

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Independent Auditor's Report and Financial Statements
June 30, 2017 and 2016



Kearny County Hospital
A Component Unit of Kearny County, Kansas
June 30, 2017 and 2016

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Independent Auditor's Report

Board of Trustees
Kearny County Hospital
Lakin, Kansas

We have audited the accompanying financial statements of Kearny County Hospital (the Hospital), a component unit of Kearny County, Kansas, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise Kearny County 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; 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of 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 Kearny County Hospital as of June 30, 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.

Emphasis of Matter

The 2016 financial statements, before they were restated for the matters discussed in *Note 14*, were audited by other auditors and their report thereon dated, January 23, 2017, expressed an unmodified opinion. Our opinion is not modified with respect to this matter.

Other Matters

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
December 15, 2017

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Balance Sheets
June 30, 2017 and 2016

Assets

	2017	2016 <i>(Restated)</i>
Current Assets		
Cash	\$ 43,912	\$ -
Patient accounts receivable, net of allowance; 2017 - \$367,306, 2016 - \$313,103	2,347,358	2,256,995
Other receivables	230,775	129,778
Employee receivables	116,274	60,880
Supplies	364,185	362,967
Prepaid expenses and other	235,717	206,624
Total current assets	<u>3,338,221</u>	<u>3,017,244</u>
Noncurrent Cash and Investments		
Designated by board of trustees	216,746	150,878
Restricted by donors for capital acquisitions	535,258	532,508
Restricted by donors for specific operating activities	66,694	18,482
	<u>818,698</u>	<u>701,868</u>
Capital Assets, Net	<u>7,904,185</u>	<u>8,569,784</u>
Other Assets		
Employee receivables	<u>106,515</u>	<u>65,239</u>
Total assets	<u><u>\$ 12,167,619</u></u>	<u><u>\$ 12,354,135</u></u>

Liabilities and Net Position

	2017	2016 <i>(Restated)</i>
Current Liabilities		
Note payable to bank	\$ 784,438	\$ 390,015
Current maturities of long-term debt	235,573	254,196
Accounts payable	542,156	397,430
Accrued payroll	300,894	793,038
Accrued vacation	293,213	263,240
Other accrued expenses	418,967	282,925
Estimated amounts due to third-party payers	265,000	40,488
Deferred revenue	161,436	-
Total current liabilities	<u>3,001,677</u>	<u>2,421,332</u>
Long-Term Debt	<u>525,335</u>	<u>711,731</u>
Total liabilities	<u>3,527,012</u>	<u>3,133,063</u>
Net Position		
Net investment in capital assets	7,143,277	7,603,857
Restricted-expendable for		
Capital acquisitions	535,258	532,508
Specific operating activities	66,694	18,482
Unrestricted	<u>895,378</u>	<u>1,066,225</u>
Total net position	<u>8,640,607</u>	<u>9,221,072</u>
Total liabilities and net position	<u><u>\$ 12,167,619</u></u>	<u><u>\$ 12,354,135</u></u>

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2017 and 2016

	2017	2016
		<i>(Restated)</i>
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2017 - \$1,264,590; 2016 - \$847,188	\$ 19,629,217	\$ 18,653,523
Other	1,985,818	1,443,771
Total operating revenues	<u>21,615,035</u>	<u>20,097,294</u>
Operating Expenses		
Salaries and wages	12,732,621	11,833,354
Employee benefits	3,272,965	2,947,812
Purchased services and professional fees	1,409,885	1,255,991
Other supplies and expenses	5,264,118	4,846,347
Depreciation	1,366,848	1,439,473
Total operating expenses	<u>24,046,437</u>	<u>22,322,977</u>
Operating Loss	<u>(2,431,402)</u>	<u>(2,225,683)</u>
Nonoperating Revenues		
Noncapital appropriations - Kearny County	694,552	1,083,926
Interest income	12,597	10,081
Interest expense	(65,167)	(56,292)
Loss on sale of capital assets	(25,030)	(7,896)
Noncapital grants and gifts	379,630	212,312
Other	9,611	5,540
Total nonoperating revenues	<u>1,006,193</u>	<u>1,247,671</u>
Deficiency of Revenues Over Expenses		
Before Capital Grants and Gifts and Other	(1,425,209)	(978,012)
Capital Grants and Gifts	513,242	266,695
Other	<u>331,502</u>	<u>-</u>
Decrease in Net Position	(580,465)	(711,317)
Net Position, Beginning of Year	<u>9,221,072</u>	<u>9,932,389</u>
Net Position, End of Year	<u><u>\$ 8,640,607</u></u>	<u><u>\$ 9,221,072</u></u>

