

Stevens County Hospital
A Component Unit of Stevens County, Kansas
Independent Auditor's Report and Financial Statements
December 31, 2018 and 2017

Stevens County Hospital
A Component Unit of Stevens County, Kansas
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Independent Auditor's Report

Board of Directors
Stevens County Hospital
Hugoton, Kansas

We have audited the accompanying financial statements of Stevens County Hospital (Hospital), a component unit of Stevens County, Kansas, as of and for the years ended December 31, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements as listed in the table of contents.

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 and the provisions of the Kansas Municipal Audit and Accounting Guide; 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 Kansas Municipal Audit and Accounting Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Stevens County Hospital as of December 31, 2018 and 2017, 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.

Required Supplementary Information

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

BKD, LLP

Wichita, Kansas
July 31, 2019

Stevens County Hospital
A Component Unit of Stevens County, Kansas
Balance Sheets
December 31, 2018 and 2017

	2018	2017
Assets		
Current Assets		
Cash and cash equivalents	\$ 726,711	\$ 581,389
Short-term certificates of deposit	4,265	2,770
Patient accounts receivable, net of allowance; 2018 – \$672,000, 2017 – \$574,000	1,919,814	1,268,475
Accounts receivable – retail pharmacy	68,199	90,498
Estimated amounts due from third-party payers	1,005	180,000
Supplies	271,333	286,798
Prepaid expenses and other	48,911	199,214
Total current assets	3,040,238	2,609,144
Capital Assets, Net	20,490,939	21,288,824
Total assets	\$ 23,531,177	\$ 23,897,968
 Liabilities and Net Position		
Current Liabilities		
Current maturities of long-term debt	\$ 29,723	\$ 29,135
Accounts payable	590,632	512,107
Accrued expenses	913,070	771,707
Estimated amounts due to third-party payers	269,000	1,753
Total current liabilities	1,802,425	1,314,702
Long-term Debt	114,208	143,931
Total liabilities	1,916,633	1,458,633
Net Position		
Net investment in capital assets	20,347,008	21,115,758
Unrestricted	1,267,536	1,323,577
Total net position	21,614,544	22,439,335
Total liabilities and net position	\$ 23,531,177	\$ 23,897,968

Stevens County Hospital
A Component Unit of Stevens County, Kansas
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2018 and 2017

	2018	2017
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2018 – \$424,000, 2017 – \$367,000	\$ 15,979,467	\$ 13,765,840
Other	20,828	24,868
Total operating revenues	16,000,295	13,790,708
Operating Expenses		
Salaries and wages	8,571,271	8,247,189
Employee benefits	2,675,873	2,589,643
Purchased services and professional fees	1,663,891	1,595,602
Supplies and other	3,480,293	2,701,102
Retail pharmacy supplies	1,009,124	892,809
Depreciation	918,247	1,179,059
Total operating expenses	18,318,699	17,205,404
Operating Loss	(2,318,404)	(3,414,696)
Nonoperating Revenues (Expenses)		
Noncapital appropriations – Stevens County	1,466,545	1,586,836
Interest income	15,549	18,952
Interest expense	(3,195)	(3,772)
Noncapital grants and gifts	27,113	7,666
Other	(12,399)	(2,052)
Total nonoperating revenues	1,493,613	1,607,630
Decrease in Net Position	(824,791)	(1,807,066)
Net Position, Beginning of Year	22,439,335	24,246,401
Net Position, End of Year	\$ 21,614,544	\$ 22,439,335

Stevens County Hospital
A Component Unit of Stevens County, Kansas
Statements of Cash Flows
Years Ended December 31, 2018 and 2017

