

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
Independent Auditor's Report and Financial Statements  
March 31, 2017 and 2016



**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**March 31, 2017 and 2016**

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## Independent Auditor's Report

Board of Trustees  
Phillips County Health Systems  
Phillipsburg, Kansas

We have audited the accompanying financial statements of Phillips County Health Systems (PCHS), a component unit of Phillips County, Kansas, as of and for the years ended March 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise PCHS'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 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 Phillips County Health Systems as of March 31, 2017 and 2016, 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 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  
September 11, 2017

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Balance Sheets**  
**March 31, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
<b>Assets</b>		
<b>Current Assets</b>		
Cash	\$ 1,105,658	\$ 439,082
Patient accounts receivable, net of allowance; 2017 – \$427,561, 2016 – \$441,476	1,721,292	1,582,359
Estimated amounts due from third-party payers	77,333	-
Supplies	187,296	179,373
Prepaid expenses and other	<u>95,986</u>	<u>95,694</u>
Total current assets	<u>3,187,565</u>	<u>2,296,508</u>
 <b>Noncurrent Cash and Investments</b>		
Restricted by donors for specific operating activities	258,691	124,836
Certificate of deposit	<u>9,500</u>	<u>9,500</u>
	<u>268,191</u>	<u>134,336</u>
 <b>Capital Assets, Net</b>	<u>1,518,031</u>	<u>1,540,299</u>
 <b>Scholarships Receivable</b>	<u>44,348</u>	<u>40,015</u>
Total assets	<u><u>\$ 5,018,135</u></u>	<u><u>\$ 4,011,158</u></u>

	2017	2016
<b>Liabilities and Net Position</b>		
<b>Current Liabilities</b>		
Current maturities of long-term debt	\$ 78,577	\$ 88,457
Accounts payable	1,264,905	295,840
Accrued salaries and wages	332,414	340,905
Accrued payroll taxes and other	264,970	387,822
Accrued benefits payable	393,104	439,668
Estimated amounts due to third-party payers	345,000	30,000
Total current liabilities	2,678,970	1,582,692
<b>Long-term Debt</b>	273,109	260,673
Total liabilities	2,952,079	1,843,365
<b>Net Position</b>		
Net investment in capital assets	1,166,345	1,191,169
Restricted - expendable for specific operating activities	258,691	124,836
Unrestricted	641,020	851,788
Total net position	2,066,056	2,167,793
Total liabilities and net position	\$ 5,018,135	\$ 4,011,158

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**Years Ended March 31, 2017 and 2016**

	<b>2017</b>	<b>2016</b>
<b>Operating Revenues</b>		
Net patient service revenue, net of provision for uncollectible accounts; 2017 - \$96,472, 2016 - \$226,756	\$ 10,844,414	\$ 10,740,462
Other	1,260,240	1,414,960
Total operating revenues	12,104,654	12,155,422
<b>Operating Expenses</b>		
Salaries and wages	5,683,203	5,615,290
Supplies and other	6,958,651	7,309,697
Depreciation	265,320	353,938
Total operating expenses	12,907,174	13,278,925
<b>Operating Loss</b>	(802,520)	(1,123,503)
<b>Nonoperating Revenues (Expenses)</b>		
Noncapital appropriations - Phillips County	367,992	356,129
Noncapital grants and gifts	356,613	247,933
Interest income	12,421	11,211
Interest expense	(36,243)	(57,301)
Total nonoperating revenues	700,783	557,972
<b>Deficiency of Revenues Over Expenses Before Capital Grants and Gifts and Special Item</b>	(101,737)	(565,531)
<b>Capital Grants and Gifts</b>	-	84,200
<b>Special Item</b>		
Termination of lease agreement ( <i>Notes 1 and 12</i> )	-	2,023,891
<b>Increase (Decrease) in Net Position</b>	(101,737)	1,542,560
<b>Net Position, Beginning of Year</b>	2,167,793	625,233
<b>Net Position, End of Year</b>	\$ 2,066,056	\$ 2,167,793

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Statements of Cash Flows**  
**Years Ended March 31, 2017 and 2016**

