Jewell County Hospital
A Component Unit of Jewell County, Kansas

Accountants' Report and Financial Statements

December 31, 2010 and 2009

BKD LLP
CPAs & Advisors

Jewell County Hospital
A Component Unit of Jewell County, Kansas
December 31, 2010 and 2009

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Independent Accountants' Report

Board of Trustees
Jewell County Hospital
Mankato, Kansas

We have audited the accompanying balance sheet of Jewell County Hospital (Hospital), a component unit of Jewell County, Kansas, as of December 31, 2010, and the related statements of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Jewell County Hospital as of and for the year ended December 31, 2009, were audited by other accountants whose report dated June 7, 2010, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2010 financial statements referred to above present fairly, in all material respects, the financial position of Jewell County Hospital as of December 31, 2010, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Hospital has not presented a management's discussion and analysis that accounting principles generally accepted in the United States of America has determined necessary to supplement, although not required to be part of, the basic financial statements.

BKD, LLP

June 9, 2011

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GLOBAL ALLIANCE OF INDEPENDENT FIRMS

Jewell County Hospital
A Component Unit of Jewell County, Kansas
Balance Sheets
December 31, 2010 and 2009

Assets

	2010	2009
Current Assets		
Cash	$ 45,053	$ 39,072
Patient accounts receivable, net	342,961	366,274
Estimated amounts due from third-party payers	160,000	45,000
Supplies	32,340	32,341
Prepaid expenses and other	28,631	35,374
Total current assets	608,985	518,061
Noncurrent Cash and Investments		
Internally designated	491,577	324,330
Restricted by grantors	6	10,934
	491,583	335,264
Capital Assets		
Land	4,760	4,760
Depreciable capital assets, net of accumulated depreciation	475,884	555,572
Total capital assets, net of accumulated depreciation	480,644	560,332
Total assets	$ 1,581,212	$ 1,413,657

See Notes to Financial Statements

Liabilities and Net Assets

	2010	2009
Current Liabilities		
Current maturities of capital lease obligations	$ 19,179	$ 18,524
Accounts payable	150,265	50,306
Salaries payable	40,123	38,818
Accrued benefits payable	110,916	96,103
Other accrued expenses	16,925	2,557
Total current liabilities	337,408	206,308
Capital Lease Obligations	69,131	88,094
Total liabilities	406,539	294,402
Net Assets		
Invested in capital assets, net of related debt	392,334	453,714
Restricted - expendable for		
Specific operating activities	6	10,934
Unrestricted	782,333	654,607
Total net assets	1,174,673	1,119,255
Total liabilities and net assets	$ 1,581,212	$ 1,413,657

Jewell County Hospital

A Component Unit of Jewell County, Kansas

Statements of Revenues, Expenses and Changes in Net Assets

Years Ended December 31, 2010 and 2009

	2010	2009
Operating Revenues		
Net patient service revenue	$ 3,094,015	$ 2,905,923
Other	86,513	87,946
Total operating revenues	3,180,528	2,993,869
Operating Expenses		
Salaries and wages	2,114,573	2,075,345
Supplies and other	1,674,188	1,588,719
Depreciation	79,281	88,714
Total operating expenses	3,868,042	3,752,778
Operating Loss	(687,514)	(758,909)
Nonoperating Revenues (Expenses)		
Property taxes	441,501	457,020
Farm rental income	41,583	41,583
Noncapital grants and gifts	41,723	34,483
Interest income	2,514	7,060
Interest expense	(6,634)	(6,032)
Gain on sale of nonoperating land	222,652	-
Loss on disposal of capital assets	(407)	-
Total nonoperating revenues	742,932	534,114
Increase (Decrease) in Net Assets	55,418	(224,795)
Net Assets, Beginning of Year	1,119,255	1,344,050
Net Assets, End of Year	$ 1,174,673	$ 1,119,255

Jewell County Hospital
A Component Unit of Jewell County, Kansas
Statements of Cash Flows
Years Ended December 31, 2010 and 2009

