



Management's Discussion and Analysis  
And Financial Statements  
March 31, 2019 and 2018

**Sequoyah County-City of Sallisaw  
Hospital Authority d/b/a Northeastern  
Health System Sequoyah**

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Table of Contents  
March 31, 2019 and 2018

---

Independent Auditor’s Report .....	1
Management’s Discussion and Analysis .....	3
Financial Statements	
Statements of Net Position .....	8
Statements of Revenues, Expenses and Changes in Net Position.....	10
Statements of Cash Flows .....	11
Notes to Financial Statements .....	13
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 <i>Government Auditing Standards</i> .....	31
Schedule of Findings and Responses .....	33



## Independent Auditor's Report

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

### Report on the Financial Statements

We have audited the accompanying statements of net position of Sequoyah County-City of Sallisaw Hospital Authority d/b/a Northeastern Health System Sequoyah (Hospital) as of March 31, 2019 and 2018, 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.

What inspires you, inspires us. | [eidebailly.com](http://eidebailly.com)

## **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 Northeastern Health System Sequoyah as of March 31, 2019 and 2018, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **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 7 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 inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our 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 a report dated May 8, 2020 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, grant agreements, and other matters. The purpose of that report is solely 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 effectiveness of the Hospital's internal control over financial reporting or on compliance. That reports 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.



Oklahoma City, Oklahoma  
May 8, 2020

## Introduction

This discussion and analysis of the financial performance of Sequoyah County-City of Sallisaw Hospital Authority d/b/a Northeastern Health System Sequoyah (Hospital) provides an overall review of the Hospital's financial activities and balances as of and for the years ended March 31, 2019, 2018, and 2017. 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 2019 by \$34,552 or 1% and increased in 2018 by \$593,788 or 30%.
- Total liabilities increased in 2019 by \$1,242,015 or 17% and increased in 2018 by \$3,216,074 or 82%.
- The Hospital's net position decreased in 2019 by \$1,749,436 or 91% and decreased in 2018 by \$2,608,114 or 382%.
- The Hospital reported an operating loss in 2019 of \$2,161,544 and an operating loss in 2018 of \$3,308,853. During 2019, operating loss decreased by \$1,147,309 or 35% and increased by \$638,294 or 24% in 2018.
- Net patient service revenue decreased in 2019 by \$792,502 or 8% and decreased by \$676,778 or 6% in 2018.
- Other operating revenue increased by \$107,598 or 473% in 2019 and decreased by \$84,767 or 79% in 2018.
- Operating expenses decreased in 2019 by \$1,832,222 or 14% and decreased \$123,251 or 1% in 2018.

## 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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah  
Management's Discussion and Analysis

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 \$1,749,436 or 91% in 2019 and decreased by \$2,608,114 or 382% in 2018 as shown below.

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

	2019	2018	2017
<b>Assets</b>			
Current assets	\$ 2,553,191	\$ 2,587,743	\$ 1,993,955
Capital assets, net	2,105,000	2,545,369	2,621,197
Noncurrent assets	64,830	97,330	7,330
	<u>\$ 4,723,021</u>	<u>\$ 5,230,442</u>	<u>\$ 4,622,482</u>
<b>Liabilities</b>			
Total current liabilities	\$ 4,084,195	\$ 2,725,554	\$ 2,156,395
Long term debt	4,313,076	4,429,702	1,782,787
	<u>8,397,271</u>	<u>7,155,256</u>	<u>3,939,182</u>
<b>Net Position</b>			
Net investment in capital assets	1,726,392	2,079,111	2,480,802
Unrestricted	(5,400,642)	(4,003,925)	(1,797,502)
	<u>(3,674,250)</u>	<u>(1,924,814)</u>	<u>683,300</u>
	<u>\$ 4,723,021</u>	<u>\$ 5,230,442</u>	<u>\$ 4,622,482</u>

Sequoiah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoiah  
Management's Discussion and Analysis

**Assets, Liabilities, and Net Position**

The Hospital's total assets decreased \$507,421 or 10% in 2018 and increased \$607,960 or 13% in 2018.

- Current assets decreased \$34,551 or 1% in 2019 compared to the increase of \$593,789 or 30% in 2018.
- Capital assets decreased by \$440,369 or 17% in 2019 due to annual depreciation. Capital assets decreased \$75,829 or 3% in 2018, depreciation expense of \$484,840 was offset by equipment purchases of \$409,012.

The Hospital's total liabilities increased \$1,242,015 or 17% in 2018 and increased \$3,216,074 or 82% in 2018.