	<b>2017</b>	<b>2016</b>
<b>Operating Activities</b>		
Receipts from and on behalf of patients	\$ 10,943,148	\$ 10,802,773
Payments to suppliers	(6,054,517)	(7,514,887)
Payments to employees	(5,861,110)	(5,284,068)
Other receipts, net	1,254,931	1,352,932
	<u>282,452</u>	<u>(643,250)</u>
Net cash provided by (used in) operating activities		
<b>Noncapital Financing Activities</b>		
Noncapital appropriations - Phillips County	367,992	356,129
Noncapital grants and gifts	356,613	247,933
	<u>724,605</u>	<u>604,062</u>
Net cash provided by noncapital financing activities		
<b>Capital and Related Financing Activities</b>		
Capital grants and gifts	-	84,200
Principal paid on long-term debt	(95,744)	(193,895)
Interest paid on long-term debt	(36,243)	(57,301)
Purchases of capital assets	(91,845)	(203,290)
Proceeds from disposal of capital assets	4,785	-
Cash received on termination of lease agreement	-	316,445
	<u>(219,047)</u>	<u>(53,841)</u>
Net cash used in capital and related financing activities		
<b>Investing Activities</b>		
Interest income	12,421	11,211
Proceeds from disposition of investments	-	225,128
	<u>12,421</u>	<u>236,339</u>
Net cash provided by investing activities		
<b>Increase in Cash</b>	800,431	143,310
<b>Cash, Beginning of Year</b>	<u>563,918</u>	<u>420,608</u>
<b>Cash, End of Year</b>	<u>\$ 1,364,349</u>	<u>\$ 563,918</u>



**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Statements of Cash Flows (Continued)**  
**Years Ended March 31, 2017 and 2016**

	<b>2017</b>	<b>2016</b>
<b>Reconciliation of Cash to the Balance Sheets</b>		
Cash in current assets	\$ 1,105,658	\$ 439,082
Cash in noncurrent cash	258,691	124,836
	<u>\$ 1,364,349</u>	<u>\$ 563,918</u>
<b>Reconciliation of Operating Loss to Net Cash Provided By (Used In) Operating Activities</b>		
Operating loss	\$ (802,520)	\$ (1,123,503)
Depreciation	265,320	353,938
Gain on disposal of capital assets	(684)	-
Provision for uncollectible accounts	96,472	226,756
Changes in operating assets and liabilities		
Patient accounts receivable, net	(235,405)	(599,445)
Estimated amounts due from and to third-party payers	237,667	435,000
Supplies	(7,923)	68,315
Prepaid expenses and other	(4,625)	(62,028)
Accounts payable and accrued expenses	734,150	57,717
	<u>\$ 282,452</u>	<u>\$ (643,250)</u>
<b>Supplemental Cash Flows Information</b>		
Capital lease obligations incurred for capital assets	\$ 98,300	\$ 59,657
Capital asset purchases included in accounts payable	\$ 59,439	\$ 2,431
As discussed in <i>Notes 1 and 12</i> , effective April 1, 2015, the Board of Trustees terminated its lease agreement with Great Plains of Phillips County, Inc. In conjunction with the termination of the lease agreement, assets, liabilities and net position were transferred as follows:		
Assets	\$ -	\$ 3,911,346
Liabilities	<u>-</u>	<u>(1,887,455)</u>
Net position	<u>\$ -</u>	<u>\$ 2,023,891</u>

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Notes to Financial Statements**  
**March 31, 2017 and 2016**

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

***Nature of Operations***

Phillips County Hospital d/b/a Phillips County Health Systems (PCHS) provides acute care, swing-bed and clinic services in the Phillipsburg, Kansas area. PCHS is a component unit of Phillips County, Kansas (County) and the Board of County Commissioners appoints members to the Board of Trustees (BOT) of PCHS.

Prior to April 1, 2015, the BOT of PCHS leased the hospital facilities, including buildings, as well as equipment and other assets, to Great Plains of Phillips County, Inc. (GPPC) for one dollar. Great Plains Health Alliance, Inc. (GPHA) is the sole member of GPPC. The lease agreement provided that GPPC would assume and continue the operations of the hospital and maintain all property and equipment in good operating condition. All assets, including working capital and liabilities were transferred to GPPC upon commencement of the original term, January 8, 2001. During the term of the lease agreement, the BOT continued to operate and control the use of tax appropriations and separate financial statements were issued for the BOT. Either party had the option to terminate the lease at any time for a material breach of terms or provisions of the agreement with a 90-day notice. The BOT elected to terminate the lease agreement effective April 1, 2015. Effective with the termination of the lease agreement, all assets, including working capital and liabilities, transferred back to PCHS (see *Note 12*).

