Management's Discussion and Analysis
And Financial Statements
March 31, 2017 and 2016

Sequoyah County-City of Sallisaw Hospital Authority d/b/a Sequoyah Memorial Hospital

EideBailly

CPAs & BUSINESS ADVISORS

Independent Auditor's Report

To the Board of Trustees
Sequoyah County-City of Sallisaw Hospital Authority
d/b/a Sequoyah Memorial Hospital
Sallisaw, OK

Report on the Financial Statements
We have audited the accompanying financial statements of Sequoyah County-City of Sallisaw Hospital Authority d/b/a Sequoyah Memorial Hospital (Hospital) which comprise the statements of net position as of March 31, 2017 and 2016, and the related statements of revenues, expenses, and changes in net position and statements of cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements.

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

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Hospital'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 Hospital'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 Sequoyah County-City of Sallisaw Hospital Authority d/b/a Sequoyah Memorial Hospital as of March 31, 2017 and 2016, and results of operations, changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information
Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 6 be presented to supplement the basic financial statements. Such 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. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquires of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquires, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*
In accordance with *Government Auditing Standards*, we have also issued our report dated June 19, 2018 on our consideration of the Hospital's internal control over financial reporting and on 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control over financial reporting and compliance.

Eide Bailly LLP

Oklahoma City, Oklahoma
June 19, 2018

Introduction

This discussion and analysis of the financial performance of Sequoyah County-City of Sallisaw Hospital Authority d/b/a Sequoyah Memorial Hospital (Hospital) provides an overall review of the Hospital's financial activities and balances as of and for the years ended March 31, 2017, 2016, and 2015. The intent of this discussion and analysis is to provide further information on the Hospital's performance as a whole; readers should also review the basic financial statements and the notes thereto to enhance their understanding of the Hospital's financial status.

Financial Highlights

- Current assets decreased in 2017 by $1,203,129 or 38% and decreased in 2016 by $146,415 or 4%.
- Total liabilities decreased in 2017 by $594,950 or 13% and increased in 2016 by $177,045 or 4%.
- The Hospital's net position decreased in 2017 by $2,101,626 or 75% and decreased in 2016 by $442,054 or 14%.
- The Hospital reported an operating loss in 2017 of $2,670,559 and an operating loss in 2016 of $1,207,661. During 2017, operating loss increased by $1,462,898 or 121% and decreased by $2,404,235 or 67% in 2016.
- Other operating revenue decreased by $186,382 or 68% in 2017 and decreased by $235,171 or 46% in 2016.
- Operating expenses decreased in 2017 by $1,541,042 or 10% and decreased $814,162 or 5% in 2016.

Using This Annual Report

The Hospital's financial statements consist of three statements – Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position, and Statements of Cash Flows. These financial statements and related notes provide information about activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by 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 Statements of Net Position and Statements of Revenues, Expenses and Changes in Net Position

One of the most important questions asked about the Hospital's finances is "Is the Hospital as a whole better or worse off as a result of the year's activities?" The Statements of Net Position and the Statements of Revenues, Expenses and Changes in Net Position report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net position and changes in it. You can think of the Hospital's net position - the difference between assets and liabilities - as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the Hospital's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the Hospital.

The Statements of Cash Flows

The final required statement is the Statements of Cash Flows, which reports cash receipts, cash payments, and net changes in cash resulting from operations, investing and financing 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 balance during the reporting period.

The Hospital's Net Position

The Hospital's net position is the difference between its assets and liabilities reported in the Statements of Net Position. The Hospital's net position decreased by $2,101,626 or 75% in 2017 and decreased by $442,054 or 14% in 2016 as shown below.

Table 1: Assets, Liabilities, and Net Position

	2017	2016	2015
Assets			
Current assets	$ 1,993,955	$ 3,197,084	$ 3,343,499
Capital assets, net	2,621,197	3,035,719	3,211,625
Noncurrent assets	7,330	1,086,255	1,028,943
Total assets	$ 4,622,482	$ 7,319,058	$ 7,584,067
Liabilities			
Total current liabilities	$ 2,156,395	$ 3,493,737	$ 3,457,087
Long term debt	1,782,787	1,040,395	900,000
Total liabilities	3,939,182	4,534,132	4,357,087
Net Position			
Net investment in capital assets	2,480,802	2,858,054	3,211,625
Restricted, expendable for capital acquisitions	-	-	445,057
Unrestricted	(1,797,502)	(73,128)	(429,702)
Total net position	683,300	2,784,926	3,226,980
Total liabilities and net position	$ 4,622,482	$ 7,319,058	$ 7,584,067

Assets, Liabilities, and Net Position

The Hospital's total assets decreased $2,696,576 or 37% in 2017 and decreased $265,009 or 3% in 2016. Cash and cash equivalents decreased $489,766 or 97% in 2017 compared to 2016 which increased $418,813 or 471%. Patient accounts receivable, net of allowances, decreased $660,132 or 31% in 2017 compared to 2016 which increased $321,948 or 18%. Certificate of deposit decreased $975,339 or 100% in 2017 compared to 2016 which increased $6,330 or 1%.

The Hospital's total liabilities decreased $594,950 or 13% in 2017 and increased $177,045 or 4% in 2016. Notes payable decreased $1,298,427 or 100% in 2017 compared to 2016 which increased $73,090 or 6%. Long-term debt increased $830,557 or 77% in 2017 compared to 2016 which increased $177,665 or 20%. Accrued expenses decreased $400,494 or 51% in 2017 compared to 2016 which increased $443,514 or 131%.