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Statements of Cash Flows
Years Ended June 30, 2017 and 2016

	2017	2016
		<i>(Restated)</i>
Operating Activities		
Receipts from and on behalf of patients	\$ 19,763,366	\$ 18,654,227
Payments to suppliers and contractors	(6,559,588)	(6,107,919)
Payments to employees	(16,064,227)	(15,121,355)
Other receipts, net	1,884,821	1,323,101
Net cash used in operating activities	<u>(975,628)</u>	<u>(1,251,946)</u>
Noncapital Financing Activities		
Noncapital appropriations - Kearny County	694,552	1,079,598
Noncapital grants and gifts	379,630	212,312
Other	9,611	5,540
Net cash provided by noncapital financing activities	<u>1,083,793</u>	<u>1,297,450</u>
Capital and Related Financing Activities		
Capital grants and gifts	513,242	6,500
Purchases of capital assets	(672,243)	(193,573)
Proceeds from sale of capital assets	2,753	-
Insurance proceeds	331,502	-
Proceeds from issuance of note payable to bank	11,368,847	9,757,540
Principal paid on note payable to bank	(10,974,424)	(9,766,930)
Proceeds from issuance of long-term debt	-	87,932
Principal paid on long-term debt	(261,808)	(242,692)
Interest paid on note payable to bank and long-term debt	(65,167)	(56,107)
Net cash provided by (used in) capital and related financing activities	<u>242,702</u>	<u>(407,330)</u>
Investing Activities		
Interest income received	12,597	10,081
Change in certificates of deposit	(2,750)	(1,727)
Advances to employees	(202,722)	31,639
Net cash provided by (used in) investing activities	<u>(192,875)</u>	<u>39,993</u>
Increase (Decrease) in Cash	157,992	(321,833)
Cash, Beginning of Year	<u>169,360</u>	<u>491,193</u>
Cash, End of Year	<u><u>\$ 327,352</u></u>	<u><u>\$ 169,360</u></u>

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Statements of Cash Flows (Continued)
Years Ended June 30, 2017 and 2016

	2017	2016
		<i>(Restated)</i>
Reconciliation of Cash to the Balance Sheets		
Cash	\$ 43,912	\$ -
Designated by board of trustees	216,746	150,878
Restricted by donors for specific operating activities	66,694	18,482
	<u>\$ 327,352</u>	<u>\$ 169,360</u>
Reconciliation of Operating Loss to		
Net Cash Used in Operating Activities		
Operating loss	\$ (2,431,402)	\$ (2,225,683)
Depreciation	1,366,848	1,439,473
Provision for uncollectible accounts	1,264,590	847,188
Forgiveness of employee receivables	106,052	51,639
Changes in operating assets and liabilities		
Patient accounts receivable	(1,354,953)	(1,419,865)
Estimated amounts due from and to third-party payers	224,512	573,381
Other receivables	(100,997)	(120,670)
Supplies	(1,218)	(5,825)
Prepaid expenses and other	(29,093)	122,955
Accounts payable and accrued expenses	(19,967)	(514,539)
Net cash used in operating activities	<u>\$ (975,628)</u>	<u>\$ (1,251,946)</u>
Noncash Investing, Capital and Financing Activities		
Capital lease obligations incurred for capital assets	\$ 56,789	\$ 983,189
Loss on sale of capital assets	\$ 25,030	\$ 7,896

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Notes to Financial Statements
June 30, 2017 and 2016

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

Nature of Operations and Reporting Entity

Kearny County Hospital (Hospital) is an acute care hospital located in Lakin, Kansas. The Hospital is a component unit of Kearny County (County), and governed by a Board of Trustees. The Board of County Commissioners appoints the members of the Board of Trustees. The Hospital primarily earns revenues by providing inpatient, outpatient, emergency care, long-term care and rural health clinic services to patients in the Kearny County area. The Hospital is licensed as a critical access hospital (CAH).