	2010	2009
Operating Activities		
Receipts from and on behalf of patients	$ 3,002,328	$ 2,767,392
Payments to and on behalf of employees	(2,098,455)	(2,082,938)
Payments to suppliers and contractors	(1,532,326)	(1,599,134)
Other receipts, net	86,513	87,946
Net cash used in operating activities	(541,940)	(826,734)
Noncapital Financing Activities		
Property taxes received to support operations	441,501	457,020
Noncapital grants and gifts	44,233	31,973
Net cash provided by noncapital financing activities	485,734	488,993
Capital and Related Financing Activities		
Purchase of capital assets	-	(50,025)
Principal payments on capital lease obligations	(18,308)	(15,092)
Interest paid on capital lease obligations	(6,634)	(6,032)
Net cash used in capital and related financing activities	(24,942)	(71,149)
Investing Activities		
Net change in noncurrent cash and investments	89,711	347,000
Farm rental income received	20,792	41,583
Interest income received	2,514	7,060
Net cash provided by investing activities	113,017	395,643
Increase (Decrease) in Cash	31,869	(13,247)
Cash, Beginning of Year	69,926	83,173
Cash, End of Year	$ 101,795	$ 69,926
Reconciliation of Cash to the Balance Sheets		
Cash in current assets	$ 45,053	$ 39,072
Cash in noncurrent cash and investments	56,742	30,854
	$ 101,795	$ 69,926

Jewell County Hospital
A Component Unit of Jewell County, Kansas
Statements of Cash Flows (Continued)
Years Ended December 31, 2010 and 2009

Reconciliation of Net Operating Revenue (Expenses) to Net Cash Used in Operating Activities		
Operating loss	$ (687,514)	$ (758,909)
Depreciation	79,281	88,714
Provision for uncollectible accounts	51,954	56,195
Changes in operating assets and liabilities		
Patient accounts receivable, net	(28,641)	274
Estimated amounts due from third-party payers	(115,000)	(195,000)
Prepaid expenses, supplies and other current assets	27,535	1,336
Accounts payable and accrued expenses	130,445	(19,344)
Net cash used in operating activities	$ (541,940)	$ (826,734)
Supplemental Cash Flows Information		
Capital lease obligation incurred for capital assets	$ -	$ 18,237

Jewell County Hospital
A Component Unit of Jewell County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

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

Nature of Operations and Reporting Entity

Jewell County Hospital (Hospital), a political subdivision of the State of Kansas, located in Mankato, Kansas, provides acute, long-term care, clinic and independent living (apartments) services. The Hospital is a component unit of Jewell County (County) and is governed by a Board of Trustees (Board), appointed by the Jewell County Board of County Commissioners.

Basis of Accounting and Presentation

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally federal and state grants and county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific (such as tax appropriations), interest income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

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

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. There were no cash equivalents at December 31, 2010 and 2009.

Intergovernmental Revenue

The Hospital received approximately 11% and 13% of its financial support from intergovernmental revenue derived from property taxes levied by the County in both 2010 and 2009, respectively. One hundred percent of these funds were used to support operations in both years.

Property taxes are assessed by the County in November of one year and are received beginning in January of the following year. Intergovernmental revenue is recognized in full in the year in which use is first permitted.

Risk Management

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

Patient Accounts Receivable

The Hospital reports patient accounts receivable for the services rendered at net realizable amounts from third-party payers, patients and others. The Hospital provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information, and existing economic conditions. As a service to the patient, the Hospital bills third-party payers directly and bills the patient when the patient's liability is determined. Patient accounts receivable are due in full when billed. Accounts are considered delinquent and subsequently written off as bad debts based on individual credit evaluation and specific circumstances of the account.

Supplies

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

Capital Assets

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

Land improvements	15-20 years
Buildings	10-40 years
Fixed equipment	5-20 years
Moveable equipment	3-20 years

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. When depreciable property is retired or otherwise disposed of, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is reflected in nonoperating revenues (expenses).

Compensated Absences

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

Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase of those assets. Restricted expendable net assets are noncapital assets that must be used for a particular purpose as specified by donors or grantors external to the Hospital. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the above conditions.

Net Patient Service Revenue

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

Charity Care

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

Income Taxes

As an essential government entity, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Hospital is subject to federal income tax on any unrelated business taxable income.

Reclassifications

Certain reclassifications have been made to the 2009 financial statements to conform to the 2010 financial statement presentation. These reclassifications had no effect on the change in net assets.

Note 2: Deposits

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State law requires collateralization of all deposits with federal depository insurance and other acceptable collateral having an aggregate value at least equal to the amount of the deposits.

