808</u>	<u>(64,000)</u>	-	<u>613,465</u>
	<u>2,311,795</u>	<u>424,870</u>	<u>(64,000)</u>	-	<u>2,672,665</u>
Capital assets, net	<u>\$ 7,369,251</u>	<u>\$ (413,882)</u>	<u>\$ (22,324)</u>	<u>\$ -</u>	<u>\$ 6,933,045</u>

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Note 7: Medical Malpractice Claims

The Hospital is a member of Cimarron Insurance Exchange, RRG (Reciprocal Risk Retention Group) (the RRG) approved by the state of Vermont to provide hospital professional and general liability coverage to its subscribers. The RRG 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. The RRG members are provided hospital professional and general liability insurance under claims-made policies on a fixed premium basis.

The Hospital has obtained letters of credit totaling \$79,928 from a commercial bank to secure equity ownership in the RRG in accordance with the subscriber agreement set forth between the Hospital and the RRG. As stated by the subscriber agreement, the beneficiary of the letters of credit is the Commissioner of Insurance of the State of Vermont. The commissioner has the authority to draw down on the letters of credit as needed to fund the RRG. As of June 30, 2011 and 2010, there have been no draws on the letters of credit.

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

Note 8: Long-Term Debt

The following is a summary of long-term debt transactions for the Hospital for the years ended June 30, 2011 and 2010:

	2011				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Revenue bonds	\$ 7,500,000	\$ -	\$ (100,000)	\$ 7,400,000	\$ 100,000
Bond discount	(266,618)	-	11,345	(255,273)	(10,759)
	<u>7,233,382</u>	<u>-</u>	<u>(88,655)</u>	<u>7,144,727</u>	<u>89,241</u>
Capital lease obligation	<u>32,282</u>	<u>-</u>	<u>(8,417)</u>	<u>23,865</u>	<u>8,848</u>
Total long-term debt	<u>\$ 7,265,664</u>	<u>\$ -</u>	<u>\$ (97,072)</u>	<u>\$ 7,168,592</u>	<u>\$ 98,089</u>

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June 30, 2011 and 2010

	2010				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Revenue bonds	\$ 7,600,000	\$ -	\$ (100,000)	\$ 7,500,000	\$ 100,000
Bond discount	(277,965)	-	11,347	(266,618)	(10,759)
	<u>7,322,035</u>	<u>-</u>	<u>(88,653)</u>	<u>7,233,382</u>	<u>89,241</u>
Note payable to bank	1,218	-	(1,218)	-	-
Capital lease obligation	<u>55,250</u>	<u>-</u>	<u>(22,968)</u>	<u>32,282</u>	<u>8,417</u>
Total long-term debt	<u>\$ 7,378,503</u>	<u>\$ -</u>	<u>\$ (112,839)</u>	<u>\$ 7,265,664</u>	<u>\$ 97,658</u>

Revenue Bonds

The Series 2006 Revenue Bonds (the Bonds) in the original amount of \$7,800,000 and sold at a discount of \$312,000 dated March 15, 2006, bear interest at 7.00%. The Bonds are payable with principal payments due annually and interest payments due semiannually through January 1, 2035. The Hospital is required to make monthly deposits to the debt service fund held by the trustee in the amount of 1/6 of the next semiannual interest payment due and 1/12 the amount of the next annual principal payment due. All of the Bonds still outstanding may be redeemed at the Hospital's option on or after January 1, 2016. The redemption price is 101% through December 31, 2016, decreasing to 100.5% from January 1 to December 31, 2017, and decreasing to 100% on or after January 1, 2018. The Bonds are secured by the revenues and certain assets of the Hospital described in the Financing and Security Agreement (the Agreement).

The Agreement requires that certain funds be established with the trustee. Accordingly, these funds are included as assets held by trustee for debt service in the accompanying balance sheets. The Agreement also requires the Hospital to comply with certain restrictive covenants, including:

- Maintaining minimum insurance coverage
- Maintaining a debt service coverage ratio of at least 1.25 to 1.00
- Restrictions on incurrence of additional debt
- Maintaining minimum days cash on hand of 45 days
- Maintaining minimum aged receivables of not more than 120 days
- Maintaining maximum aged payables of not more than 120 days
- Maintaining minimum current ratio of 2.00 to 1.00

**Okeene Municipal Hospital and Schallmo Authority
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June 30, 2011 and 2010**