Kearney County Health Care Foundation (Foundation) is a legally separate, tax-exempt component unit of the Hospital. The Foundation's primary function is to raise and hold funds to support the Hospital and its programs. The board of the Foundation is substantially the same as the Hospital Board of Trustees. Although the Hospital does not control the timing or amount of receipts from the Foundation, the majority of the Foundation's resources and related income are for the benefit of the Hospital. Because these resources held by the Foundation can only be used by, or for the benefit of, the Hospital, the Foundation is considered to be a component unit of the Hospital and is presented in the Hospital's financial statements using the blending method. Separate financial statements of the Foundation are not available.

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, liabilities and deferred inflows and outflows of resources from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated or voluntary 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 or voluntary nonexchange 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 are 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, liabilities and deferred inflows and outflows of resources 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.

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Notes to Financial Statements
June 30, 2017 and 2016

Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents.

Noncapital Appropriations – Kearny County

The Hospital received approximately 3% and 5% in 2017 and 2016, respectively, of its financial support from proceeds of noncapital appropriations for property taxes.

Property taxes are levied in November of one year and are received beginning in January of the following year. Revenue from noncapital appropriations – Kearny County 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.

The Hospital is self-insured for a portion of its exposure to risk of loss from employee health claims. Annual estimated provisions are accrued for the self-insured portion of employee health claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Noncurrent Investments

Noncurrent investments include assets consisting of certificates of deposit restricted by donors for future capital acquisitions. The certificates of deposit are carried at amortized cost.

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 average cost method.

Kearny County Hospital
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Notes to Financial Statements
June 30, 2017 and 2016

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 – 20 years
Buildings	5 – 40 years
Equipment	5 – 20 years

Compensated Absences

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

Net Position

Net position of the Hospital is classified in three 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 purchase or construction of those assets. Restricted expendable net position is made up of noncapital assets that must be used for a particular purpose, as specified by creditors, grantors or donors external to the Hospital. Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets or restricted net position.

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.

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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 generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law.

The Foundation has been recognized as exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the Foundation is subject to federal income tax on any unrelated business taxable income. The Foundation files tax returns in the U.S. federal jurisdiction.

Electronic Health Records Incentive Program

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records (EHR) technology. CAHs are eligible to receive incentive payments in the cost reporting period beginning in the federal fiscal year in which meaningful use criteria have been met. The Medicare incentive payment is for qualifying costs of the purchase of certified EHR technology multiplied by the Hospital's Medicare share fraction, which includes a 20% incentive. This payment is an acceleration of amounts that would have been received in future periods based on reimbursable costs incurred, including depreciation. If meaningful use criteria are not met in future periods, the Hospital is subject to penalties that would reduce future payments for services. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. The final amount for any payment year under both programs is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Hospital has recognized the incentive payment revenue received for qualified EHR technology expenditures during the period which management was reasonably assured meaningful use was achieved and the earnings process was complete. Management believes the incentive payments reflect a change in how "allowable costs" are determined in paying CAHs for providing services to Medicare beneficiaries. The Hospital recorded revenue of \$4,767 and \$259,995, which is included in net patient service revenue in the statement of revenues, expenses and changes in position as of the years ended June 30, 2017 and 2016, respectively.

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Notes to Financial Statements
June 30, 2017 and 2016

Reclassifications

Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 presentation. The reclassifications had no effect on the changes in financial position.

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 CAH, and is paid for inpatient acute care, skilled, swing-bed and outpatient services rendered to Medicare program beneficiaries at one hundred one percent (101%) of actual cost subject to certain limitations. Medicare Rural Health Clinic services are reimbursed under a cost-based methodology. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor. Beginning April 1, 2013, a mandatory payment reduction, known as sequestration, of 2% went into effect. Under current legislation, sequestration is scheduled to last until 2023.