- Accounts payable and accrued expenses increased \$1,332,557 or 52% in 2019 and increased \$644,082 or 34% in 2018. The increase in payables and accruals attributable to process changes in billings and collections and timing issues.

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

	<u>2019</u>	<u>2018</u>	<u>2017</u>
Operating Revenues			
Net patient service revenue	\$ 9,047,685	\$ 9,840,187	\$ 10,516,965
Other operating revenue	130,319	22,730	107,497
Total operating revenues	<u>9,178,004</u>	<u>9,862,917</u>	<u>10,624,462</u>
Operating Expenses			
Salaries and wages	-	4,095,836	5,967,169
Employee benefits	-	893,905	891,205
Contract salary and benefits	6,105,200	2,002,190	-
Purchased services and professional fees	2,360,735	3,004,282	2,749,199
Supplies and other	2,433,244	2,690,717	3,150,822
Depreciation	440,369	484,840	536,626
Total operating expenses	<u>11,339,548</u>	<u>13,171,770</u>	<u>13,295,021</u>
Operating Loss	<u>(2,161,544)</u>	<u>(3,308,853)</u>	<u>(2,670,559)</u>
Nonoperating Revenues (Expenses)			
Interest income	178	15	3,728
Noncapital appropriations	702,714	736,695	673,549
Interest expense	(292,159)	(173,171)	(112,221)
Noncapital gifts	1,375	-	16,004
Gain on disposal of capital assets	-	12,200	(12,127)
Net nonoperating revenues	<u>412,108</u>	<u>575,739</u>	<u>568,933</u>
Expenses in Excess of Revenues Before Capital Contributions	(1,749,436)	(2,733,114)	(2,101,626)
Capital Contributions	-	125,000	-
Change in Net Position	<u>\$ (1,749,436)</u>	<u>\$ (2,608,114)</u>	<u>\$ (2,101,626)</u>

### **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 2019 decreased by \$1,147,309 or 35% as compared to the increase of \$638,294 or 24% in 2018. The primary components of the operating loss are:

- Net patient service revenue decreased \$792,502 or 8% in 2019 compared to a decrease of \$676,778 or 6% in 2018. The decreases in 2019 and 2018 is attributed to a decrease in services provided by the Hospital.
- Salaries, wages, benefits, contract salary and benefits expenses decreased \$886,731 or 13% in 2019 compared to an increase in 2018 of \$133,557 or 2%.
- Purchased services and professional fees decreased in 2019 by \$643,547 or 21% compared to an increase of \$255,083 or 9% in 2018.

### **Non-operating Revenues and Expenses**

Non-operating revenues and expenses consist primarily of tax appropriations and interest expense. Tax appropriations decreased \$33,981 or 5% in 2019 and increased \$63,146 or 9% in 2018. Interest expense increased \$118,988 or 69% in 2019 as compared to the increase of \$60,950 or 54% in 2018.

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

Changes in the Hospital's cash flows are consistent with changes in operating income and nonoperating revenues and expenses discussed earlier. The principal changes in the Hospital's nonoperating cash flows were:

- Net cash used for operating activities decreased in 2019 by \$2,103,017 or 85% and increased in 2018 by \$1,040,509 or 72%.
- Net cash from noncapital financing activities decreased in 2019 by \$2,314,197 or 85% and increased in 2018 by \$2,583,455 or 1670%.
- Net cash used for capital and capital related financing activities increased in 2019 by \$25,632 or 34% and decreased in 2018 by \$101,781 or 58%.
- Net cash from investing activities increased in 2019 by \$163 or 1,087% and decreased in 2018 by \$979,052 or 100%.

### **Capital Assets**

The Hospital had \$2,105,000 invested in capital assets at the end of 2019 and \$2,545,369 at the end of 2018, net of accumulated depreciation, as detailed in Note 4 to the financial statements. The Hospital did not acquire any new capital assets in 2019. The Hospital acquired new capital assets in 2018 costing \$409,012.