Table 2: Operating Results and Changes in Net Position

	2017	2016	2015
Operating Revenues			
Net patient service revenue	$ 10,538,565	$ 13,356,123	$ 11,530,879
Other operating revenue	85,897	272,279	507,450
Total operating revenues	10,624,462	13,628,402	12,038,329
Operating Expenses			
Salaries and wages	5,968,245	6,756,553	7,569,507
Employee benefits	891,205	1,485,385	1,466,838
Purchased services and professional fees	2,748,891	2,722,416	2,994,706
Supplies and other	3,150,054	3,297,005	3,034,067
Depreciation	536,626	574,704	585,107
Total operating expenses	13,295,021	14,836,063	15,650,225
Operating Loss	(2,670,559)	(1,207,661)	(3,611,896)
Nonoperating Revenues (Expenses)			
Interest income	3,728	7,994	7,239
Noncapital appropriations	673,549	618,431	-
Interest expense	(112,221)	(93,361)	(53,783)
Noncapital gifts	16,004	14,622	3,194
Gain (loss) on disposal of capital assets	(12,127)	147,648	300
Total nonoperating revenues (expenses)	568,933	695,334	(43,050)
Expenses in Excess of Revenues Before Capital Appropriations	(2,101,626)	(512,327)	(3,654,946)
Capital Appropriations, City of Sallisaw, Oklahoma	-	70,273	675,229
Change in Net Position	$ (2,101,626)	$ (442,054)	$ (2,979,717)

Operating Results

The first component of the overall change in the Hospital's net position is its operating results. Generally, the operating income or loss is the difference between net patient service and other operating revenues and the expenses incurred to perform those services. The past three years the Hospital has had operating losses.

The operating loss for 2017 increased by $1,489,898 or 123% as compared to the decrease of $2,404,235 or 67% in 2016.

The primary components of the operating loss are:

- Net patient service revenue decreased $2,817,558 or 21% in 2017 compared to an increase of $1,825,244 or 16% in 2016. The decrease in 2017 is attributed to additional write-offs due to untimely billing. The increase in 2016 is attributed to the increased services provided by the Hospital.
- Salaries, wages and employee benefits expense decreased $1,382,488 or 17% in 2017 and $794,407 or 9% in 2015. The increases are primarily due to a reduction in employees during 2017 and 2016.

Non-operating Revenues and Expenses

Non-operating revenues and expenses consist primarily of non-capital appropriations and interest expense. Non-capital appropriations increased $55,118 or 9% in 2017 and increased $13,475 or 2% in 2016. Interest expense increased $18,860 or 20% in 2017 as compared to the increase of $39,578 or 74% in 2016.

The Hospital's Cash Flows

The Hospital's overall liquidity decreased during the year with a net decrease to cash of $489,766 when compared with 2016. Cash flows used for operating activities increased by $868,316 during 2017 when compared with 2016. Cash from non-capital financing activities decreased by $401,627 when compared with 2016. Cash used for capital and capital related financing activities increased by $226,474 when compared with 2016. Cash from investing activities increased by $977,403 when compared to 2016.

Capital Assets

The Hospital had $2,621,197 invested in capital assets at the end of 2017 and $3,035,719 at the end of 2016, net of accumulated depreciation, as detailed in Note 4 to the financial statements. The Hospital acquired new capital assets costing $146,734 in 2017 and $531,493 in 2016.

Debt

The Hospital refinanced the line of credit with a long-term debt and had a reduction in debt of $467,871 during 2017. The Hospital had total debt of $1,908,221 at the end of 2017, as detailed in Note 6 to the financial statements. The Hospital incurred additional debt of $250,755 for a capital lease and line of credit in 2016 and had debt of $2,553,757 at the end of 2016, as detailed in Note 6 to the financial statements.

Contacting the Hospital's Financial Management

This financial report is designed to provide our patients, suppliers 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 administration by calling 918-774-1100.

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	2017	2016
Assets		
Current Assets		
Cash	$ 18,056	$ 507,822
Receivables		
Patient, net of estimated uncollectibles of $4,412,000 in 2017 and $6,218,000 in 2016	1,463,803	2,123,935
Capital appropriations	56,170	58,950
Other	32	28,542
Supplies	387,981	385,735
Prepaid expenses	67,913	92,100
Total current assets	1,993,955	3,197,084
Noncurrent Cash and Investments		
Certificate of deposit	-	975,339
Capital Assets		
Capital assets not being depreciated	193,633	200,133
Capital assets being depreciated, net	2,427,564	2,835,586
Total capital assets	2,621,197	3,035,719
Other Assets		
Cash value of life insurance	7,330	110,916
Total assets	$ 4,622,482	$ 7,319,058

	2017	2016
Liabilities and Net Position		
Current Liabilities		
Notes payable	$ -	$ 1,298,427
Current maturities of long-term debt	125,435	37,270
Accounts payable	1,525,302	1,374,888
Estimated third-party payor settlements	123,000	-
Accrued expenses	382,658	783,152
Total current liabilities	2,156,395	3,493,737
Long-Term Debt, Less Current Maturities	1,782,787	1,040,395
Total liabilities	3,939,182	4,534,132
Net Position		
Net investment in capital assets	2,480,802	2,858,054
Unrestricted	(1,797,502)	(73,128)
Total net position	683,300	2,784,926
Total liabilities and net position	$ 4,622,482	$ 7,319,058

	2017	2016
Operating Revenue		
Net patient service revenue, net of provision for bad debts of $5,750,390 in 2017 and $6,037,124 in 2016	$ 10,538,565	$ 13,356,123
Other revenue	85,897	272,279
Total operating revenues	10,624,462	13,628,402
Operating Expenses		
Salaries and wages	5,968,245	6,756,553
Employee benefits	891,205	1,485,385
Purchased services and professional fees	2,748,891	2,722,416
Supplies and other	3,150,054	3,297,005
Depreciation	536,626	574,704
Total operating expenses	13,295,021	14,836,063
Operating Loss	(2,670,559)	(1,207,661)
Nonoperating Revenues (Expenses)		
Interest income	3,728	7,994
Noncapital appropriation	673,549	618,431
Interest expense	(112,221)	(93,361)
Noncapital gifts	16,004	14,622
Gain (loss) on disposal of capital assets	(12,127)	147,648
Total nonoperating revenues (expenses)	568,933	695,334
Expenses in Excess of Revenues Before Capital Appropriations	(2,101,626)	(512,327)
Capital Appropriations - City of Sallisaw, Oklahoma	-	70,273
Change in Net Position	(2,101,626)	(442,054)
Net Position, Beginning of Year	2,784,926	3,226,980
Net Position, End of Year	$ 683,300	$ 2,784,926