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. The Hospital is reimbursed at tentative rates with final settlements determined after submission of annual cost reports by the Hospital and reviews thereof by the Kansas Department of Health and Environment. Services rendered for long-term care facility residents are reimbursed at a prospective rate, with annual cost reports submitted to the Medicaid program. Through June 30, 2016, rates are computed using an average of the 2010, 2011 and 2012 cost reports. Rates are adjusted twice annually on July 1 and January 1 for changes in the Medicaid resident case mix index (CMI) using the simple average of the CMI from the two preceding quarters. The Medicaid cost reports are subject to audit by the state and adjustments to rates can be made retroactively. Effective July 1, 2016, rates are computed using an average of the 2013, 2014 and 2015 cost reports. Each year's cost data is inflation adjusted from the mid-point of that year to June 30, 2016. Effective for dates of service on or after July 1, 2016, the calculated per diem reimbursement will be reduced by 4.47% as part of cuts enacted to balance the Kansas State budget. Due to certain financial and clinical criteria, the Hospital also receives Medicaid Disproportionate Share (DSH) funding. DSH payments received were \$521,808 and \$543,552 in 2017 and 2016, respectively.

Kearny County Hospital
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June 30, 2017 and 2016

Approximately 53% and 55% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for years ended December 31, 2017 and 2016, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

Net patient service revenue consists of the following for the years ended June 30, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Gross patient service revenue	\$ 29,935,509	\$ 26,328,698
Less:		
Medicare contractual adjustments	2,221,778	1,094,851
Medicaid contractual adjustments	2,249,936	1,729,426
Blue Cross contractual adjustments	2,974,105	2,586,543
Other contractual adjustments and discounts	1,444,764	1,313,446
Charity care	151,119	103,721
Provision for uncollectible accounts	1,264,590	847,188
	<u>\$ 19,629,217</u>	<u>\$ 18,653,523</u>

Note 3: Deposits

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.

Kearny County Hospital
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June 30, 2017 and 2016

At June 30, 2017 and 2016, \$723,199 and \$554,188 of the Hospital's bank balances of \$973,199 and \$817,370, respectively, were exposed to custodial credit risk as follows:

	<u>2017</u>	<u>2016</u>
Uninsured and collateral held by pledging financial institution	<u>\$ 723,199</u>	<u>\$ 554,188</u>

Summary of Carrying Values

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

	<u>2017</u>	<u>2016</u>
Carrying value		
Deposits	\$ 327,352	\$ 169,360
Certificates of deposit	<u>535,258</u>	<u>532,508</u>
	<u>\$ 862,610</u>	<u>\$ 701,868</u>
Included in the following balance sheet captions		
Cash	\$ 43,912	\$ -
Designated by board of trustees	216,746	150,878
Restricted by donors for capital acquisitions	535,258	532,508
Restricted by donors for specific operating activities	<u>66,694</u>	<u>18,482</u>
	<u>\$ 862,610</u>	<u>\$ 701,868</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 consisted of:

	<u>2017</u>	<u>2016</u>
Medicare	\$ 483,840	\$ 705,104
Medicaid	469,179	413,612
Other third-party payers	895,871	522,912
Patients	<u>865,774</u>	<u>928,470</u>
	2,714,664	2,570,098
Less allowance for uncollectible accounts	<u>367,306</u>	<u>313,103</u>
	<u>\$ 2,347,358</u>	<u>\$ 2,256,995</u>

Kearny County Hospital
A Component Unit of Kearny County, Kansas
Notes to Financial Statements
June 30, 2017 and 2016

Note 5: Capital Assets

Capital assets activity for the years ended June 30 was:

2017					
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 97,298	\$ -	\$ -	\$ -	\$ 97,298
Land improvements	634,019	-	-	-	634,019
Buildings	17,739,029	-	(32,858)	571,198	18,277,369
Equipment	6,599,918	171,918	(671,914)	3,916	6,103,838
Construction in progress	18,000	557,114	-	(575,114)	-
	<u>25,088,264</u>	<u>729,032</u>	<u>(704,772)</u>	<u>-</u>	<u>25,112,524</u>
Less accumulated depreciation					
Land improvements	459,724	30,798	-	-	490,522
Buildings	11,605,806	758,798	(6,138)	-	12,358,466
Equipment	4,452,950	577,252	(670,851)	-	4,359,351
	<u>16,518,480</u>	<u>1,366,848</u>	<u>(676,989)</u>	<u>-</u>	<u>17,208,339</u>
Capital assets, net	<u>\$ 8,569,784</u>	<u>\$ (637,816)</u>	<u>\$ (27,783)</u>	<u>\$ -</u>	<u>\$ 7,904,185</u>