	2018	2017
Operating Activities		
Receipts from and on behalf of patients	\$ 15,796,669	\$ 13,396,789
Payments to suppliers and contractors	(5,909,015)	(5,335,431)
Payments to and on behalf of employees	(11,105,781)	(10,861,723)
Other receipts, net	20,828	24,868
Net cash used in operating activities	(1,197,299)	(2,775,497)
Noncapital Financing Activities		
Noncapital appropriations – Stevens County	1,466,545	1,586,836
Noncapital grants and gifts	27,113	7,666
Other	(12,399)	(2,052)
Net cash provided by noncapital financing activities	1,481,259	1,592,450
Capital and Related Financing Activities		
Principal paid on long-term debt	(29,135)	(28,558)
Interest paid on long-term debt	(3,195)	(3,772)
Purchase of capital assets	(120,362)	(402,260)
Net cash used in capital and related financing activities	(152,692)	(434,590)
Investing Activities		
Interest income received	15,549	18,952
Change in certificates of deposit	(1,495)	(298)
Proceeds from disposition of certificates of deposit	-	322,389
Net cash provided by investing activities	14,054	341,043
Increase (Decrease) in Cash and Cash Equivalents	145,322	(1,276,594)
Cash and Cash Equivalents, Beginning of Year	581,389	1,857,983
Cash and Cash Equivalents, End of Year	\$ 726,711	\$ 581,389

Stevens County Hospital
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Statements of Cash Flows (Continued)
Years Ended December 31, 2018 and 2017

	2018	2017
Reconciliation of Operating Loss to Net		
Cash Used in Operating Activities		
Operating loss	\$ (2,318,404)	\$ (3,414,696)
Depreciation	918,247	1,179,059
Provision for uncollectible accounts	424,176	367,326
Changes in operating assets and liabilities		
Patient accounts receivable, net	(1,053,216)	116,870
Estimated amounts due from and to third-party payers	446,242	(853,247)
Accounts payable and accrued expenses	219,888	(114,093)
Supplies and prepaid expenses and other	165,768	(56,716)
Net cash used in operating activities	\$ (1,197,299)	\$ (2,775,497)

Stevens County Hospital
A Component Unit of Stevens County, Kansas
Notes to Financial Statements
December 31, 2018 and 2017

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

Nature of Operations and Reporting Entity

Stevens County Hospital (the Hospital) is an acute care hospital located in Hugoton, Kansas. The Hospital is a component unit of Stevens County (County) and the Board of County Commissioners appoints members to the Board of Directors of the Hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in the Stevens County area. It also operates a long-term care facility and retail pharmacy a in the same geographic area.

Basis of Accounting and Presentation

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

Use of Estimates

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

Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2018 and 2017, cash equivalents consisted primarily of certificates of deposit, which are carried at amortized cost.

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Noncapital Appropriations – Stevens County

The Hospital received approximately 8% and 10% of its financial support from county appropriations derived from property taxes levied by the County in 2018 and 2017, 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; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters, except workers' compensation and property and casualty coverage. Settled claims have not exceeded commercial coverage in any of the three preceding years.

Workers' compensation coverage is provided through a fund managed by the Kansas Hospital Association. The workers' compensation premiums are subject to retrospective adjustment based upon the overall performance of the fund. Property and casualty coverage is provided through a fund managed by the Kansas Counties Association Multi-Line Pool. The property and casualty premiums are subject to retrospective adjustment based upon the overall performance of the fund. Management believes adequate reserves are in place to cover claims incurred but not reported for both workers' compensation and property and casualty risks.

Patient Accounts Receivable

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

Supplies

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

Stevens County Hospital
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Capital Assets

Capital assets are recorded at cost at the date of acquisition, or acquisition 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	10 – 40 years
Building	5 – 40 years
Fixed equipment	5 – 25 years
Major moveable equipment	3 – 20 years

Capital Asset Impairment

The Hospital evaluates capital assets for impairment whenever events or circumstances indicate a significant, unexpected decline in the service utility of a capital asset has occurred. If a capital asset is tested for impairment and the magnitude of the decline in service utility is significant and unexpected, accumulated depreciation is increased by the amount of the impairment loss.

No asset impairment was recognized during the years ended December 31, 2018 and 2017.

Compensated Absences

Hospital policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as vacation benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Expense and the related liability for sick leave benefits are recognized when earned to the extent the employee is expected to realize the benefit in cash determined using the termination payment method. Sick leave benefits expected to be realized as paid time off are recognized as expense when the time off occurs and no liability is accrued for such benefits employees have earned but not yet realized. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at that date.

Net Position

Net position of the Hospital is classified in two components. Net investment in capital assets consists of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purpose or construction of those assets. Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets.

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Net Patient Service Revenue

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

Charity Care

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

Income Taxes

As an essential government function of the County, the Hospital is exempt from income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law.