	2017	2016
Operating Activities		
Receipts from and on behalf of patients	$ 11,321,697	$ 13,061,166
Payments to suppliers and contractors	(5,623,004)	(6,288,507)
Payments to employees	(7,259,944)	(7,798,424)
Other receipts	114,407	447,237
Net Cash used for Operating Activities	(1,446,844)	(578,528)
Noncapital Related Financing Activities		
Noncapital appropriations	676,329	559,481
Proceeds from note payable	749,203	11,987,610
Principal payments on note payable	(1,179,803)	(11,914,520)
Interest paid	(106,999)	(90,832)
Noncapital grants and contributions	16,004	14,622
Net Cash from Noncapital Related Financing Activities	154,734	556,361
Capital and Related Financing Activities		
Capital appropriations	-	125,765
Principal payments on long-term debt	(37,270)	(18,717)
Interest paid	(5,222)	(2,529)
Purchase of property and equipment	(140,234)	(335,111)
Proceeds from the sale of equipment	6,003	280,343
Net Cash from (used for) Capital and Related Financing Activities	(176,723)	49,751
Investing Activities		
Proceeds from redemption of certificates of deposit	975,339	-
Purchase of certificates of deposit	-	(6,330)
Interest income	3,728	7,994
Net Cash from Investing Activities	979,067	1,664
Net Change in Cash	(489,766)	29,248
Cash, Beginning of Year	507,822	478,574
Cash, End of Year	$ 18,056	$ 507,822

	2017	2016
Reconciliation of Operating Loss to Net Cash used for Operating Activities		
Operating Loss	$ (2,670,559)	$ (1,207,661)
Adjustments to reconcile operating loss to net cash used for operating activities		
Depreciation	536,626	574,704
Provision for bad debts	5,750,390	6,037,124
Changes in assets and liabilities		
Patient receivables	(5,090,258)	(6,359,081)
Other receivables	28,510	174,958
Supplies	(2,246)	119,562
Prepaid expenses and other	127,773	128,576
Accounts payable	150,414	(517,224)
Accrued expenses	(400,494)	443,514
Estimated third-party payor settlements	123,000	27,000
Net Cash used for Operating Activities	$ (1,446,844)	$ (578,528)
Supplemental Disclosures of Non Capital and Capital Related Financing Activities		
Equipment financed through lease arrangement	$ -	$ 196,382

Note 1 - Reporting Entity and Summary of Significant Accounting Policies

The financial statements of Sequoyah County-City of Sallisaw Hospital Authority d/b/a Sequoyah Memorial Hospital (Hospital) have been prepared in accordance with generally accepted accounting principles in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting and reporting policies and practices used by the Hospital are described below.

Reporting Entity

The Hospital is a 35-bed acute care hospital located in the city of Sallisaw, Oklahoma (City). The Hospital is a public trust created under the laws of the State of Oklahoma, and is exempt from income taxes under Section 115 of the Internal Revenue Code as a political subdivision of the State of Oklahoma. The Hospital is governed by the Board of Trustees, which is appointed by the City.

For financial reporting purposes, the Hospital has included all funds, organizations, agencies, boards, commissions, and authorities. The Hospital has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Hospital are such that the exclusion would cause the Hospital's financial situation to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the Hospital to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the Hospital.

Blended Component Unit

On December 10, 2012, the SMH Physician Group, LLC (Physician Group), was established as a limited liability company in the state of Oklahoma for the purpose of providing physician services to patients in Sallisaw, Oklahoma and the surrounding communities. The Hospital is the sole member of the LLC. The Physician Group began operations on April 1, 2013. The Physician Group is included as a blended component unit of the Hospital. The financial statements include only the financial activity of the Hospital and Physician Group, collectivity referred to as the Hospital. Financial statements of the Physician Group can be obtained by contacting the Hospital's Administration.

Measurement Focus and Basis of Accounting and Presentation

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Revenues are recognized when earned, and expenses are recorded when the liability is incurred.

Basis of Presentation

The statement of net position displays the Hospital's assets and liabilities with the difference reported as net position. Net position is reported in the following categories/components:

> *Net investment in capital assets* consists of net capital assets reduced by the outstanding balances of any related debt obligations attributable to the acquisition, construction or improvement of those assets or the related debt obligations related to those assets or debt obligations.
>
> *Restricted, expendable* consists of assets whose use is restricted for a specific purpose. The Hospital does not have restricted net position as of March 31, 2017 and 2016.
>
> *Restricted, nonexpendable* is subject to externally imposed stipulations which require them to be maintained permanently by the Hospital. The Hospital does not have restricted net position as of March 31, 2017 and 2016.
>
> *Unrestricted net position* consists of net position not meeting the definition of the preceding categories. Unrestricted net position often has constraints on resources imposed by management which can be removed or modified.

When an expense is incurred that can be paid using either restricted or unrestricted resources (net position), the Hospital's policy is to first apply the expense toward the most restrictive resources and then toward unrestricted resources.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The net patient service revenue for the years ended March 31, 2017 and 2016 decreased approximately $529,000 and $19,000 due to removal of allowances previously estimated that are no longer necessary as a result of decreasing commercial insurance and patient payments compared to originally estimated amounts.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with an original maturity of three months or less, excluding internally designated or restricted cash and investments. For purposes of the statement of cash flows, the Hospital considers all cash and investments with an original maturity of three months or less as cash and cash equivalents.

Patient Receivables

Patient receivables are uncollateralized patient and third-party payor obligations. Patient receivables, excluding amounts due from third-party payors, are turned over to a collection agency if the receivables remain unpaid after the Hospital's collections procedures. The Hospital does not charge interest on the unpaid patient receivables. Payments of patient receivables are allocated to the specific claims identified on the remittance advice or, if unspecified, are applied to the earliest unpaid claim.

The carrying amount of patient receivables is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected from patients and third-party payors. Management reviews patient receivables by payor class and applies percentages to determine estimated amounts that will not be collected from third parties under contractual agreements and amounts that will not be collected from patients due to bad debts. Management considers historical write off and recovery information in determining the estimated bad debt provision.

Capital and Non Capital Appropriations

The Hospital benefits from a 0.5% sales tax assessment. The tax, approved by the Board of Commissioners of the City of Sallisaw, has no expiration date. The Hospital received approximately 6% and 4% of its financial support from city appropriations during the years ended March 31, 2017 and 2016. These funds are restricted for capital improvements and debt service. In November 2015, Board of Commissioners of the City of Sallisaw, released the restriction on the sales tax funds to be used for operations of the Hospital.

Supplies

Supplies are stated at lower of cost (first-in, first-out) or market and are expenses when used.