2016					
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 97,298	\$ -	\$ -	\$ -	\$ 97,298
Land improvements	634,019	-	-	-	634,019
Buildings	17,221,885	37,222	-	479,922	17,739,029
Equipment	6,722,495	1,352,239	(1,474,816)	-	6,599,918
Construction in progress	497,922	-	-	(479,922)	18,000
	<u>25,173,619</u>	<u>1,389,461</u>	<u>(1,474,816)</u>	<u>-</u>	<u>25,088,264</u>
Less accumulated depreciation					
Land improvements	428,291	31,433	-	-	459,724
Buildings	10,792,533	874,320	(61,047)	-	11,605,806
Equipment	5,325,103	533,720	(1,405,873)	-	4,452,950
	<u>16,545,927</u>	<u>1,439,473</u>	<u>(1,466,920)</u>	<u>-</u>	<u>16,518,480</u>
Capital assets, net	<u>\$ 8,627,692</u>	<u>\$ (50,012)</u>	<u>\$ (7,896)</u>	<u>\$ -</u>	<u>\$ 8,569,784</u>

Kearny County Hospital
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Notes to Financial Statements
June 30, 2017 and 2016

Note 6: Medical Malpractice Coverage and Claims

The Hospital purchases medical malpractice insurance 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 near term.

Note 7: Employee Health Claims

Substantially all of the Hospital's employees and their dependents are eligible to participate in the Hospital's employee health insurance plan. The Hospital is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$35,000. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Hospital's estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability during 2017 and 2016 is summarized as follows:

	2017	2016
Balance, beginning of year	\$ 182,620	\$ 182,686
Current year claims incurred and changes in estimates for claims incurred in prior years	1,854,148	1,533,636
Claims and expenses paid	<u>(1,854,148)</u>	<u>(1,533,702)</u>
	<u><u>\$ 182,620</u></u>	<u><u>\$ 182,620</u></u>

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Note 8: Note Payable to Bank

The Hospital has a revolving line of credit agreement with a local bank. The maximum principal that can be borrowed is \$1,000,000, and the line of credit carries an interest rate of 3%. Interest is payable monthly. The line of credit is collateralized by patient accounts receivable. At June 30, 2017 and 2016, there were outstanding borrowings against the line of credit of \$284,438 and \$390,015, respectively. The line of credit expires March 2, 2018. Management intends to renew the line of credit on comparable terms at or near the maturity date and believes it is probable such renewal will be successful.

The Hospital has a bulge line of credit agreement with a local bank. The maximum principal that can be borrowed is \$500,000, and the line of credit carries an interest rate of 3.5%. Interest is payable monthly. The line of credit is collateralized by patient accounts receivable. At June 30, 2017 and 2016, there were outstanding borrowings against the line of credit of \$500,000 and \$0, respectively. The line of credit expires December 5, 2017. Management intends to pay off the line of credit at the maturity date.

Note 9: Long-Term Obligations

The following is a summary of long-term obligation transactions for the Hospital for the years ended June 30:

2017					
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Note payable to bank	\$ 50,982	\$ -	\$ 50,982	\$ -	\$ -
Capital lease obligations	914,945	56,789	210,826	760,908	235,573
	<u>\$ 965,927</u>	<u>\$ 56,789</u>	<u>\$ 261,808</u>	<u>\$ 760,908</u>	<u>\$ 235,573</u>
2016					
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Note payable to bank	\$ 55,558	\$ 87,932	\$ 92,508	\$ 50,982	\$ 50,982
Capital lease obligations	81,940	983,189	150,184	914,945	203,214
	<u>\$ 137,498</u>	<u>\$ 1,071,121</u>	<u>\$ 242,692</u>	<u>\$ 965,927</u>	<u>\$ 254,196</u>

Note Payable to Bank

The note payable to bank is due June 30, 2018, with principal payable monthly and interest at 3% payable monthly. The note is secured by certain capital assets. The Hospital made additional principal payments in 2016 and fully retired the obligation in 2017 prior to the stated maturity date.