At June 30, 2010, the Hospital had a debt service coverage ratio of 0.64 to 1.00, which is considered an Event of Default as defined by the Agreement. The Agreement stipulates that as a result of the Event of Default the Bonds may be declared and immediately shall become due and payable at the option of the bond trustee. The bond trustee has not formally waived this Event of Default. Under accounting principles generally accepted in the United States of America, debt subject to acceleration is classified on the balance sheet as a current liability. Hospital management has elected to classify the portion of the Bonds not originally scheduled to mature in the next year as long-term debt in the accompanying 2010 balance sheet. The effect of this treatment is to understate current liabilities and overstate long-term debt by \$7,144,141 in the accompanying 2010 balance sheet.

At June 30, 2011, the Hospital had a current ratio of 1.80 to 1.00, which is in violation of the covenants.

The discount on the Bonds is being amortized over the term of the Bonds using the straight-line method.

The debt service requirements as of June 30, 2011, are as follows:

Year Ending June 30,	Total to be Paid	Principal	Interest
2012	\$ 618,000	\$ 100,000	\$ 518,000
2013	611,000	100,000	511,000
2014	604,000	100,000	504,000
2015	697,000	200,000	497,000
2016	683,000	200,000	483,000
2017–2021	3,205,000	1,000,000	2,205,000
2022–2026	3,285,000	1,500,000	1,785,000
2027–2031	3,218,000	2,000,000	1,218,000
2032–2035	2,599,000	2,200,000	399,000
	<u>\$ 15,520,000</u>	<u>\$ 7,400,000</u>	<u>\$ 8,120,000</u>

Note Payable to Bank

The note payable to bank was due December 3, 2009, with principal and interest at 8.5% payable monthly. The note was secured by certain capital assets. The note was paid in full during the year ended June 30, 2010.

**Okeene Municipal Hospital and Schallmo Authority
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June 30, 2011 and 2010

Capital Lease Obligation

The Hospital is obligated under a lease for equipment that is accounted for as a capital lease. Assets under a capital lease at June 30, 2011 and 2010, totaled \$42,991, net of accumulated depreciation of \$13,819 and \$7,677, respectively. The following is a schedule by year of future minimum lease payments under the capital lease, including interest at 5% together with the present value of the future minimum lease payments as of June 30, 2011:

2012	\$	9,837
2013		9,837
2014		<u>5,810</u>
Total minimum lease payments		25,484
Less amount representing interest		<u>1,619</u>
Present value of future minimum lease payments	\$	<u><u>23,865</u></u>

Note 9: 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 charges relating to these services are approximately as follows:

	<u>2011</u>	<u>2010</u>
Charity allowances	\$ 72,000	\$ 71,000
Medicaid welfare	<u>448,000</u>	<u>310,000</u>
	<u><u>\$ 520,000</u></u>	<u><u>\$ 381,000</u></u>

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

Okeene Municipal Hospital and Schallmo Authority
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Notes to Financial Statements
June 30, 2011 and 2010

Note 10: Risks and Uncertainties

Current Economic Conditions

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

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

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

Note 11: 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 required contributions, determined in accordance with the terms of the plan. The plan is administered by the Hospital. 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 2.7% and 0.2%, respectively, for 2011 and 3.7% and 1.6%, respectively, for 2010. Contributions actually made by plan members and the Hospital aggregated approximately \$73,000 and \$4,000, respectively, during the year ended June 30, 2011, and approximately \$64,000 and \$28,000, respectively, during the year ended June 30, 2010.

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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 Accountants' 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
Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal Hospital
Okeene, Oklahoma

We have audited the financial statements of Okeene Municipal Hospital and Schallmo Authority d/b/a Okeene Municipal Hospital (the Hospital) as of and for the year ended June 30, 2011, and have issued our report thereon dated November 17, 2011, which expressed a qualified opinion on the 2010 financial statements because of a departure from accounting principles generally accepted in the United States of America. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the Hospital's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over financial reporting.

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 Hospital's financial statements will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses as defined above.

Board of Trustees
Okeene Municipal Hospital and Schallmo Authority
d/b/a Okeene Municipal 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*.

We also noted certain matters that we reported to the Hospital's management in a separate letter dated November 17, 2011.

This report is intended solely for the information and use of the governing body, management and others within the Hospital and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

November 17, 2011