### **Debt**

The Hospital had total debt of \$4,470,672 at the end of 2019. The Hospital did not incur additional debt in 2019, as detailed in Note 6 to the financial statements. The Hospital had total debt of \$4,584,214 at the end of 2018. The Hospital incurred additional debt of \$4,484,361 for notes payable in 2018, 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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah  
Statements of Net Position  
March 31, 2019 and 2018

	2019	2018
Assets		
Current Assets		
Cash	\$ 133,225	\$ 193,965
Receivables		
Patient, net of estimated uncollectibles		
of \$5,414,000 in 2019 and \$8,749,000 in 2018	1,834,148	1,865,098
Tax appropriation	122,078	115,627
Supplies	370,082	327,407
Prepaid expenses and other current assets	93,658	85,646
Total current assets	2,553,191	2,587,743
Capital Assets		
Capital assets not being depreciated	193,633	193,633
Capital assets being depreciated, net	1,911,367	2,351,736
Total capital assets	2,105,000	2,545,369
Other Assets		
Cash value of life insurance	7,330	7,330
Prepaid expenses, net of current portion	57,500	90,000
Total other assets	64,830	97,330
Total assets	\$ 4,723,021	\$ 5,230,442

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah  
Statements of Net Position  
March 31, 2019 and 2018

	2019	2018
Liabilities and Net Position		
Current Liabilities		
Current maturities of long-term debt	\$ 157,596	\$ 154,512
Accounts payable	3,880,508	2,529,179
Estimated third-party payor settlements	42,000	19,000
Accrued expenses	4,091	22,863
Total current liabilities	4,084,195	2,725,554
Long-Term Debt, Less Current Maturities	4,313,076	4,429,702
Total liabilities	8,397,271	7,155,256
Net Position (Deficit)		
Net investment in capital assets	1,726,392	2,079,111
Unrestricted	(5,400,642)	(4,003,925)
Total net position (deficit)	(3,674,250)	(1,924,814)
Total liabilities and net position	\$ 4,723,021	\$ 5,230,442

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah  
Statements of Revenues, Expenses and Changes in Net Position  
Years Ended March 31, 2019 and 2018

	2019	2018
Operating Revenue		
Net patient service revenue, net of provision for bad debts of \$4,578,447 in 2019 and \$5,770,517 in 2018	\$ 9,047,685	\$ 9,840,187
Other revenue	130,319	22,730
Total operating revenues	9,178,004	9,862,917
Operating Expenses		
Salaries and wages	-	4,095,836
Employee benefits	-	893,905
Contract salary and benefits	6,105,200	2,002,190
Purchased services and professional fees	2,360,735	3,004,282
Supplies and other	2,433,244	2,690,717
Depreciation	440,369	484,840
Total operating expenses	11,339,548	13,171,770
Operating Loss	(2,161,544)	(3,308,853)
Nonoperating Revenues (Expenses)		
Interest income	178	15
Tax appropriation	702,714	736,695
Interest expense	(292,159)	(173,171)
Noncapital grants and contributions	1,375	-
Gain on disposal of capital assets	-	12,200
Total nonoperating revenues (expenses)	412,108	575,739
Expenses in Excess of Revenues Before Capital Contributions	(1,749,436)	(2,733,114)
Capital Contributions	-	125,000
Change in Net Position	(1,749,436)	(2,608,114)
Net Position (Deficit), Beginning of Year	(1,924,814)	683,300
Net Position (Deficit), End of Year	\$ (3,674,250)	\$ (1,924,814)

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Statements of Cash Flows  
Years Ended March 31, 2019 and 2018

	2019	2018
Operating Activities		
Receipts from and on behalf of patients	\$ 9,101,635	\$ 9,334,892
Payments to suppliers and contractors	(3,460,837)	(4,493,281)
Payments to contract employees	(6,155,453)	(7,351,726)
Other receipts	130,319	22,762
Net Cash used for Operating Activities	(384,336)	(2,487,353)
Noncapital Related Financing Activities		
Tax appropriations	696,263	677,238
Proceeds from long-term debt	-	4,000,000
Principal payments on long-term debt	(25,892)	(1,769,871)
Interest paid	(247,754)	(169,178)
Noncapital grants and contributions	1,375	-
Net Cash from Noncapital Related Financing Activities	423,992	2,738,189
Capital and Related Financing Activities		
Principal payments on long-term debt	(87,650)	(38,498)
Interest paid	(12,924)	(3,993)
Purchase of property and equipment	-	(44,651)
Proceeds from the sale of equipment	-	12,200
Net Cash used for Capital and Related Financing Activities	(100,574)	(74,942)
Investing Activities		
Interest income	178	15
Net Change in Cash	(60,740)	175,909
Cash, Beginning of Year	193,965	18,056
Cash, End of Year	\$ 133,225	\$ 193,965

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah  
Statements of Cash Flows  
Years Ended March 31, 2019 and 2018