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Capital Lease Obligations

The Hospital is obligated under leases for equipment that are accounted for as capital leases. Assets under capital leases at June 30, 2017 and 2016, totaled \$1,085,894 and \$1,113,943, respectively, net of accumulated depreciation of \$395,840 and \$421,959, respectively. The following is a schedule by year of future minimum lease payments under the capital lease including interest at rates of 1.11% to 14.29% together with the present value of the future minimum lease payments as June 30, 2017:

Year Ending June 30,	
2018	\$ 265,300
2019	235,010
2020	200,905
2021	113,858
2022	<u>11,254</u>
Total minimum lease payments	826,327
Less amounts representing interest	<u>65,419</u>
	<u><u>\$ 760,908</u></u>

Note 10: Pension Plan

The Hospital maintains a contributory pension plan covering substantially all employees in lieu of social security. Prior to July 1, 1997, employees made contributions equal to 5% of their gross compensation. The Hospital contribution was 10% of the employees' gross compensation for those employed for two years or more and 5% for all others. Effective July 1, 1997, employees are required to contribute the same percentage required under the Social Security laws (OASDI). The Hospital is required to make a matching contribution in the same amount. An additional 3% contribution is made by the Hospital on behalf of all employees continuously employed for three years or more. Voluntary employee contributions may be made up to a specified percent of eligible compensation as specified in the plan document. Employee and employer contributions vest immediately. Benefits are funded by an annuity contract with an insurance company. The total cost of the plan was \$991,825 and \$939,128 for 2017 and 2016, respectively.

Note 11: 340B Drug Pricing Program

The Hospital participates in the 340B Drug Pricing Program (340B Program) enabling the Hospital to receive discounted prices from drug manufactures on outpatient pharmaceutical purchases. The Hospital recorded revenues of \$1,641,817 and \$1,184,471 for the years ended June 30, 2017 and 2016, respectively, which is included in other operating revenues in the accompanying statements of revenues, expenses and changes in net position. The Hospital recorded expenses of \$399,362

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and \$291,906 for the years ended June 30, 2017 and 2016, respectively, which is included in supplies and other expenses in the accompanying statements of revenues, expenses and changes in net position. This program is overseen by the Health Resources and Services Administration (HRSA) Office of Pharmacy Affairs (OPA). HRSA is currently conducting routine audits of this program at health care organizations and increasing its compliance monitoring processes. Laws and regulations governing the 340B Program are complex and subject to interpretation and change. As a result, it is reasonably possible that material changes to financial statement amounts related to the 340B Program could occur in the near term.

Note 12: Condensed Combining Information

The following tables include condensed combining balance sheet information for the Hospital and its blended component unit as of June 30, 2017 and 2016:

	June 30, 2017			
	Hospital	Foundation	Eliminations	Total
Assets				
Current assets	\$ 3,338,221	\$ -	\$ -	\$ 3,338,221
Noncurrent cash and investments	722,163	96,535	-	818,698
Capital assets, net	7,904,185	-	-	7,904,185
Other assets	106,515	-	-	106,515
Total assets	<u>\$ 12,071,084</u>	<u>\$ 96,535</u>	<u>\$ -</u>	<u>\$ 12,167,619</u>
Liabilities				
Current liabilities	\$ 3,001,677	\$ -	\$ -	\$ 3,001,677
Noncurrent liabilities	525,335	-	-	525,335
Total liabilities	<u>3,527,012</u>	<u>-</u>	<u>-</u>	<u>3,527,012</u>
Net Position				
Net investments in capital assets	7,143,277	-	-	7,143,277
Restricted expendable	505,417	96,535	-	601,952
Unrestricted	895,378	-	-	895,378
Total net position	<u>8,544,072</u>	<u>96,535</u>	<u>-</u>	<u>8,640,607</u>
Total liabilities and net position	<u>\$ 12,071,084</u>	<u>\$ 96,535</u>	<u>\$ -</u>	<u>\$ 12,167,619</u>

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	June 30, 2016			
	Hospital	Foundation	Eliminations	Total
	<i>(Restated)</i>			
Assets				
Current assets	\$ 3,017,244	\$ -	\$ -	\$ 3,017,244
Noncurrent cash and investments	655,897	45,971	-	701,868
Capital assets, net	8,569,784	-	-	8,569,784
Other assets	65,239	-	-	65,239
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total assets	<u>\$ 12,308,164</u>	<u>\$ 45,971</u>	<u>\$ -</u>	<u>\$ 12,354,135</u>
Liabilities				
Current liabilities	\$ 2,421,332	\$ -	\$ -	\$ 2,421,332
Noncurrent liabilities	711,731	-	-	711,731
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total liabilities	<u>3,133,063</u>	<u>-</u>	<u>-</u>	<u>3,133,063</u>
Net Position				
Net investments in capital assets	7,603,857	-	-	7,603,857
Restricted expendable	505,019	45,971	-	550,990
Unrestricted	1,066,225	-	-	1,066,225
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total net position	<u>9,175,101</u>	<u>45,971</u>	<u>-</u>	<u>9,221,072</u>
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total liabilities and net position	<u>\$ 12,308,164</u>	<u>\$ 45,971</u>	<u>\$ -</u>	<u>\$ 12,354,135</u>