***Basis of Accounting and Presentation***

The financial statements of PCHS 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 (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), property taxes, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. PCHS first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position are available.

**Phillips County Health Systems**  
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**Notes to Financial Statements**  
**March 31, 2017 and 2016**

***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 and Cash Equivalents***

PCHS considers all liquid investments with original maturities of three months or less to be cash equivalents. There were no cash equivalents at March 31, 2017 and 2016.

***Noncurrent Cash and Investments***

Noncurrent cash and investments include assets restricted by donors for specific operating activities and a certificate of deposit carried at amortized cost. Noncurrent cash consists primarily of money market accounts.

***Noncapital Appropriations – Phillips County***

PCHS received approximately 3% of its financial support from noncapital appropriations from the County property tax levy in 2017 and 2016. These funds were used to support operations.

Property taxes are assessed in November and are received beginning in January of the following year. Noncapital appropriations revenue from property taxes is recognized in full in the year in which use is first permitted.

***Risk Management***

PCHS 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 other than employee health and dental claims. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

***Patient Accounts Receivable***

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

**Phillips County Health Systems**  
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**Notes to Financial Statements**  
**March 31, 2017 and 2016**

***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 PCHS:

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

***Compensated Absences***

PCHS policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off. Expense and the related liability are recognized as vacation benefits are earned. 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. Accrued benefits payable are computed using the regular pay rates in effect at the balance sheet date.

***Net Position***

Net position of PCHS 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 PCHS. 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***

PCHS has agreements with third-party payers that provide for payments to PCHS 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 include estimated retroactive revenue adjustments. 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.

**Phillips County Health Systems**  
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**Notes to Financial Statements**  
**March 31, 2017 and 2016**

**Charity Care**

PCHS provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because PCHS 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, PCHS 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, PCHS is subject to federal income tax on any unrelated business taxable income.

**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. Critical access hospitals (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 PCHS'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, PCHS 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.

PCHS recorded revenue under the Medicaid EHR program of \$18,543 and \$27,814, which is included in net patient service revenue in the statement of revenues, expenses and changes in net position for the years ended March 31, 2017 and 2016, respectively.

**Reclassifications**

Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 financial statement presentation. These reclassifications had no effect on the change in net position.

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Notes to Financial Statements**  
**March 31, 2017 and 2016**

**Note 2: Net Patient Service Revenue**

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

*Medicare.* PCHS is recognized as a CAH. Under CAH rules, inpatient acute care, skilled swing-bed and outpatient services rendered to Medicare program beneficiaries are paid at one hundred one percent (101%) of allowable cost subject to certain limitations. Other outpatient services related to Medicare beneficiaries are paid based on a combination of fee schedules and cost reimbursement methodologies. PCHS is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by PCHS 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 2025.

*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. PCHS is reimbursed at tentative rates with final settlements determined after submission of annual cost reports by PCHS and reviews thereof by the Kansas Department of Health and Environment.

Approximately 72% and 73% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended March 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.

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

**Phillips County Health Systems**  
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**Notes to Financial Statements**  
**March 31, 2017 and 2016**

Net patient service revenue consists of the following for the years ending March 31, 2017 and 2016:

	<b>2017</b>	<b>2016</b>
Gross patient service revenue	\$ 11,660,655	\$ 11,507,012
Contractual adjustments		
Medicare	195,848	412,283
Medicaid	(182,557)	(244,936)
Blue Cross	(384,105)	(378,158)
Other	(247,092)	(195,801)
Administrative adjustments	(39,185)	(43,664)
Charity care	(62,678)	(89,518)
Provision for uncollectible accounts	(96,472)	(226,756)
	<u>\$ 10,844,414</u>	<u>\$ 10,740,462</u>

**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. PCHS'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 March 31, 2017 and 2016, respectively, \$897,469 and \$404,023 of PCHS's bank balances of \$1,377,682 and \$654,023 were exposed to custodial credit risk as follows:

	<b>2017</b>	<b>2016</b>
Uninsured and uncollateralized	\$ 301,661	\$ -
Uninsured and collateral held by pledging financial institution	<u>595,808</u>	<u>404,023</u>
	<u>\$ 897,469</u>	<u>\$ 404,023</u>