Note 2: Net Patient Service Revenue

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

Medicare. The Hospital is recognized as a critical access hospital (CAH) and is paid at one hundred one percent (101%) of allowable costs for certain inpatient and outpatient services. The Hospital is reimbursed for certain services and 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. Rural health clinic services are paid on a cost basis. Home health services are paid on a per-episode basis using clinical diagnostic and other factors. A mandatory payment reduction, known as sequestration, of 2% is in effect and will reduce payments until 2025.

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Medicaid. Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed on a prospective payment methodology, which includes a hospital specific add-on percentage based on prior filed cost reports. The add-on percentage may be rebased at some time in the future.

Services rendered for long-term care facility residents are reimbursed under a prospective rate, with annual cost reposts submitted to the Medicaid program. Effective July 1, 2016, rates are computed using an average of the three most recent filed calendar cost reports and changes in the Medicaid resident case mix. The Medicaid cost reports are subject to audit by the State and adjustments to rates can be made retroactively.

Approximately 40% and 50% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2018 and 2017, 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 rates per discharge, discounts from established charges and prospectively determined daily rates.

Note 3: 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; bonds and other obligations of the U.S. Treasury, U.S. agencies or instrumentalities or the state of Kansas, bonds of any city, county, school district or special road district of the state of Kansas; bonds of any state; or a surety bond having an aggregate value at least equal to the amount of the deposits.

At December 31, 2018 and 2017, respectively, \$328,812 and \$267,211 of the Hospital's bank balances of \$886,042 and \$848,019 were exposed to custodial credit risk as follows:

	2018	2017
Uninsured and collateral held by pledging financial institution's trust department or agent in other than the Hospital's name	\$ 328,812	\$ 267,211

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Summary of Carrying Values

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

	<u>2018</u>	<u>2017</u>
Carrying value		
Deposits	<u>\$ 730,976</u>	<u>\$ 584,159</u>
Included in the following balance sheet captions		
Cash and cash equivalents	\$ 726,711	\$ 581,389
Short-term certificates of deposit	<u>4,265</u>	<u>2,770</u>
	<u>\$ 730,976</u>	<u>\$ 584,159</u>

Note 4: Patient Accounts Receivable

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31, 2018 and 2017, consisted of:

	<u>2018</u>	<u>2017</u>
Medicare	\$ 745,933	\$ 654,346
Medicaid	280,048	185,274
Blue Cross	217,805	178,076
Other third-party payers	391,928	206,278
Patients	<u>956,100</u>	<u>618,501</u>
	2,591,814	1,842,475
Less allowance for uncollectible accounts	<u>672,000</u>	<u>574,000</u>
	<u>\$ 1,919,814</u>	<u>\$ 1,268,475</u>

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Notes to Financial Statements
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Note 5: Capital Assets

Capital assets activity for the years ended December 31, 2018 and 2017, was:

	2018				Ending Balance
	Beginning Balance	Additions	Disposals	Transfers	
Land improvements	\$ 103,580	\$ -	\$ -	\$ -	\$ 103,580
Buildings	24,758,716	5,850	-	-	24,764,566
Fixed equipment	3,023,124	43,559	-	-	3,066,683
Major moveable equipment	7,498,276	70,953	-	-	7,569,229
	<u>35,383,696</u>	<u>120,362</u>	<u>-</u>	<u>-</u>	<u>35,504,058</u>
Less accumulated depreciation					
Land improvements	80,278	6,216	-	-	86,494
Buildings	6,255,236	601,300	-	-	6,856,536
Fixed equipment	621,773	192,796	-	-	814,569
Major moveable equipment	7,137,585	117,935	-	-	7,255,520
	<u>14,094,872</u>	<u>918,247</u>	<u>-</u>	<u>-</u>	<u>15,013,119</u>
Capital assets, net	<u>\$21,288,824</u>	<u>\$ (797,885)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$20,490,939</u>
	2017				Ending Balance
	Beginning Balance	Additions	Disposals	Transfers	
Land improvements	\$ 103,580	\$ -	\$ -	\$ -	\$ 103,580
Buildings	24,459,255	299,461	-	-	24,758,716
Fixed equipment	3,004,754	18,370	-	-	3,023,124
Major moveable equipment	7,413,847	84,429	-	-	7,498,276
	<u>34,981,436</u>	<u>402,260</u>	<u>-</u>	<u>-</u>	<u>35,383,696</u>
Less accumulated depreciation					
Land improvements	74,061	6,217	-	-	80,278
Buildings	5,662,968	592,268	-	-	6,255,236
Fixed equipment	429,122	192,651	-	-	621,773
Major moveable equipment	6,749,662	387,923	-	-	7,137,585
	<u>12,915,813</u>	<u>1,179,059</u>	<u>-</u>	<u>-</u>	<u>14,094,872</u>
Capital assets, net	<u>\$22,065,623</u>	<u>\$ (776,799)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$21,288,824</u>