At December 31, 2010 and 2009, none of the Hospital's deposits (checking and savings accounts) were exposed to custodial credit risk.

The carrying amounts of deposits are included in the Hospital's balance sheet captions as follows at December 31, 2010 and 2009:

	2010	2009
Cash	$ 44,578	$ 38,596
Noncurrent cash and investments	56,742	30,854
	$ 101,320	$ 69,450

Note 3: Patient Accounts Receivable, Net/Net Patient Service Revenue

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

Medicare. The Hospital is recognized as a Critical Access Hospital (CAH). Under CAH rules, inpatient acute care, skilled swing-bed and certain outpatient services rendered to Medicare program beneficiaries are paid at one hundred one percent (101%) of allowable cost subject to certain limitations. Other outpatient, including clinic services, related to Medicare beneficiaries are paid based on a combination of fee schedules and cost reimbursement methodologies. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare administrative contractor.

Medicaid. The Medicaid State Plan provides for a cost reimbursement methodology for inpatient and outpatient services rendered to beneficiaries who are not part of a Medicaid managed care network. The Hospital is reimbursed for services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital with audits thereof by the Medicaid administrative contractor.

Medicaid reimbursement for long-term care facility residents is based on a cost-based prospective reimbursement methodology. The Hospital is reimbursed at a prospective rate with annual cost reports submitted to the Medicaid program. Rates are computed each calendar quarter using an average of the 2005, 2006 and 2007 cost reports and changes in the Medicaid resident case mix index. The Medicaid cost reports are subject to audit by the State and adjustments to rates can be made retroactively.

Approximately 85% and 82% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2010 and 2009, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined case rates and discounts from established charges.

During March 2010, President Obama signed into law the *Patient Protection and Affordable Care Act* and the *Health Care and Education Tax Credits Reconciliation Act of 2010*. Together, these two acts will reform the health care system and will impact payments received by health care providers. Any reductions in payments may be offset by reductions in bad debts and charity care, as the number of uninsured Americans is reduced. However, the overall impact on the Hospital of the health care reform is not presently determinable.

Accounts receivable are recorded net of the allowance for uncollectible accounts and allowance for contractual adjustments at December 31, 2010 and 2009, as follows:

	2010	2009
Gross patient accounts receivable		
Medicare	$ 176,255	$ 201,418
Medicaid	30,260	34,757
Blue Cross	68,472	35,696
Other third-party payers	52,374	46,611
Self-pay	94,140	94,746
	421,501	413,228
Less allowance for uncollectible accounts	(51,948)	(57,075)
Plus (less) allowance for contractual adjustments	(26,592)	10,121
Patient accounts receivable, net	$ 342,961	$ 366,274

Net patient service revenue for the years ending December 31, 2010 and 2009, are as follows:

	2010	2009
Gross patient service revenue	$ 3,046,572	$ 3,032,593
Plus (less):		
Contractual adjustments		
Medicare	341,979	180,153
Medicaid	26,360	2,596
Blue Cross	(126,093)	(126,778)
Other	(46,409)	(45,057)
Administrative adjustments	(39,171)	(24,579)
Charity care	(57,269)	(56,810)
Provision for uncollectible accounts	(51,954)	(56,195)
Net patient service revenue	$ 3,094,015	$ 2,905,923

Note 4: Concentration of Credit Risk

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer arrangements. The mix of accounts receivable net of allowance for uncollectible accounts and contractual allowances at December 31, 2010 and 2009, are as follows:

	2010	2009
Medicare	52%	63%
Medicaid	4	4
Blue Cross	14	7
Other third-party payers	10	9
Self-pay	20	17
	100%	100%

Note 5: Noncurrent Cash and Investments

Noncurrent cash and investments include 1) funds internally designated by the Board of Trustees and 2) assets restricted by grantors. Board designated assets represent those assets over which the Board retains control and may designate, at its discretion, for a specific purpose. Grant funds are restricted for specific purposes, as determined by the grantor.

The internally designated funds consist primarily of farmland, funds held by the County on behalf of the Hospital and cash. The Hospital sold a portion of the farmland during 2010. The gain on the sale of $222,652 is included as nonoperating revenue in the accompanying statements of revenues, expenses and changes in net assets. The externally restricted assets totaled $6 and $10,934 at December 31, 2010 and 2009, respectively.