**Phillips County Health Systems**  
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**Notes to Financial Statements**  
**March 31, 2017 and 2016**

**Summary of Carrying Values**

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

	<u><b>2017</b></u>	<u><b>2016</b></u>
Carrying value		
Cash	\$ 1,364,349	\$ 563,918
Certificates of deposit	<u>9,500</u>	<u>9,500</u>
	<u><u>\$ 1,373,849</u></u>	<u><u>\$ 573,418</u></u>
Included in the following balance sheet captions		
Cash	\$ 1,105,658	\$ 439,082
Certificates of deposit	<u>9,500</u>	<u>9,500</u>
Noncurrent cash	<u>258,691</u>	<u>124,836</u>
	<u><u>\$ 1,373,849</u></u>	<u><u>\$ 573,418</u></u>

**Note 4: Patient Accounts Receivable**

PCHS grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at March 31 consisted of:

	<u><b>2017</b></u>	<u><b>2016</b></u>
Medicare	\$ 1,026,071	\$ 1,054,723
Medicaid	10,367	11,793
Blue Cross	271,673	116,560
Other third-party payers	211,465	260,175
Self-pay	<u>629,277</u>	<u>580,584</u>
	2,148,853	2,023,835
Less allowance for uncollectible accounts	<u>(427,561)</u>	<u>(441,476)</u>
	<u><u>\$ 1,721,292</u></u>	<u><u>\$ 1,582,359</u></u>



**Phillips County Health Systems**  
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**Notes to Financial Statements**  
**March 31, 2017 and 2016**

**Note 5: Capital Assets**

Capital assets activity for the years ended March 31 was:

<b>2017</b>						
	<b>Beginning Balance</b>	<b>Termination of Lease</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Land	\$ 48,100	\$ -	\$ -	\$ -		\$ 48,100
Land improvements	107,381	-	-	-		107,381
Buildings	3,715,772	-	7,409	(32,505)		3,690,676
Fixed equipment	2,417,142	-	29,421	(264,835)	64,933	2,246,661
Major moveable equipment	2,778,756	-	159,913	(272,854)		2,665,815
Construction in progress	123,814	-	50,410	-	(64,933)	109,291
	<u>9,190,965</u>	<u>-</u>	<u>247,153</u>	<u>(570,194)</u>	<u>-</u>	<u>8,867,924</u>
Less accumulated depreciation						
Land improvements	106,331	-	407	-	-	106,738
Buildings	2,848,714	-	121,921	(28,612)	-	2,942,023
Fixed equipment	2,287,189	-	36,492	(264,834)	-	2,058,847
Major moveable equipment	2,408,432	-	106,500	(272,647)	-	2,242,285
	<u>7,650,666</u>	<u>-</u>	<u>265,320</u>	<u>(566,093)</u>	<u>-</u>	<u>7,349,893</u>
Capital Assets, Net	<u>\$ 1,540,299</u>	<u>\$ -</u>	<u>\$ (18,167)</u>	<u>\$ (4,101)</u>	<u>\$ -</u>	<u>\$ 1,518,031</u>

  

<b>2016</b>						
	<b>Beginning Balance</b>	<b>Termination of Lease</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Land	\$ -	\$ 48,100	\$ -	\$ -	\$ -	\$ 48,100
Land improvements	-	107,381	-	-	-	107,381
Buildings	-	3,644,268	71,504	-	-	3,715,772
Fixed equipment	-	2,417,142	-	-	-	2,417,142
Major moveable equipment	-	2,627,078	169,551	(17,873)	-	2,778,756
Construction in progress	-	99,491	24,323	-	-	123,814
	<u>-</u>	<u>8,943,460</u>	<u>265,378</u>	<u>(17,873)</u>	<u>-</u>	<u>9,190,965</u>
Less accumulated depreciation						
Land improvements	-	105,790	541	-	-	106,331
Buildings	-	2,719,397	129,317	-	-	2,848,714
Fixed equipment	-	2,251,831	35,358	-	-	2,287,189
Major moveable equipment	-	2,237,583	188,722	(17,873)	-	2,408,432
	<u>-</u>	<u>7,314,601</u>	<u>353,938</u>	<u>(17,873)</u>	<u>-</u>	<u>7,650,666</u>
Capital Assets, Net	<u>\$ -</u>	<u>\$ 1,628,859</u>	<u>\$ (88,560)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,540,299</u>