	2019	2018
Reconciliation of Operating Loss to Net Cash used for Operating Activities		
Operating Loss	\$ (2,161,544)	\$ (3,308,853)
Adjustments to reconcile operating loss to net cash used for operating activities		
Depreciation	440,369	484,840
Provision for bad debts	4,578,447	5,770,517
Changes in assets and liabilities		
Patient receivables	(4,547,497)	(6,171,812)
Other receivables	-	32
Supplies	(42,675)	60,574
Prepaid expenses and other	24,488	12,267
Accounts payable	1,351,329	1,128,877
Accrued expenses	(50,253)	(359,795)
Estimated third-party payor settlements	23,000	(104,000)
Net Cash used for Operating Activities	\$ (384,336)	\$ (2,487,353)
Supplemental Disclosure of Noncash Capital and Capital Related Financing Activities		
Equipment financed through capital lease arrangement	\$ -	\$ 364,361
Supplemental Disclosure of Noncash Noncapital Related Financing Activities		
Physician retention financed through debt agreement	\$ -	\$ 120,000

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

**Note 1 - Reporting Entity and Summary of Significant Accounting Policies**

The financial statements of Sequoyah County-City of Sallisaw Hospital Authority d/b/a Northeastern Health System Sequoyah (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. During 2018, the Hospital changed their trade name from Sequoyah Memorial Hospital to Northeastern Health System Sequoyah. Effective June 1, 2017 the Hospital signed a management service agreement with Tahlequah Hospital Authority (THA). The terms of the management service agreement are discussed in Note 11.

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, collectively 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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

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, 2019 and 2018.

*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, 2019 and 2018.

*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 year ended March 31, 2019 increased approximately \$18,000 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. The net patient service revenue for the year ended March 31, 2018 increased approximately \$73,000 as a result of increased payments compared to originally estimated amounts.



Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

**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.

**Tax Appropriations**

The Hospital benefits from a 0.5% sales tax assessment to be used for operations of the Hospital. The tax, approved by the Board of Commissioners of the City of Sallisaw, has no expiration date. The Hospital received approximately 7% and 7% of its financial support from city appropriations during the years ended March 31, 2019 and 2018.

**Supplies**

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

**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

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

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.

### **Physician Retention**

The Hospital signed an agreement to pay a physician \$120,000 over four years as part of their retention process. The amount will be amortized over a four-year period. At March 31, 2019 and 2018, the balance totaled \$87,500 and \$120,000.

### **Compensated Absences**

Effective January 2018, the Hospital transferred all employees to THA as part of the management service agreement. The Hospital has a payable recorded for compensated absences as they will reimburse THA when used. 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 statements 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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

### 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 \$353,000 and \$77,000 for the years ended September 30, 2019 and 2018. Total direct and indirect costs related to these foregone charges were approximately \$101,000 and \$25,000 at March 31, 2019 and 2018, 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 nonoperating revenues. Amounts restricted to capital acquisitions are reported after expenses in excess of revenues.

### 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, 2016.

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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

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, 2019 and 2018:

	2019	2018
Medicare	47%	48%
Medicaid	19%	19%
Blue Cross	8%	8%
Commercial insurance	15%	12%
Other third-party payors and patients	11%	13%
	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, 2019 did not change and increased approximately \$77,000 in 2018 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**

Cash consisted of cash deposits in banks as of March 31, 2019 and 2018.

**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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

The Hospital's deposits in banks at March 31, 2019 and 2018 were entirely covered by federal depository insurance or by collateral held by the Hospital's custodial bank in the Hospital's name.

**Note 4 - Capital Assets**

Capital assets additions, retirements, transfers and balances for the year ended March 31, 2019 are as follows:

	Balance March 31, 2018	Additions	Transfers and Retirements	Balance March 31, 2019
Capital assets not being depreciated				
Land	\$ 193,633	\$ -	\$ -	\$ 193,633
Capital assets being depreciated				
Land improvements	\$ 34,488	\$ -	\$ -	\$ 34,488
Building and improvements	3,362,534	-	-	3,362,534
Major moveable and fixed equipment	9,468,556	-	-	9,468,556
Total capital assets being depreciated	12,865,578	\$ -	\$ -	12,865,578
Less accumulated depreciation for				
Land improvements	20,766	\$ 2,458	\$ -	23,224
Building and improvements	2,577,272	60,370	-	2,637,642
Major moveable and fixed equipment	7,915,804	377,541	-	8,293,345
Total accumulated depreciation	10,513,842	\$ 440,369	\$ -	10,954,211
Net capital assets being depreciated	\$ 2,351,736			\$ 1,911,367
Capital assets, net	\$ 2,545,369			\$ 2,105,000

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

Capital assets additions, retirements, transfers and balances for the year ended March 31, 2018 are as follows:

	<u>Balance March 31, 2017</u>	<u>Additions</u>	<u>Transfers and Retirements</u>	<u>Balance March 31, 2018</u>
Capital assets not being depreciated				
Land	\$ 193,633	\$ -	\$ -	\$ 193,633
Capital assets being depreciated				
Land improvements	\$ 34,488	\$ -	\$ -	\$ 34,488
Building and improvements	3,317,883	44,651	-	3,362,534
Major moveable and fixed equipment	<u>9,123,145</u>	<u>364,361</u>	<u>(18,950)</u>	<u>9,468,556</u>
Total capital assets being depreciated	<u>12,475,516</u>	<u>\$ 409,012</u>	<u>\$ (18,950)</u>	<u>12,865,578</u>
Less accumulated depreciation for				
Land improvements	17,410	\$ 3,356	\$ -	20,766
Building and improvements	2,540,966	36,306	-	2,577,272
Major moveable and fixed equipment	<u>7,489,576</u>	<u>445,178</u>	<u>(18,950)</u>	<u>7,915,804</u>
Total accumulated depreciation	<u>10,047,952</u>	<u>\$ 484,840</u>	<u>\$ (18,950)</u>	<u>10,513,842</u>
Net capital assets being depreciated	<u>\$ 2,427,564</u>			<u>\$ 2,351,736</u>
Capital assets, net	<u>\$ 2,621,197</u>			<u>\$ 2,545,369</u>

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

**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, 2019 and 2018 for all operating leases was approximately \$92,000 and \$71,000. The capitalized leased assets consist of:

	2019	2018
Major movable equipment	\$ 560,743	\$ 560,743
Less accumulated amortization	(225,744)	(111,204)
	\$ 334,999	\$ 449,539

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

<u>Year Ending March 31,</u>	Capital Leases	Operating Leases
2020	\$ 111,925	\$ 39,638
2021	78,504	37,682
2022	57,256	37,682
2023	57,256	37,682
2024	57,256	37,682
2025	42,943	28,262
Total minimum lease payments	405,140	\$ 218,628
Less interest	(26,532)	
Present value of minimum lease payments - Note 6	\$ 378,608	

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

**Note 6 - Long-Term Debt**

A schedule of changes in the Hospital's long-term debt for March 31, 2019 and 2018 is as follows:

	Balance March 31, 2018	Additions	Payments	Balance March 31, 2019	Due Within One Year
Note payable (1)	\$ 4,000,000	\$ -	\$ -	\$ 4,000,000	\$ 26,190
Note payable (2)	117,956	-	(25,892)	92,064	28,603
Capital lease (3)	101,897	-	(39,769)	62,128	41,081
Capital lease (4)	364,361	-	(47,881)	316,480	61,722
	<u>\$ 4,584,214</u>	<u>\$ -</u>	<u>\$ (113,542)</u>	<u>\$ 4,470,672</u>	<u>\$ 157,596</u>
	Balance March 31, 2017	Additions	Payments	Balance March 31, 2018	Due Within One Year
Note payable (5)	\$1,767,827	\$ -	\$ (1,767,827)	\$ -	\$ -
Note payable (1)	-	4,000,000	-	4,000,000	28,793
Note payable (2)	-	120,000	(2,044)	117,956	25,892
Capital lease (3)	140,395	-	(38,498)	101,897	39,770
Capital lease (4)	-	364,361	-	364,361	60,057
	<u>\$1,908,222</u>	<u>\$ 4,484,361</u>	<u>\$ (1,808,369)</u>	<u>\$ 4,584,214</u>	<u>\$ 154,512</u>

The terms and due dates of the Hospital's long-term debt at March 31, 2019 and 2018 are as follows:

1. Demand note payable to bank with a variable interest rate WSJ prime plus 1.75% (6.00% as of March 31, 2019). The note was modified March 28, 2019 changing maturity date of December 28, 2037 to December 28, 2038 and extending the interest only payments to December 28, 2019. The Hospital will make monthly principal and interest in monthly installments of \$29,550 beginning January 28, 2020, secured by assets of the Hospital.
2. Promissory note to a physician with an interest rate of 10.00%, due in monthly installments of \$3,044, unsecured, due February 2022.
3. Capital lease with imputed interest rate of 3.25%, due in monthly installments of \$3,541, collateralized by associated equipment, due September 2020.
4. Capital lease with imputed interest rate of 2.74%, due in monthly installments of \$4,771, collateralized by associated equipment, due December 2024.
5. The note was refinanced during 2018 with the 6% variable interest demand note.



Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

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

<u>Year Ending March 31,</u>	<u>Notes Payable</u>		<u>Capital Lease Obligations</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2020	\$ 54,793	\$ 262,388	\$ 102,803	\$ 9,122
2021	136,496	255,826	71,966	6,538
2022	143,665	245,613	52,330	4,926
2023	119,159	236,641	53,781	3,475
2024	127,001	228,799	55,271	1,985
2025-2029	771,927	1,007,073	42,457	486
2030-2034	1,061,627	717,373	-	-
2035-2039	1,399,788	319,289	-	-
2040-2041	277,608	15,783	-	-
Total	<u>\$ 4,092,064</u>	<u>\$ 3,288,785</u>	<u>\$ 378,608</u>	<u>\$ 26,532</u>

**Note 7 - 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, 2019 and 2018 was as follows:

	<u>2019</u>	<u>2018</u>
Medicare	26%	21%
Medicaid	9%	7%
Blue Cross	6%	5%
Other commercial insurance	19%	16%
Other third-party payors and patients	40%	51%
	<u>100%</u>	<u>100%</u>

## **Note 8 - 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 an occurrence-based coverage subject to a limit of \$1,000,000 per claim and an annual aggregate limit of \$3,000,000.

### **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.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

**Note 9 - 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, 2019.

Statement of net position as of March 31, 2019:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
<b>Assets</b>				
Current assets	\$ 2,868,855	\$ 77,418	\$ (393,082)	\$ 2,553,191
Capital assets	2,003,907	101,093	-	2,105,000
Other non current assets	64,830	-	-	64,830
Total assets	\$ 4,937,592	\$ 178,511	\$ (393,082)	\$ 4,723,021
<b>Liabilities and Net Position</b>				
Current liabilities	\$ 4,084,195	\$ 393,082	\$ (393,082)	\$ 4,084,195
Long-term liabilities	4,313,076	-	-	4,313,076
Total liabilities	8,397,271	393,082	(393,082)	8,397,271
<b>Net Position (Deficit)</b>				
Net investment in capital assets	1,625,299	101,093	-	1,726,392
Unrestricted net position	(5,084,978)	(315,664)	-	(5,400,642)
Total net position (deficit)	(3,459,679)	(214,571)	-	(3,674,250)
Total liabilities and net position	\$ 4,937,592	\$ 178,511	\$ (393,082)	\$ 4,723,021

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

Operating results and changes in net position for the year ended March 31, 2019:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
Operating Revenues				
Net patient service revenue	\$ 8,577,344	\$ 470,341	\$ -	\$ 9,047,685
Other operating revenue	151,919	-	(21,600)	130,319
Total operating revenue	<u>8,729,263</u>	<u>470,341</u>	<u>(21,600)</u>	<u>9,178,004</u>
Operating Expenses				
Depreciation	430,671	9,698	-	440,369
Other operating expenses	10,487,707	433,072	(21,600)	10,899,179
Total operating expenses	<u>10,918,378</u>	<u>442,770</u>	<u>(21,600)</u>	<u>11,339,548</u>
Operating Income (Loss)	<u>(2,189,115)</u>	<u>27,571</u>	<u>-</u>	<u>(2,161,544)</u>
Nonoperating Revenue (Expense)				
Interest income	178	-	-	178
Noncapital appropriation	702,714	-	-	702,714
Interest expense	(292,159)	-	-	(292,159)
Noncapital grants and contributions	1,375	-	-	1,375
Total nonoperating revenue (expense)	<u>412,108</u>	<u>-</u>	<u>-</u>	<u>412,108</u>
Change in Net Position	(1,777,007)	27,571	-	(1,749,436)
Net Position (Deficit), Beginning of Year	<u>(1,682,672)</u>	<u>(242,142)</u>	<u>-</u>	<u>(1,924,814)</u>
Net Position (Deficit), End of Year	<u>\$ (3,459,679)</u>	<u>\$ (214,571)</u>	<u>\$ -</u>	<u>\$ (3,674,250)</u>

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

Cash flows for the year ended March 31, 2019:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Total
Net Cash from (used for) Operating Activities	\$ (399,589)	\$ 15,253	\$ (384,336)
Net Cash from Noncapital Financing Activities	423,992	-	423,992
Net Cash used for Capital and related Financing Activities	(100,574)	-	(100,574)
Net Cash from Investing Activities	178	-	178
Net Change in Cash	(75,993)	15,253	(60,740)
Cash, Beginning of Year	187,807	6,158	193,965
Cash, End of Year	<u>\$ 111,814</u>	<u>\$ 21,411</u>	<u>\$ 133,225</u>

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, 2018.