Note 6: Capital Assets

Capital assets activity for the years ended December 31, 2010 and 2009, was:

	2010			
	Beginning Balance	Additions	Disposals	Ending Balance
Land	$ 4,760	$ -	$ -	$ 4,760
Land improvements	104,021	-	(279)	103,742
Buildings	1,180,703	-	(1,562)	1,179,141
Fixed equipment	353,302	-	(2,102)	351,200
Moveable equipment	862,478	-	(16,635)	845,843
	2,505,264	-	(20,578)	2,484,686
Less accumulated depreciation				
Land improvements	33,879	5,911	(279)	39,511
Buildings	904,716	28,504	(1,273)	931,947
Fixed equipment	259,631	11,255	(2,102)	268,784
Moveable equipment	746,706	33,611	(16,517)	763,800
	1,944,932	79,281	(20,171)	2,004,042
Capital Assets, Net	$ 560,332	$ (79,281)	$ (407)	$ 480,644

	2009			
	Beginning Balance	Additions	Disposals	Ending Balance
Land	$ 4,760	$ -	$ -	$ 4,760
Land improvements	98,259	5,762	-	104,021
Buildings	1,180,703	-	-	1,180,703
Fixed equipment	328,207	36,300	(11,205)	353,302
Moveable equipment	853,970	26,200	(17,692)	862,478
	2,465,899	68,262	(28,897)	2,505,264
Less accumulated depreciation				
Land improvements	28,319	5,560	-	33,879
Buildings	875,537	29,179	-	904,716
Fixed equipment	258,755	12,081	(11,205)	259,631
Moveable equipment	722,504	41,894	(17,692)	746,706
	1,885,115	88,714	(28,897)	1,944,932
Capital Assets, Net	$ 580,784	$ (20,452)	$ -	$ 560,332

Note 7: Capital Lease Obligations

Capital lease obligation activity for the years ended December 31, 2010 and 2009, was:

	Beginning Balance	Additions	Deductions	Ending Balance	Amounts Due Within One Year
2010	$ 106,618	$ -	$ (18,308)	$ 88,310	$ 19,179
2009	$ 103,473	$ 18,237	$ (15,092)	$ 106,618	$ 18,524

A schedule of the cost and accumulated depreciation on equipment under capital lease at December 31, 2010 and 2009, is as follows:

	2010	2009
Moveable equipment	$ 144,518	$ 144,518
Accumulated amortization	(112,473)	(94,954)
	$ 32,045	$ 49,564

The following is a schedule by year of future minimum lease payments under the capital leases including interest rates of 5% to 12% together with the present value of the future minimum lease payments:

Year Ending December 31,	
2011	$ 23,741
2012	23,805
2013	22,766
2014	22,154
2015	6,830
Total minimum lease payments	99,296
Less amount representing interest	10,986
Present value of net minimum lease payments	$ 88,310

Note 8: Medical Malpractice Coverage and Claims

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

Note 9: Deferred Compensation

The Hospital maintains a matching deferred compensation plan for all eligible employees. Eligibility is established by all employees who have completed one year of continuous service. Full-time employees may contribute up to 4% of their gross compensation per year. Part-time employees may contribute up to 2% of their gross compensation per year. Employee contributions to all benefit plans cannot exceed 25% of their gross compensation or $16,500. The Hospital matches employee contributions up to 4% and 2% of eligible compensation for full-time and part-time employees, respectively. Employer and employee contributions vest immediately. Benefits are funded by fixed and variable annuities with an insurance company. Contributions actually made by employees totaled $53,835 and $48,958 in 2010 and 2009, respectively. Hospital contributions totaled $41,894 and $38,269 in 2010 and 2009, respectively.

Note 10: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Allowance for Net Patient Service Revenue Adjustments

Estimates of allowances for adjustments included in net patient service revenue are described in *Notes 1* and *3*.

Current Economic Conditions

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

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

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

Note 11: Subsequent Event – Medicaid Provider Assessment

On February 2, 2011, the Centers for Medicare and Medicaid Services (CMS) approved a Medicaid State Plan amendment which provides for additional funds to be paid to operators of long-term care facilities. The Kansas Department on Aging has estimated the additional net receipts for the Hospital to be approximately $246,000. These receipts began in March 2011.