**Phillips County Health Systems**  
**A Component Unit of Phillips County, Kansas**  
**Notes to Financial Statements**  
**March 31, 2017 and 2016**

**Note 6: Medical Malpractice Claims**

PCHS purchases medical malpractice insurance under a claims-made (or occurrence-basis) 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 PCHS'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: Long-term Debt**

The following is a summary of long-term debt transactions for PCHS for the years ended March 31:

<b>2017</b>						
	<b>Beginning Balance</b>	<b>Termination of Lease</b>	<b>Additions</b>	<b>Deductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Note payable	\$ 119,047	\$ -	\$ -	\$ (6,925)	\$ 112,122	\$ 7,203
Capital lease obligations	230,083	-	98,300	(88,819)	239,564	71,374
	<u>\$ 349,130</u>	<u>\$ -</u>	<u>\$ 98,300</u>	<u>\$ (95,744)</u>	<u>\$ 351,686</u>	<u>\$ 78,577</u>
<b>2016</b>						
	<b>Beginning Balance</b>	<b>Termination of Lease</b>	<b>Additions</b>	<b>Deductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Revenue bonds	\$ -	\$ 28,572	\$ -	\$ (28,572)	\$ -	\$ -
Note payable	-	125,705	-	(6,658)	119,047	6,925
Capital lease obligations	-	329,091	59,657	(158,665)	230,083	81,532
	<u>\$ -</u>	<u>\$ 483,368</u>	<u>\$ 59,657</u>	<u>\$ (193,895)</u>	<u>\$ 349,130</u>	<u>\$ 88,457</u>

**Revenue Bonds**

The Phillips County, Kansas, Hospital Revenue Bonds, Series 2006 (Bonds) dated January 26, 2006, were issued to finance, along with other funds, renovation of an existing clinic building. The Bonds were issued with an interest rate of zero percent (0%). Imputed interest has been computed on the Bonds using an interest rate of 5%.

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**Note Payable**

PCHS entered into a note payable agreement (Note) with Farmers National Bank in August 2014 for the purchase of a residence that will be used to house newly hired employees, such as doctors, therapists and nurses who need time to find a permanent residence. The Note is due July 31, 2029, with monthly payments of \$958 at an interest rate of 3.95%. The debt service requirements as of March 31, 2017, are as follows:

<b>Year Ending March 31,</b>	<b>Total to be Paid</b>	<b>Principal</b>	<b>Interest</b>
2018	\$ 11,494	\$ 7,203	\$ 4,291
2019	11,493	7,492	4,001
2020	11,494	7,793	3,701
2021	11,494	8,106	3,388
2022	11,494	8,431	3,063
2023 - 2027	57,469	47,513	9,956
2028 - 2029	26,821	25,584	1,237
	<u>\$ 141,759</u>	<u>\$ 112,122</u>	<u>\$ 29,637</u>

**Capital Lease Obligations**

PCHS is obligated under leases for equipment that are accounted for as capital leases. Assets under capital leases at March 31, 2017 and 2016, totaled \$476,894 and \$448,494, respectively, net of accumulated depreciation of \$257,186 and \$259,964, respectively. The following is a schedule by year of future minimum lease payments under the capital lease including interest at rates of 2.75% to 11.00% together with the present value of the future minimum lease payments as of March 31, 2017:

Year Ending March 31,	
2018	\$ 85,671
2019	71,453
2020	63,737
2021	25,321
2022	18,201
2023 - 2024	9,956
Total minimum lease payments	<u>274,339</u>
Less amounts representing interest	<u>34,775</u>
Present value of future minimum lease payments	<u>\$ 239,564</u>

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***Line of Credit***

During October 2016, PCHS entered into a line of credit agreement totaling \$600,000 with First National Bank and Trust. The line is for operating purposes with a fixed interest rate of 5.25%, collateralized by primarily all of PCHS's assets. At March 31, 2017, there was \$0 borrowed against the line. Principal on the line of credit is due in April 2017. Subsequent to year-end, the line was renewed with a maturity date of November 2017.