Noncurrent Cash and Deposits

Noncurrent cash and deposits, certificates of deposit and other deposits are recorded at historical cost.

Capital Assets

Capital assets acquisitions in excess of $500 are capitalized and recorded at cost. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Amortization is included in depreciation and amortization in the financial statements. The estimated useful lives of property and equipment are as follows:

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

Gifts of long-lived assets such as land, buildings, or equipment are reported as additions to unrestricted net position, and are excluded from expenses in excess of revenues. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted net position.

Compensated Absences

The Hospital's employees earn vacation days at varying rates depending on years of service. Employees may accumulate vacation days up to a specified maximum. Compensated absence liabilities are computed using the regular pay in effect at the statements of net position date plus an additional amount for compensation related payments such as Social Security and Medicare taxes computed using rates in effect at that date.

Operating Revenues and Expenses

The Hospital's statement of revenues, expenses, and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues and expenses of the Hospital result from exchange transactions associated with providing health care services - the Hospital's principal activity, and the costs of providing those services, including depreciation and excluding interest cost. All other revenues and expenses are reported as nonoperating.

Net Patient Service Revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Since the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The amount of charges foregone for services provided under the Hospital's charity care policy were approximately $0 and $22,000 for the years ended September 30, 2017 and 2016. Total direct and indirect costs related to these foregone charges were approximately $0 and $8,000 at March 31, 2017 and 2016, based on an average ratio of cost to gross charges.

Grants and Contributions

The Hospital may receive grants as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after expenses in excess of revenues.

Electronic Health Record Incentive Payments

The American Recovery and Reinvestment Act of 2009 (ARRA) amended the Social Security Act to establish incentive payments under the Medicare and Medicaid programs for certain hospitals and professionals that demonstrate meaningful use of certified Electronic Health Records (EHR) technology.

To qualify for the EHR incentive payments, hospitals and physicians must meet designated EHR meaningful use criteria. In addition, hospitals must attest that they have used certified EHR technology, satisfied the meaningful use objectives, and specify the EHR reporting period. This attestation is subject to audit by the federal government or its designee. The EHR incentive payment to hospitals for each payment year is calculated as a product of (1) an initial amount; (2) the Medicare share; and (3) a transition factor applicable to that payment year.

The Hospital recognizes EHR incentive payments as revenue when there is reasonable assurance that the Hospital will comply with the conditions attached to the incentive payments. EHR incentive payments are included in other operating revenue in the accompanying financial statements. The amount of EHR incentive payments recognized are based on management's best estimate and those amounts are subject to change with such changes impacting the period in which they occur.

The Hospital recognized revenue of $10,610 and $240,473 for the years March 31, 2017 and 2016 related to EHR incentive payments. These incentive payments are included in other revenue in the accompanying financial statements.

Supplemental Hospital Offset Payment Program Act

The Supplemental Hospital Offset Payment Program Act (SHOPP), designated as House Bill 1381 (HB 1381), was passed during 2011 implementing a fee on hospitals to generate matching funds to the state of Oklahoma from federal sources. The program is designed to assess Oklahoma hospitals, unless exempt, a supplemental hospital offset payment program fee. The collected fees will be placed in pools and then allocated to hospitals as directed by legislation. The Oklahoma Health Care Authority (OHCA) does not guarantee that allocations will or equal or exceed the amount of the supplemental hospital offset payment program fee paid by the hospital.

The Hospital records payments to other expenses and receipts as net patient service revenue. Future changes in law or regulation at the federal or state level can adversely affect or eliminate SHOPP.

The Hospital made SHOPP payments totaling $364,875, for the year ended March 31, 2017. In return, the Hospital received $906,334. The Hospital made SHOPP payments totaling $354,842, for the year ended March 31, 2016. In return, the Hospital received $912,861.

Reclassifications

Reclassifications have been made to the March 31, 2016 financial information to make it conform to the current year presentation. The reclassifications had no effect on previously reported operating results or changes in net position.

Note 2 - Net Patient Service Revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare: Inpatient acute care and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per visit. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Outpatient services are paid based on a prospectively determined amount per procedure. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor (MAC). The Hospital's Medicare cost reports have been audited by the MAC through March 31, 2015.

Medicaid: The Hospital is reimbursed for services rendered to patients covered by the State Medicaid Program on a prospective basis at predetermined rates with no retroactive adjustment.
The Hospital has also entered into payment agreements with certain commercial insurance carriers and other 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.

Concentration of gross charges by major payor accounted for the following percentages of the Hospital's patient service revenues for the years ended March 31, 2017 and 2016:

	2017	2016
Medicare	49%	48%
Medicaid	19%	20%
Blue Cross	9%	8%
Commercial insurance	13%	14%
Other third-party payors and patients	10%	10%
	100%	100%

Laws and regulations governing the Medicare, Medicaid, and other programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The net patient service revenue for the years ended March 31, 2017 and 2016 decreased approximately $110,000 and increased approximately $297,000 due to removal of allowances previously estimated that are no longer necessary as a result of final cost report settlements, adjustments to previously estimated settlements and cost report periods that are no longer likely subject to audits, reviews, and investigations.

The Centers for Medicare and Medicaid Services (CMS) has implemented a Recovery Audit Contractor (RAC) program under which claims are reviewed by contractors for validity, accuracy, and proper documentation. A demonstration project completed in several other states resulted in the identification of potential overpayments, some being significant. If selected for audit, the potential exists that the Hospital may incur a liability for a claims overpayment at a future date. The Hospital is unable to determine if it will be audited and, if so, the extent of the liability of overpayments, if any. As the outcome of such potential reviews is unknown and cannot be reasonably estimated, it is the Hospital’s policy to adjust revenue for deductions from overpayment amounts or additions from underpayment amounts determined under the RAC audits at the time a change in reimbursement is agreed upon between the Hospital and CMS.

Note 3 - Deposits and Investments

The carrying amounts of deposits and investments as of March 31, 2017 and 2016 are as follows:

	2017	2016
Cash deposits in banks	$ 18,056	$ 507,822
Certificates of deposit	-	975,339
	$ 18,056	$ 1,483,161

Deposits and investments are reported in the following statement of net position captions:

	2017	2016
Cash	$ 18,056	$ 507,822
Certificates of deposit	-	975,339
	$ 18,056	$ 1,483,161

Deposits – Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank or investment company failure, the Hospital’s deposits may not be returned to it. State statute requires that any deposits in excess of federal depository or other insured amounts be collateralized by U.S. Government securities in the name of the Hospital. Statutes also require that the market value of the collateral be at least 100% of the excess deposits. The Hospital’s deposit policy does not further restrict bank deposits or limit investment deposits.