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The following tables include condensed combining statements of revenues, expenses and change in net position information for the Hospital and its blended component unit for the years ended June 30, 2017 and 2016:

	June 30, 2017			
	Hospital	Foundation	Eliminations	Total
Operating Revenues				
Net patient service revenue	\$ 19,629,217	\$ -	\$ -	\$ 19,629,217
Other	1,985,818	-	-	1,985,818
Total operating revenues	21,615,035	-	-	21,615,035
Operating Expenses				
Other operating expenses	22,661,793	17,796	-	22,679,589
Depreciation	1,366,848	-	-	1,366,848
Total operating expenses	24,028,641	17,796	-	24,046,437
Operating Loss	(2,413,606)	(17,796)	-	(2,431,402)
Nonoperating Revenues (Expenses)				
Noncapital appropriations -				
Kearny County	694,552	-	-	694,552
Interest income	12,229	368	-	12,597
Interest expense	(65,167)	-	-	(65,167)
Loss on sale of capital assets	(25,030)	-	-	(25,030)
Noncapital grants and gifts	297,511	82,119	-	379,630
Other	-	9,611	-	9,611
Transfers	303,202	(303,202)	-	-
Total nonoperating revenues	1,217,297	(211,104)	-	1,006,193
Deficiency of Revenues				
Over Expenses Before Capital Grants and Gifts and Other	(1,196,309)	(228,900)	-	(1,425,209)
Capital Grants and Gifts	233,778	279,464	-	513,242
Other	331,502	-	-	331,502
Increase (Decrease) in Net Position	(631,029)	50,564	-	(580,465)
Net Position, Beginning of Year	9,175,101	45,971	-	9,221,072
Net Position, End of Year	<u>\$ 8,544,072</u>	<u>\$ 96,535</u>	<u>\$ -</u>	<u>\$ 8,640,607</u>

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	June 30, 2016			
	Hospital	Foundation	Eliminations	Total
	<i>(Restated)</i>			
Operating Revenues				
Net patient service revenue	\$ 18,653,523	\$ -	\$ -	\$ 18,653,523
Other	1,443,771	-	-	1,443,771
Total operating revenues	20,097,294	-	-	20,097,294
Operating Expenses				
Other operating expenses	20,880,041	3,463	-	20,883,504
Depreciation	1,439,473	-	-	1,439,473
Total operating expenses	22,319,514	3,463	-	22,322,977
Operating Loss	(2,222,220)	(3,463)	-	(2,225,683)
Nonoperating Revenues (Expenses)				
Noncapital appropriations -				
Kearny County	1,083,926	-	-	1,083,926
Interest income	9,993	88	-	10,081
Interest expense	(56,292)	-	-	(56,292)
Loss on sale of capital assets	(7,896)	-	-	(7,896)
Noncapital grants and gifts	200,239	12,073	-	212,312
Other	-	5,540	-	5,540
Transfers	20,330	(20,330)	-	-
Total nonoperating revenues	1,250,300	(2,629)	-	1,247,671
Deficiency of Revenues				
Over Expenses Before Capital				
Grants and Gifts and Other	(971,920)	(6,092)	-	(978,012)
Capital Grants and Gifts	266,695	-	-	266,695
Other	-	-	-	-
Decrease in Net Position	(705,225)	(6,092)	-	(711,317)
Net Position, Beginning of Year	9,880,326	52,063	-	9,932,389
Net Position, End of Year	<u>\$ 9,175,101</u>	<u>\$ 45,971</u>	<u>\$ -</u>	<u>\$ 9,221,072</u>

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The following tables include condensed combining statements of cash flows information for the Hospital and its blended component unit for the years ended June 30, 2017 and 2016:

	June 30, 2017			
	Hospital	Foundation	Eliminations	Total
Net Cash Used In				
Operating Activities	\$ (957,832)	\$ (17,796)	\$ -	\$ (975,628)
Net Cash Provided By (Used In)				
Noncapital Financing Activities	1,295,265	(211,472)	-	1,083,793
Net Cash Provided By (Used In)				
Capital and Related Financing Activities	(36,762)	279,464	-	242,702
Net Cash Provided By (Used In)				
Investing Activities	(193,243)	368	-	(192,875)
Increase in Cash	107,428	50,564	-	157,992
Cash, Beginning of Year	123,389	45,971	-	169,360
Cash, End of Year	<u>\$ 230,817</u>	<u>\$ 96,535</u>	<u>\$ -</u>	<u>\$ 327,352</u>

	June 30, 2016			
	Hospital	Foundation	Eliminations	Total
	<i>(Restated)</i>			
Net Cash Used In				
Operating Activities	\$ (1,248,483)	\$ (3,463)	\$ -	\$ (1,251,946)
Net Cash Provided By (Used In)				
Noncapital Financing Activities	1,300,167	(2,717)	-	1,297,450
Net Cash Provided By (Used In)				
Capital and Related Financing Activities	(407,330)	-	-	(407,330)
Net Cash Provided By				
Investing Activities	39,905	88	-	39,993
Decrease in Cash	(315,741)	(6,092)	-	(321,833)
Cash, Beginning of Year	439,130	52,063	-	491,193
Cash, End of Year	<u>\$ 123,389</u>	<u>\$ 45,971</u>	<u>\$ -</u>	<u>\$ 169,360</u>

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Note 13: Contingencies

Litigation

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Hospital's self-insurance program (discussed elsewhere in these notes) or by commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Hospital evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

Note 14: Restatement of Prior Year Financial Statements

Certain material reclassifications have been made to the 2016 financial statements. These material reclassifications are considered to be error corrections and thus the 2016 financial statements have been restated to correct these misstatements. The material reclassifications had no effect on the changes in financial position.

The table below reflects the financial statement line items affected by the 2016 material reclassifications as well as disaggregation of certain operating expenses.

	As Restated	As Previously Reported	Effect of Change
Balance Sheet			
Assets whose use is limited	\$ -	\$ 701,868	\$ (701,868)
Patient accounts receivable, net of allowance	2,256,995	2,394,309	(137,314)
Other receivables	129,778	-	129,778
Prepaid expenses and other	206,624	198,216	8,408
Total current assets	3,017,244	3,718,240	(700,996)
Designated by board of trustees	150,878	-	150,878
Restricted by donors for capital acquisitions	532,508	-	532,508
Restricted by donors for specific operating	18,482	-	18,482
Total noncurrent cash and investments	701,868	-	701,868
Capital assets, net	8,569,784	8,570,664	(880)

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	As Restated	As Previously Reported	Effect of Change
Statement of Revenues, Expenses and Changes in Net Position			
Net patient service revenue, net of provision for uncollectible accounts	\$ 18,653,523	\$ 18,399,191	\$ 254,332
Other	1,443,771	776,277	667,494
Total operating revenues	20,097,294	19,175,468	921,826
Employee benefits	2,947,812	-	2,947,812
Purchased services and professional fees	1,255,991	-	1,255,991
Other supplies and expenses	4,846,347	8,377,116	(3,530,769)
Total operating expenses	22,322,977	21,649,943	673,034
Operating loss	(2,225,683)	(2,474,475)	248,792
Other nonoperating revenues	5,540	254,332	(248,792)
Total nonoperating revenues	1,247,671	1,496,463	(248,792)
Statement of Cash Flows			
Receipts from and on behalf of patients	18,654,227	18,286,776	367,451
Payments to suppliers and contractors	(6,107,919)	(8,389,864)	2,281,945
Payments to employees	(15,121,355)	(11,730,113)	(3,391,242)
Other receipts, net	1,323,101	752,500	570,601
Net cash used in operating activities	(1,251,946)	(1,080,701)	(171,245)
Noncapital appropriations - Kearny County	1,079,598	908,353	171,245
Net cash provided by noncapital financing activities	1,297,450	1,126,205	171,245
Change in certificates of deposit	(1,727)	-	(1,727)
Cash, Beginning of Year	491,193	1,021,974	(530,781)
Cash, End of Year	169,360	701,868	(532,508)