Statement of net position as of March 31, 2018:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
<b>Assets</b>				
Current assets	\$ 2,916,612	\$ 39,201	\$ (368,070)	\$ 2,587,743
Capital assets	2,434,576	110,793	-	2,545,369
Other non current assets	97,330	-	-	97,330
Total assets	<u>\$ 5,448,518</u>	<u>\$ 149,994</u>	<u>\$ (368,070)</u>	<u>\$ 5,230,442</u>
<b>Liabilities and Net Position</b>				
Current liabilities	\$ 2,701,488	\$ 392,136	\$ (368,070)	\$ 2,725,554
Long-term liabilities	4,429,702	-	-	4,429,702
Total liabilities	<u>7,131,190</u>	<u>392,136</u>	<u>(368,070)</u>	<u>7,155,256</u>
<b>Net Position (Deficit)</b>				
Net investment in capital assets	1,968,318	110,793	-	2,079,111
Unrestricted net position	<u>(3,650,990)</u>	<u>(352,935)</u>	<u>-</u>	<u>(4,003,925)</u>
Total net position (deficit)	<u>(1,682,672)</u>	<u>(242,142)</u>	<u>-</u>	<u>(1,924,814)</u>
Total liabilities and net position	<u>\$ 5,448,518</u>	<u>\$ 149,994</u>	<u>\$ (368,070)</u>	<u>\$ 5,230,442</u>

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

Operating results and changes in net position for the year ended March 31, 2018:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Eliminations	Total
<b>Operating Revenues</b>				
Net patient service revenue	\$ 9,403,429	\$ 436,758	\$ -	\$ 9,840,187
Other operating revenue	44,330	-	(21,600)	22,730
<b>Total operating revenue</b>	<b>9,447,759</b>	<b>436,758</b>	<b>(21,600)</b>	<b>9,862,917</b>
<b>Operating Expenses</b>				
Depreciation	473,938	10,902	-	484,840
Other operating expenses	12,312,076	396,454	(21,600)	12,686,930
<b>Total operating expenses</b>	<b>12,786,014</b>	<b>407,356</b>	<b>(21,600)</b>	<b>13,171,770</b>
<b>Operating Income (Loss)</b>	<b>(3,338,255)</b>	<b>29,402</b>	<b>-</b>	<b>(3,308,853)</b>
<b>Nonoperating Revenue (Expense)</b>				
Interest income	15	-	-	15
Noncapital appropriation	736,695	-	-	736,695
Interest expense	(173,171)	-	-	(173,171)
Gain on disposal of equipment	12,200	-	-	12,200
<b>Total non operating revenue (expense)</b>	<b>575,739</b>	<b>-</b>	<b>-</b>	<b>575,739</b>
<b>Expenses in Excess of Revenues Before Capital Contributions</b>	<b>(2,762,516)</b>	<b>29,402</b>	<b>-</b>	<b>(2,733,114)</b>
<b>Capital Contributions</b>	<b>125,000</b>	<b>-</b>	<b>-</b>	<b>125,000</b>
<b>Change in Net Position</b>	<b>(2,637,516)</b>	<b>29,402</b>	<b>-</b>	<b>(2,608,114)</b>
<b>Net Position (Deficit), Beginning of Year</b>	<b>954,844</b>	<b>(271,544)</b>	<b>-</b>	<b>683,300</b>
<b>Net Position (Deficit), End of Year</b>	<b>\$ (1,682,672)</b>	<b>\$ (242,142)</b>	<b>\$ -</b>	<b>\$ (1,924,814)</b>

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

Cash flows for the year ended March 31, 2018:

	Sequoyah Memorial Hospital	SMH Physician Group, LLC	Total
Net Cash from (used for) Operating Activities	\$ (2,493,481)	\$ 6,128	\$ (2,487,353)
Net Cash from Noncapital Financing Activities	2,738,189	-	2,738,189
Net Cash used for Capital and related Financing Activities	(74,942)	-	(74,942)
Net Cash from Investing Activities	15	-	15
Net Change in Cash	169,781	6,128	175,909
Cash, Beginning of Year	18,026	30	18,056
Cash, End of Year	<u>\$ 187,807</u>	<u>\$ 6,158</u>	<u>\$ 193,965</u>

**Note 10 - 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 \$349,729, for the year ended March 31, 2019. In return, the Hospital received \$677,045. The Hospital made SHOPP payments totaling \$401,664, for the year ended March 31, 2018. In return, the Hospital received \$837,749. Future changes in law or regulation at the federal or state level can adversely affect or eliminate SHOPP.