The Hospital’s deposits in banks at March 31, 2017 and 2016 were entirely covered by federal depository insurance or by collateral held by the Hospital’s custodial bank in the Hospital’s name.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The Hospital’s investment policy does not provide specific maturity limits in certificates of deposits to manage exposure to fair value losses arising from changing interest rates.

Concentration of Credit Risk

The Hospital does not have a formally adopted investment policy for managing concentration of credit risk.

Investment Income

Investment income, primarily interest income, for the years ended March 31, 2017 and 2016 was $3,728 and $7,994.

Note 4 - Capital Assets

Capital assets additions, retirements, transfers and balances for the year ended March 31, 2017 are as follows:

	Balance March 31, 2016	Additions	Transfers and Retirements	Balance March 31, 2017
Capital assets not being depreciated				
Land	$ 193,633	$ -	$ -	$ 193,633
Construction in progress	6,500	-	(6,500)	-
Total capital assets not being depreciated	$ 200,133	$ -	$ (6,500)	$ 193,633
Capital assets being depreciated				
Land improvements	$ 34,488	$ -	$ -	$ 34,488
Building and improvements	3,374,383	-	(56,500)	3,317,883
Major moveable and fixed equipment	8,976,411	140,234	6,500	9,123,145
Total capital assets being depreciated	12,385,282	$ 140,234	$ (50,000)	12,475,516
Less accumulated depreciation for				
Land improvements	13,972	$ 3,438	$ -	17,410
Building and improvements	2,522,990	56,346	(38,370)	2,540,966
Major moveable and fixed equipment	7,012,734	476,842	-	7,489,576
Total accumulated depreciation	9,549,696	$ 536,626	$ (38,370)	10,047,952
Net capital assets being depreciated	$ 2,835,586			$ 2,427,564
Capital assets, net	$ 3,035,719			$ 2,621,197

Capital assets additions, retirements, transfers and balances for the year ended March 31, 2016 are as follows:

	Balance March 31, 2015	Additions	Transfers and Retirements	Balance March 31, 2016
Capital assets not being depreciated				
Land	$ 193,633	$ -	$ -	$ 193,633
Construction in progress	5,550	101,962	(101,012)	6,500
Total capital assets not being depreciated	$ 199,183	$ 101,962	$ (101,012)	$ 200,133
Capital assets being depreciated				
Land improvements	$ 12,443	$ -	$ 22,045	$ 34,488
Building and improvements	3,664,913	24,327	(314,857)	3,374,383
Major moveable and fixed equipment	8,486,263	405,204	84,944	8,976,411
Total capital assets being depreciated	12,163,619	$ 429,531	$ (207,868)	12,385,282
Less accumulated depreciation for				
Land improvements	13,066	$ 3,391	$ (2,485)	13,972
Building and improvements	2,585,218	53,594	(115,822)	2,522,990
Major moveable and fixed equipment	6,552,893	517,719	(57,878)	7,012,734
Total accumulated depreciation	9,151,177	$ 574,704	$ (176,185)	9,549,696
Net capital assets being depreciated	$ 3,012,442			$ 2,835,586
Capital assets, net	$ 3,211,625			$ 3,035,719

Note 5 - Lease Obligations

The Hospital leases certain equipment under noncancelable long-term lease agreements. Certain leases have been recorded as capital leases and others as operating leases. Total lease expense for the years ended March 31, 2017 and 2016 for all operating leases was approximately $79,000 and $101,000. The capitalized leased assets consist of:

	2017	2016
Major movable equipment	$ 196,382	$ 196,382
Less accumulated amortization	(58,915)	(19,638)
	$ 137,467	$ 176,744

Minimum future lease payments for capital and operating leases are as follows:

Year Ending March 31,	Capital Leases	Operating Leases
2018	$ 42,492	$ 11,593
2019	42,492	3,853
2020	42,492	1,956
2021	21,246	-
Total minimum lease payments	148,722	$ 17,402
Less interest	(8,327)	
Present value of minimum lease payments - Note 6	$ 140,395	

Note 6 - Notes Payable and Long-Term Debt

A schedule of changes in the Hospital's notes payable for March 31, 2017 and 2016 is as follows:

	Balance March 31, 2016	Additions	Payments	Balance March 31, 2017
Notes payable:				
Line of credit	$ 1,298,427	$ 247,629	$ (1,546,056)	$ -

	Balance March 31, 2015	Additions	Payments	Balance March 31, 2016
Notes payable:				
Line of credit	$1,225,337	$11,987,610	$ (11,914,520)	$ 1,298,427

During 2017, the Hospital's line of credit was refinanced with note payable (2) listed below.

A schedule of changes in the Hospital's long-term debt for March 31, 2017 and 2016 is as follows:

	Balance March 31, 2016	Additions	Payments	Balance March 31, 2017	Due Within One Year
Note payable (1)	$ 900,000	$ -	$ (900,000)	$ -	$ -
Note payable (2)	-	1,800,000	(32,174)	1,767,826	86,936
Capital lease (3)	177,665	-	(37,270)	140,395	38,499
	$ 1,077,665	$ 1,800,000	$ (969,444)	$ 1,908,221	$ 125,435

	Balance March 31, 2015	Additions	Payments	Balance March 31, 2016	Due Within One Year
Note payable (1)	$900,000	$ -	$ -	$900,000	$ -
Capital lease (3)	177,665	196,382	(18,717)	355,330	37,270
	$ 1,077,665	$ 196,382	$ (18,717)	$ 1,255,330	$ 37,270

The terms and due dates of the Hospital's long-term debt at March 31, 2017 and 2016 are as follows:

1. Promissory note with an interest rate of 1.65%, due annually with the principal balance to be paid in a single payment on July 29, 2017. The note was paid in full during 2017.
2. Note payable to bank with a variable interest rate (4.75% as of March 31, 2017), due in monthly installments of $14,085 including interest, due October 2031, secured by assets of the Authority.
3. Capital lease with imputed interest rate of 3.25%, due in monthly installments of $3,541, collateralized by associated equipment, due September 2020.