Stevens County Hospital
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Note 6: Medical Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy with a fixed premium, which provides \$200,000 of coverage for each medical incident and \$600,000 of aggregate coverage for each policy year. The policy only covers claims made and reported to the insurer during the policy term, regardless of when the incident giving rise to the claim occurred. The Kansas Health Care Stabilization Fund provides an additional \$800,000 of coverage for each medical incident and \$2,400,000 of aggregate coverage for each policy year.

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

Note 7: Long-term Debt

The following is a summary of long-term obligation transactions for the Hospital for the years ended December 31, 2018 and 2017:

		2018				
		Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt						
	Capital lease obligations	\$ 173,066	\$ -	\$ 29,135	\$ 143,931	\$ 29,723
	Total long-term debt	<u>\$ 173,066</u>	<u>\$ -</u>	<u>\$ 29,135</u>	<u>\$ 143,931</u>	<u>\$ 29,723</u>
		2017				
		Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt						
	Capital lease obligations	\$ 201,624	\$ -	\$ 28,558	\$ 173,066	\$ 29,135
	Total long-term debt	<u>\$ 201,624</u>	<u>\$ -</u>	<u>\$ 28,558</u>	<u>\$ 173,066</u>	<u>\$ 29,135</u>

Stevens County Hospital
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December 31, 2018 and 2017

Capital Lease Obligations

The Hospital is obligated under leases for equipment and software that are accounted for as capital leases. At the end of the lease terms, the leased assets become the assets of the Hospital. Assets under capital leases at December 31, 2018 and 2017, totaled \$63,763 and \$106,271, respectively, net of accumulated depreciation of \$233,797 and \$191,289, respectively. The following is a schedule by year of future minimum lease payments under the capital lease, including interest at 2.00% together with the present value of the future minimum lease payments as of December 31, 2018:

2019	\$	32,330
2020		32,330
2021		32,330
2022		32,330
2023		21,553
Total minimum lease payments		150,873
Less amount representing interest		6,942
Present value of future minimum lease payments	\$	143,931

Note 8: Defined Contribution Plan

The Hospital contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's required contributions, determined in accordance with the terms of the plan. The plan is administered by a board of trustees appointed by the Board of County Commissioners. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Hospital's governing body. Contribution rates for plan members and the Hospital expressed as a percentage of covered payrolls were 3% and 4%, respectively, for both 2018 and 2017. Contributions actually made by plan members aggregated \$146,756 and \$147,619 during 2018 and 2017, respectively. Contributions actually made by the Hospital aggregated \$194,177 and \$195,588 during 2018 and 2017, respectively.

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Note 9: Charity Care

The costs of charity care provided under the Hospital's charity care policy were \$132,571 and \$95,002 for 2018 and 2017, respectively. The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges.

Note 10: Future Change in Accounting Principle

Governmental Accounting Standards Board (GASB) Statement No. 87, *Leases* (GASB 87) provides a new framework for accounting for leases under the principle that leases are financings. No longer will leases be classified between capital and operating. Lessees will recognize an intangible asset and a corresponding liability. The liability will be based on the payments expected to be paid over the lease term, which includes an evaluation of the likelihood of exercising renewal or termination options in the lease. Lessors will recognize a lease receivable and related deferred inflow of resources. Lessors will not derecognize the underlying asset. An exception to the general model is provided for short-term leases that cannot last more than 12 months. Contracts that contain lease and nonlease components will need to be separated so each component is accounted for accordingly. GASB 87 is effective for financial statements for fiscal years beginning after December 15, 2019. Earlier application is encouraged. Governments will be allowed to transition using the facts and circumstances in place at the time of adoption, rather than retroactive to the time each lease was begun. The Hospital is evaluating the impact the statement will have on the financial statements.