Sequoyah County-City of Sallisaw Hospital Authority  
d/b/a Northeastern Health System Sequoyah

Notes to Financial Statements  
March 31, 2019 and 2018

---

**Note 11 - Management Agreement**

Effective June 1, 2017, the Hospital's board entered into a management contract with THA. The contract is for a five-year term with automatic renewal term of five years. 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 Hospital will reimburse THA all salaries plus 30% for benefits. The Hospital will pay THA an incentive based on net profits above \$250,000. The Hospital paid THA \$6,620,375 and \$1,516,610 for contracted salary and benefits, management fees and other professional services in the year ended March 31, 2019 and 2018. As of March 31, 2019 and 2018, the Hospital owes THA \$2,661,175 and \$848,405 for management fees and other professional services. As of March 31, 2019 and 2018, the Hospital owes \$316,480 and \$364,361 for equipment leased from THA.

**Note 12 - Recurring Losses and Management Plans**

The Hospital has incurred operating losses during the years ended March 31, 2019 and 2018. For the years ended March 31, 2019 and 2018, the Hospital experienced a decrease in net position of \$1,749,436 and \$2,608,114. The Hospital is looking into areas to reduce cost without impacting patient care. The Hospital is in the second year of the management agreement which has resulted in additional services being provided at the Hospital. Management believes these plans alleviate substantial doubt about the Hospital's ability to continue as a going concern for one year from the report date.

**Note 13 - Subsequent Events**

The Hospital has evaluated subsequent events through May 8, 2020 the date which the financial statements were available to be issued.

On February 4, 2020, the Hospital approved and submitted an amended offer in compromise for payroll tax penalties and interest for \$7,329. The Internal Revenue Service approved the amended offer in compromise. The Hospital will be relieved of approximately \$328,000 of accrued payroll tax penalty and interest liabilities.

The Hospital has been negatively impacted by the effects of the world-wide coronavirus pandemic. The Hospital is closely monitoring its operations, liquidity, and capital resources and is actively working to minimize the current and future impact of this unprecedented situation. As of the date of issuance of these financial statements, the full impact to the Hospital's financial position is not known.





**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 Northeastern Health System Sequoyah  
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 Northeastern Health System Sequoyah (Hospital) as of and for the year ended March 31, 2019, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements, and have issued our report thereon dated May 8, 2020.

**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 have not been identified. However, as described in the accompanying Schedule of Findings and Responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and 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 and Responses to be material weaknesses: 2019-001 through 2019-005.

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 deficiency described in the accompanying Schedule of Findings and Responses to be a significant deficiency: 2019-006.

### **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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **Hospital's Response to Findings**

The Hospital's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The Hospital's 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.



Oklahoma City, Oklahoma  
May 8, 2020

**Material Weaknesses In Internal Control Over Financial Reporting:**

**2019-001 Preparation of Financial Statements**

*Criteria:* A properly designed system of internal control over financial reporting includes the preparation of an Hospital's financial statements and accompanying notes to the financial statements by internal personnel of the Hospital. 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. 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:* We agree with the auditor's recommendation.

**2019-002 Account Reconciliations**

*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.

*Cause:* Areas with differences that resulted in significant adjustments to the financial statements included cash, patient receivables, prepaid insurance, capital assets, accounts payables, accrued liabilities, long term debt and net position.

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

*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.

**2019-003 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.

**2019-004 Capital Lease**

*Criteria:* There are two types of leases, capital and operating. A capital lease is identified by meeting one of four criteria. If the lease does not meet any of the criteria for a capital lease, it is considered an operating lease. Each type of lease is accounted for differently within an organization.

*Condition:* During the course of the engagement, we identified payments for a capital lease that were not properly recorded.

*Cause:* The Hospital was recording the capital lease payments to expense instead of reducing long-term debt.

*Effect:* Long-term debt was not properly stated in the interim financial statements.

*Auditor's Recommendation:* It is recommended that the Hospital develop policies and procedures to properly record lease payments.

*Views of Responsible Officials:* Management will develop a process to identify capital lease payments and reconcile long-term debt appropriately.

**2019-005 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.

*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.

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

*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 determining the monthly settlement estimates.

**Significant Deficiency In Internal Control Over Financial Reporting:**

**2019-006 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 Hospital's 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 Hospital.

*Views of Responsible Officials:* Management agrees with the finding and has revised the assignment of duties to obtain the maximum internal control possible under the circumstances.