Future payments of principal and interest on the long-term debt obligations are as follows:

	Notes Payable		Capital Lease Obligations	
Year Ending March 31,	Principal	Interest	Principal	Interest
2018	$ 86,936	$ 82,084	$ 38,499	$ 3,993
2019	91,157	77,863	39,769	2,723
2020	95,582	73,438	41,081	1,411
2021	100,223	68,798	21,046	200
2022	105,088	63,932	-	-
2023-2027	607,105	237,995	-	-
2028-2032	681,735	76,509	-	-
Total	$ 1,767,826	$ 680,619	$ 140,395	$ 8,327

Note 7 - Pension Plan

The Hospital has 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 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 Hospital's Board of Trustees. Contributions by the Hospital to the plan are subject to the Board of Trustees approval annually. The Hospital did not make any contributions to the plan in 2017, 2016 or 2015.

Note 8 - Concentration of Credit Risk

The Hospital grants credit without collateral to its patients, many of whom are insured under third-party payor agreements. The mix of receivables from third-party payors and patients at March 31, 2017 and 2016 was as follows:

	2017	2016
Medicare	33%	22%
Medicaid	5%	5%
Blue Cross	6%	4%
Other commercial insurance	15%	11%
Other third-party payors and patients	41%	58%
	100%	100%

Note 9 - Contingencies

Risk Management

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

Malpractice Insurance

The Hospital has malpractice insurance coverage to provide protection for professional liability losses on a claims-made basis subject to a limit of $1,000,000 per claim and an annual aggregate limit of $3,000,000. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term, but reported subsequently, would be uninsured.

Litigations, Claims, and Disputes

The Hospital is subject to the usual contingencies in the normal course of operations relating to the performance of its tasks under its various programs. In the opinion of management, the ultimate settlement of any litigation, claims, and disputes in process will not be material to the financial position, operations, or cash flows of the Hospital.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Federal government activity has increased with respect to investigations and allegations concerning possible violations by health care providers of regulations, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenues from patient services.

Note 10 - Condensed Combining Information

The following summarizes combining information for the Hospital and Physician Group, which has been presented as a blended component unit, as of and for the year ended March 31, 2017.

Statement of net position as of March 31, 2017:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
Assets				
Current assets	$ 2,387,191	$ 49,727	$ (442,963)	$ 1,993,955
Capital assets	2,499,505	121,692	-	2,621,197
Other non current assets	7,330	-	-	7,330
Total assets	$ 4,894,026	$ 171,419	$ (442,963)	$ 4,622,482
Liabilities and Net Position				
Current liabilities	$ 2,156,395	$ 442,963	$ (442,963)	$ 2,156,395
Long term liabilities	1,782,787	-	-	1,782,787
Total liabilities	3,939,182	442,963	(442,963)	3,939,182
Net Position				
Net investment in capital assets	2,359,110	121,692	-	2,480,802
Unrestricted net position	(1,404,266)	(393,236)	-	(1,797,502)
Total net position	954,844	(271,544)	-	683,300
Total liabilities and net position	$ 4,894,026	$ 171,419	$ (442,963)	$ 4,622,482

Operating results and changes in net position for the year ended March 31, 2017:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
Operating Revenues				
Net patient service revenue	$ 10,056,228	$ 482,337	$ -	$ 10,538,565
Other operating revenue	107,497	-	(21,600)	85,897
Total operating revenue	10,163,725	482,337	(21,600)	10,624,462
Operating Expenses				
Depreciation	525,621	11,005	-	536,626
Other operating expenses	12,226,344	553,651	(21,600)	12,758,395
Total operating expenses	12,751,965	564,656	(21,600)	13,295,021
Operating Loss	(2,588,240)	(82,319)	-	(2,670,559)
Nonoperating Revenue (Expense)				
Interest income	3,728	-	-	3,728
Noncapital appropriation	673,549	-	-	673,549
Interest expense	(112,221)	-	-	(112,221)
Noncapital gifts	16,004	-	-	16,004
Loss on disposal of equipment	(12,127)	-	-	(12,127)
Total non operating revenue (expense)	568,933	-	-	568,933
Change in Net Position	(2,019,307)	(82,319)	-	(2,101,626)
Net Position Beginning of Year	2,974,151	(189,225)	-	2,784,926
Net Position End of Year	$ 954,844	$ (271,544)	$ -	$ 683,300

Cash flows for the year ended March 31, 2017:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Total
Net Cash used for Operating Activities	$ (1,445,270)	$ (1,574)	$ (1,446,844)
Net Cash from Noncapital Financing Activities	154,734	-	154,734
Net Cash used for Capital and related Financing Activities	(176,723)	-	(176,723)
Net Cash from Investing Activities	979,067	-	979,067
Net Change in Cash	(488,192)	(1,574)	(489,766)
Cash, Beginning of Year	506,218	1,604	507,822
Cash, End of Year	$ 18,026	$ 30	$ 18,056

The following summarizes combining information for the Hospital and Physician Group, which has been presented as a blended component unit, as of and for the year ended March 31, 2016.

Statement of net position as of March 31, 2016:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
Assets				
Current assets	$ 3,519,008	$ 101,958	$ (423,882)	$ 3,197,084
Capital assets	2,903,020	132,699	-	3,035,719
Limited to use	975,339	-	-	975,339
Other non current assets	110,916	-	-	110,916
Total assets	$ 7,508,283	$ 234,657	$ (423,882)	$ 7,319,058
Liabilities and Net Position				
Current liabilities	$ 3,493,737	$ 423,882	$ (423,882)	$ 3,493,737
Long term liabilities	1,040,395	-	-	1,040,395
Total liabilities	4,534,132	423,882	(423,882)	4,534,132
Net Position				
Net investment in capital assets	2,725,355	-	-	2,725,355
Unrestricted net position	248,796	(189,225)	-	59,571
Total net position	2,974,151	(189,225)	-	2,784,926
Total liabilities and net position	$ 7,508,283	$ 234,657	$ (423,882)	$ 7,319,058