**Note 8: Pension Plan**

PCHS maintains a contributory pension plan for all eligible employees. Eligibility is established by all employees 18 years of age or older who have completed one year of service. Benefits are funded by a money purchase annuity with an insurance company. The plan is funded for past service on an installment basis over the estimated remaining duration of employment from the effective date of the plan to the employee's normal retirement date. Employee contributions to the plan are computed at the rate of 2.5% of annual compensation up to \$16,000 and 5% of annual compensation in excess of \$16,000. Employer contributions to the plan are computed at the rate of 5% of the annual compensation of eligible employees up to \$16,000 and 10% of annual compensation in excess of \$16,000. Benefits vest at 20% per year with 100% vesting after five years of service. Contributions actually made by plan members and PCHS aggregated \$616,296 and \$576,234 during 2017 and \$589,998 and \$574,793 during 2016, respectively.

**Note 9: Management/Services Agreement**

The Board of Trustees of PCHS has contracted with GPHA for various services, including management and data processing services. The terms of the agreements vary from one to seven years and can be canceled with 60 days' notice. The agreements can be renewed after the initial term has expired on a year-to-year basis. Fees incurred for the various services provided by GPHA to PCHS totaled \$549,471 and \$580,982 in 2017 and 2016, respectively. Amounts included in accounts payable related to these services totaled \$322,795 and \$46,549 at March 31, 2017 and 2016, respectively.

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**Note 10: 340B Drug Pricing Program**

PCHS participates in the 340B Drug Pricing Program (340B Program), enabling PCHS to receive discounted prices from drug manufacturers on outpatient pharmaceutical purchases. PCHS recorded revenues of \$1,040,591 and \$1,206,671 for the years ending March 31, 2017 and 2016, respectively, which is included in other operating revenue in the accompanying statements of revenues, expenses and changes in net position. PCHS recorded expenses of \$994,327 and \$1,087,385 for the years ending March 31, 2017 and 2016, respectively, which is included in supplies and other 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 these programs 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 11: Great Plains Employee Benefits Trust**

In response to amendments to Kansas Insurance Code related to multi-employer welfare arrangements, GPHA restated its existing voluntary employees' beneficiary association (VEBA) trust as described in Section 501(c)(9) of the Internal Revenue Code, which is named the Great Plains Employee Benefits Trust (the Trust). The Trust is governed by its Board of Trustees. One of the purposes of the Trust is to provide the self-funded GPHA Employee Benefits Plan (the Plan) for its member organizations and their participating employees. PCHS is a member organization in the Trust and substantially all of PCHS's employees and their dependents are eligible to participate in the Plan. The Plan provides medical benefits, prescription drug benefits and dental benefits for a benefit period that runs each year from July 1 through June 30. The participant's monthly premiums are determined by the Trust. The Trust may change the premiums from time to time. The Plan agreement specifies that the Trust will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of stop-loss amounts. The Trust accrues a provision for self-insured employee benefit claims including both claims reported and claims incurred but not yet reported. If a net deficit position is anticipated by the Trust after consideration of the accrued provision, the Trust will administer insurance assessments to its member organizations based on a systematic allocation method. During 2016, PCHS was assessed approximately \$126,400, of which \$94,800 was estimated to cover the shortfall at March 31, 2016, which is included in accrued payroll taxes and other in the accompanying balance sheets. The insurance assessment was paid in full as of March 31, 2017. No further insurance assessment was necessary.

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**Note 12: Termination of Lease Agreement**

The assets and liabilities transferred to PCHS as of April 1, 2015, represent an integrated set of assets and liabilities managed for the purpose of providing acute care and clinic services in the Phillipsburg, Kansas area. There was no consideration given in the transaction. PCHS determined that no adjustments were necessary to the carrying value of assets transferred and as such, no impairment of capital assets transferred was recognized. As a result of the transfer, PCHS recognized the following assets, liabilities and net position as of April 1, 2015:

	<b><u>Carrying Value</u></b>
<b>Assets</b>	
Current assets	\$ 2,086,345
Noncurrent cash	151,785
Capital assets, net ( <i>Note 5</i> )	1,628,859
Other assets	<u>44,357</u>
Total assets	<u><u>\$ 3,911,346</u></u>
<b>Liabilities</b>	
Current liabilities	\$ 1,587,135
Long-term debt ( <i>Note 7</i> )	<u>300,320</u>
Total liabilities	<u><u>\$ 1,887,455</u></u>
<b>Net Position</b>	
Net investment in capital assets	\$ 1,145,491
Restricted - expendable for specific operating activities	151,785
Unrestricted	<u>726,615</u>
Total net position	<u><u>\$ 2,023,891</u></u>