Operating results and changes in net position for the year ended March 31, 2016:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
Operating Revenues				
Net patient service revenue	$ 12,826,575	$ 529,548	$ -	$ 13,356,123
Other operating revenue	293,879	-	(21,600)	272,279
Total operating revenue	13,120,454	529,548	(21,600)	13,628,402
Operating Expenses				
Depreciation	560,639	14,065	-	574,704
Other operating expenses	13,686,906	596,053	(21,600)	14,261,359
Total operating expenses	14,247,545	610,118	(21,600)	14,836,063
Operating Loss	(1,127,091)	(80,570)	-	(1,207,661)
Nonoperating Revenue (Expense)				
Interest income	7,994	-	-	7,994
Noncapital appropriation	618,431	-	-	618,431
Interest expense	(93,361)	-	-	(93,361)
Noncapital gifts	14,622	-	-	14,622
Gain on disposal of equipment	147,648	-	-	147,648
Total non operating revenue (expense)	695,334	-	-	695,334
Capital appropriations	70,273	-	-	70,273
Change in Net Position	(361,484)	(80,570)	-	(442,054)
Net Position Beginning of Year	3,335,635	(108,655)	-	3,226,980
Net Position End of Year	$ 2,974,151	$ (189,225)	$ -	$ 2,784,926

Cash flows for the year ended March 31, 2016:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Total
Net Cash from Operating Activities	$ (578,452)	$ (76)	$ (578,528)
Net Cash from Noncapital Financing Activities	556,361	-	556,361
Net Cash from Capital and related Financing Activities	49,751	-	49,751
Net Cash from Investing Activities	1,664	-	1,664
Net Change in Cash	29,324	(76)	29,248
Cash, Beginning of Year	476,894	1,680	478,574
Cash, End of Year	$ 506,218	$ 1,604	$ 507,822

Note 11 - **Recurring Losses and Management Plans**

The Hospital has incurred operating losses during the years ended March 31, 2017 and 2016. For the years ended March 31, 2017 and 2016, the Hospital experienced a decrease in net position of $2,101,626 and $442,054. The Hospital's board signed a management agreement with a health system to manage the operations of the Hospital effective June 1, 2017. The Hospital is to pay $15,000 per month for the management services and 5% of receipts from patient billing for billing and collection services. The Authority will pay the health system an incentive based on net profits above $250,000. In addition, the Hospital issued a variable interest rate note payable in the amount of $4,000,000 to be used for operations and pay off the variable interest rate note payable in Note 6 during December 2017. The Hospital is to pay 12 payments of interest only starting on January 2018 followed by 228 payments of principal and interest. Secured with assets of the Hospital.

Note 12 - **Subsequent Events**

The Hospital has evaluated subsequent events through June 19, 2018 the date which the financial statements were available to be issued.

On November 1, 2017, the Hospital entered in to an agreement to lease mammography equipment. The Hospital will pay $7,912 a month for seven years.

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

The Board of Trustees
Sequoyah County-City of Sallisaw Hospital Authority
d/b/a Sequoyah Memorial Hospital
Sallisaw, 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 Sequoyah Memorial Hospital Authority d/b/a Sequoyah Memorial Hospital (Hospital) as of and for the year ended March 31, 2017, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements, and have issued our report thereon dated June 19, 2018.

Internal Control over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings, we identified certain deficiencies in internal control that we consider to be material weaknesses, and other deficiencies we consider to be significant deficiencies.

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. We consider the deficiencies described in the accompanying Schedule of Findings to be material weaknesses: 2017-A through 2017-E.

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. We consider the following deficiencies in the accompanying Schedule of Findings to be a significant deficiencies: 2017-F through 2017-I.

Compliance and Other Matters
As part of obtaining reasonable assurance about whether the Hospital's financial statements are free from 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* which is described in the accompanying Schedule of Findings and Responses as item 2017-001.

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

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

Eide Bailly LLP

Oklahoma City, Oklahoma
June 19, 2018

Material Weaknesses In Internal Control Over Financial Reporting:

2017-A Preparation of Financial Statements

Criteria: A properly designed system of internal control over financial reporting includes the preparation of an entity's financial statements and accompanying notes to the financial statements by internal personnel of the entity. Management is responsible for establishing and maintaining internal control over financial reporting and procedures related to the fair presentation of the financial statements in accordance with U.S. generally accepted accounting principles (GAAP).

Condition: The Hospital does not have the internal control system over financial reporting designed to provide for the preparation of the financial statements, including the accompanying footnotes as required by generally accepted accounting standards, on a periodic or annual basis. This circumstance is not unusual in an organization of your size. It is the responsibility of management and those charged with governance to make the decisions whether to accept the degree of risk associated with this condition because of the cost or other considerations.

Cause: Misstatements to the internal financial statements were not prevented or detected on a timely basis in the normal course of business. Therefore, there were several significant adjusting journal entries at year end proposed during the audit process.

Effect: Failure to timely prepare interim financial statements represents a weakness in internal control over financial reporting. Also, the year-end financial report is prepared by the auditors, a party outside of the Hospital. The outside party does not have constant contact with ongoing financial transactions that the internal staff has. Furthermore, it is possible that new standards may not be adopted and applied timely to the interim financial reporting. It is the responsibility of Hospital management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

Auditor's Recommendation: It is recommended the Hospital implement a system that allows the preparation of financial statements in accordance with GAAP.

Views of Responsible Officials: Given the size of the Hospital, we do not think it would be cost-effective to fully cure this technical deficiency at this time. In addition, given the complex and constantly changing nature of financial reporting requirements, we believe that better results can be achieved by continuing to rely on the expertise of our outside auditors regarding these matters.

2017-B Account Reconciliation

Criteria: Reviewing and reconciling accounts to the general ledger is a necessary step in the Hospital's internal control process.

Condition: During the course of our engagement, it was identified that certain accounts are not reconciled from a sub-ledger or other detail or support to the general ledger on a timely basis.

Effect: Misstatements are not identified and corrected in a timely manner.

Cause: Areas with differences that resulted in significant adjustments to the financial statements included capital assets, accounts payables and accrued liabilities.

Auditor's Recommendation: We recommend management prepare account reconciliations on a timely basis as well as a review of these reconciliations, in order to identify potential misstatements and reconciling items. Significant accounts should be reconciled from a sub-ledger or other detail or support to the general ledger at least on a monthly basis. Any variances should also be reconciled on a periodic basis to ensure that these balances also remain applicable.

Views of Responsible Officials: Management will develop a process to reconcile accounts on a regular basis and investigate any variances.

2017-C Calculation of Bad Debt and Contractual Allowances

Criteria: Accountings standards require an entity to estimate an allowance on the collectability of receivables. The allowance should be based on historical data and current reimbursement rates.

Condition: The allowance calculations were not properly estimated during the year.

Cause: Historical collections are not reviewed and considered in determining the potential impact on contractual adjustments or bad debt write-offs.

Effect: Interim financial statements may not be properly stated. A material audit adjustment was made to the allowance accounts.

Auditor's Recommendation: We recommend that management fully implement the developed methodology for estimating collections and adjustments. The allowance accounts should be reviewed each month as well for reasonableness in relation to the accounts receivable and revenue.

Views of Responsible Officials: Management is in the implementation stage of developing a model to properly calculate the bad debt and contractual allowances for the hospital and physician practice. The model is in place for the physician practice and is being tested and revised for the hospital.

2017-D Restricted Donations

Criteria: When restricted donations are received, they should only be used for the specific purpose. There may be serious implications if restricted donations are not used for the specific purpose, some of which may include violations of laws and regulations that can carry stiff fines and/or penalties.

Condition: During the year, the Hospital received a donation to be used on the purchase of a mammography unit.

Cause: The Hospital used the donation for operations instead of purchasing the required equipment.

Effect: The Hospital was not in compliance with the restricted donation. The donor could request the funds be returned.

Auditor's Recommendation: We recommend that the Hospital use restricted funds on the intended purpose of the donation.

Views of Responsible Officials: We will implement a policy to review and verify the proper use of restricted donations.

2017-E Charity Care

Criteria: The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates.

Condition: During the audit, we noted the Hospital did not provide charity care throughout the year.

Cause: the Hospital did not work with patients to complete the necessary forms to quality for the Hospital's charity care.

Effect: Patients that would qualify for charity care will then be sent to collection and amounts will be written off as bad debt.

Auditor's Recommendation: We recommend that the Hospital work with patients to complete the necessary forms and apply for charity care.

Views of Responsible Officials: We will implement policies and procedures to assist patients with applying for charity care.

Significant Deficiencies In Internal Control Over Financial Reporting:

2017-F Segregation of Duties

Criteria: A properly designed system of internal control segregates the initiation, record keeping, and authorization of transactions.

Condition: During the course of our engagement, we noted that the Hospital has limited staff completing incompatible accounting functions due to the size of the Hospital. There were no review of the journal entries or monthly reconciliations for a portion of the year.

Cause: The Hospital's size and budget constraints limit the number of personnel and does not facilitate the segregation of duties necessary to adequately separate procedures.

Effect: Inadequate segregation of duties could adversely affect the organizations ability to detect and correct unintentional or intentional misstatements in a timely manner by employees in the normal course of performing their assigned functions.

Auditor's Recommendation: It is the responsibility of management and those charged with governance to make the decisions whether to accept the degree of risk associated with this condition because of cost or other considerations. In addition, we recommend that the functions be reviewed to determine if additional segregation is feasible to improve efficiency and effectiveness of the financial management of the organization.

Views of Responsible Officials: Management agrees with the finding and has reviewed the operating procedures of the Hospital. Due to the limited number of office employees, management will continue to monitor the Hospital's operations and procedures. Furthermore, we will continually review the assignment of duties to obtain the maximum internal control possible under the circumstances.

2017-G Cost Report Estimate

Criteria: Accountings standards require an entity to estimate the Medicare cost report settlement in order to fairly state the financial position monthly and as of year-end.

Condition: During the current year, the Hospital did not estimate the financial effect of the Medicare cost report settlement for the current year correctly. The Hospital should record adjustments for current year activity to the estimated third party payor settlement account.

Effect: This resulted in an adjusting journal entry to properly state the current year settlement.

Cause: The current year cost report settlement was not properly estimated at year end which resulted in a material journal entry to the financial statements.

Auditor's Recommendation: It is recommended the Hospital implement a system that provides adequate controls over estimating cost report settlements.

Views of Responsible Officials: Management will obtain a cost report estimate model to assist with monthly account reconciliation.

2017-H Review of Compensated Absences

Criteria: The Hospital implemented policies to ensure proper treatment of employees' paid time off. The policy does not allow employees to use more than what the employee has earned.

Condition: During the course of our engagement, we noted that several employees had negative paid time off balances.

Cause: The Hospital allowed employees to have negative paid time off balances which is not allowed per the Hospital's policy.

Effect: The Hospital was not in compliance with their own policies.

Auditor's Recommendation: We recommend that employees' paid time off balance be reviewed each pay period to adhere to the Hospital's policies.

Views of Responsible Officials: We will review paid time off balances each pay period to insure employees do not use amounts in excess of their balance.

2017-I Journal Entry Support

Criteria: Journal entries should always be supported by appropriate documentation where possible. Good documentation serves as an accounting record and facilitates future follow-up as well as additional insight for other users.

Condition: During the audit, it was noted that journal entries did not have supporting documentation.

Cause: The Hospital did not have documentation to support journal entries posted to the general ledger.

Effect: There could be failure to detect fraud or material misstatement.

Auditor's Recommendation: We recommend that documentation be kept for journal entries posted to the general ledger.

Views of Responsible Officials: We will maintain all documentation to support journal entries posted to the general ledger.

Material Weaknesses In Internal Control Over Compliance:

2017-001 Payroll Taxes

Criteria: An employer is required to withhold federal and state income and payroll taxes from its employees' wages and pay them to the taxing authority. Withheld taxes are called trust fund taxes because the employer holds the employee's money (federal and state income taxes and the employee portion Federal Insurance Contributions Act taxes) in trust until federal and state deposits of the amounts are made.

Condition: During the course of our engagement, we noted that the Hospital did not make timely federal income and payroll tax deposits during the year.

Cause: Failure to monitor and pay trust taxes timely.

Effect: Potential violation of federal and state laws, which could result in significant penalties and interest.

Auditor's Recommendation: It is recommended that the Hospital establish policies and procedures to ensure trust tax deposits are made in a timely manner.

Views of Responsible Officials: A payment and monitoring plan has been arranged with the taxing authorities to maintain current payroll tax deposits. The hospital is working to secure short term financing for the purpose of providing additional funds to cover cash short falls and to help with delays in cash flow timing issues.