

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Independent Auditor's Report and Financial Statements
December 31, 2019 and 2018

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
December 31, 2019 and 2018

Contents

Independent Auditor's Report	1
 Financial Statements	
Balance Sheets.....	3
Statements of Revenues, Expenses and Changes in Net Position	4
Statements of Cash Flows	5
Notes to Financial Statements	7

Independent Auditor's Report

Board of Trustees
Fredonia Regional Hospital
Fredonia, Kansas

We have audited the accompanying financial statements of Fredonia Regional Hospital (the Hospital), a component unit of the City of Fredonia, Kansas, as of and for the years ended December 31, 2019 and 2018, 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; 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 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 Fredonia Regional Hospital as of December 31, 2019 and 2018, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

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 information, although not 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
May 18, 2020

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Balance Sheets
December 31, 2019 and 2018

Assets and Deferred Outflows of Resources

	<u>2019</u>	<u>2018</u>
Current Assets		
Cash	\$ 562,806	\$ 599,407
Restricted cash and investments – current	303,967	265,446
Patient accounts receivable, net of allowance 2019 – \$380,843; 2018 – \$307,238	1,828,722	1,339,482
Estimated amounts due from third-party payers	-	60,000
Supplies	336,552	403,914
Prepaid expenses and other	<u>201,289</u>	<u>87,190</u>
Total current assets	<u>3,233,336</u>	<u>2,755,439</u>
Noncurrent Cash and Investments		
Designated by Board of Trustees	601,839	905,544
Restricted by donors for capital acquisitions and specific operating activities	3,921	50,345
Held by trustee for debt service	<u>762,125</u>	<u>758,509</u>
Total noncurrent cash and investments	<u>1,367,885</u>	<u>1,714,398</u>
Capital Assets, Net	<u>5,293,982</u>	<u>5,967,829</u>
Total assets	<u>9,895,203</u>	<u>10,437,666</u>
Deferred Outflows of Resources		
Unamortized loss on refunding of long-term debt	<u>630,624</u>	<u>668,280</u>
Total assets and deferred outflows of resources	<u><u>\$ 10,525,827</u></u>	<u><u>\$ 11,105,946</u></u>

Liabilities and Net Position (Deficit)

	<u>2019</u>	<u>2018</u>
Current Liabilities		
Current maturities of long-term debt	\$ 496,996	\$ 496,338
Accounts payable	1,062,054	526,385
Accrued salaries and wages	155,700	152,241
Accrued vacation benefits	275,885	286,023
Accrued interest payable	147,351	152,259
Estimated amounts due to third-party payers	<u>116,600</u>	<u>268,606</u>
Total current liabilities	<u>2,254,586</u>	<u>1,881,852</u>
Long-term Debt	<u>8,683,798</u>	<u>9,186,443</u>
Estimated Amounts Due to Third-party Payers	<u>-</u>	<u>71,549</u>
Total liabilities	<u>10,938,384</u>	<u>11,139,844</u>
Net Position (Deficit)		
Net deficit in capital assets	(3,886,812)	(3,714,952)
Restricted - expendable for		
Debt service	1,066,092	1,023,955
Capital acquisitions and specific operating activities	3,921	50,345
Unrestricted	<u>2,404,242</u>	<u>2,606,754</u>
Total net deficit	<u>(412,557)</u>	<u>(33,898)</u>
Total liabilities and net deficit	<u>\$ 10,525,827</u>	<u>\$ 11,105,946</u>

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2019 and 2018

	2019	2018
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2019 – \$595,085; 2018 – \$776,891	\$ 10,522,853	\$ 12,112,344
Other	395,252	380,225
Total operating revenues	10,918,105	12,492,569
Operating Expenses		
Salaries and wages	4,563,595	5,427,959
Employee benefits	1,029,664	1,274,411
Supplies and other	5,409,351	6,321,076
Depreciation	752,616	898,323
Total operating expenses	11,755,226	13,921,769
Operating Loss	(837,121)	(1,429,200)
Nonoperating Revenues (Expenses)		
Noncapital appropriations – City of Fredonia and Wilson County	592,963	567,871
Interest income	22,446	19,219
Interest expense	(470,709)	(513,887)
Noncapital grants and gifts	290,762	200,303
Total nonoperating revenues	435,462	273,506
Deficiency of Revenues Over Expenses Before Capital Grants and Gifts	(401,659)	(1,155,694)
Capital Grants and Gifts	23,000	174,000
Decrease in Net Position	(378,659)	(981,694)
Net Position (Deficit), Beginning of Year	(33,898)	947,796
Net Deficit, End of Year	\$ (412,557)	\$ (33,898)

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Statements of Cash Flows
Years Ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Cash Flows From Operating Activities		
Receipts from and on behalf of patients	\$ 9,870,058	\$ 12,260,846
Payments to suppliers and contractors	(4,885,427)	(6,101,967)
Payments to employees	(5,599,938)	(6,813,670)
Other receipts	394,552	380,225
	<u> </u>	<u> </u>
Net cash used in operating activities	<u>(220,755)</u>	<u>(274,566)</u>
 Cash Flows From Noncapital Financing Activities		
Noncapital appropriations - City of Fredonia and Wilson County	592,963	567,871
Noncapital grants and gifts	290,762	200,303
	<u> </u>	<u> </u>
Net cash provided by noncapital financing activities	<u>883,725</u>	<u>768,174</u>
 Cash Flows From Capital and Related Financing Activities		
Capital grants and gifts	23,000	174,000
Principal paid on long-term debt	(501,987)	(476,589)
Interest paid on long-term debt	(433,053)	(476,231)
Proceeds from disposal of capital assets	700	-
Purchases of capital assets	(118,669)	(252,118)
	<u> </u>	<u> </u>
Net cash used in capital and related financing activities	<u>(1,030,009)</u>	<u>(1,030,938)</u>
 Cash Flows From Investing Activities		
Interest income	22,446	19,219
Purchases of investments	(837,687)	(1,026,010)
Proceeds from disposition of investments	1,023,955	1,014,832
	<u> </u>	<u> </u>
Net cash provided by investing activities	<u>208,714</u>	<u>8,041</u>
 Decrease in Cash	<u>(158,325)</u>	<u>(529,289)</u>
 Cash, Beginning of Year	<u>1,034,152</u>	<u>1,563,441</u>
 Cash, End of Year	<u>\$ 875,827</u>	<u>\$ 1,034,152</u>

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Statements of Cash Flows (Continued)
Years Ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Reconciliation of Cash to the Balance Sheets		
Cash in current assets	\$ 562,806	\$ 599,407
Cash designated by Board of Trustees	309,100	384,400
Cash restricted by donors	<u>3,921</u>	<u>50,345</u>
	<u>\$ 875,827</u>	<u>\$ 1,034,152</u>
Reconciliation of Operating Loss to Net Cash Used in Operating Activities		
Operating loss	\$ (837,121)	\$ (1,429,200)
Depreciation	752,616	898,323
Provision for uncollectible accounts	595,085	776,891
Gain on disposal of capital assets	(700)	-
Changes in operating assets and liabilities		
Patient accounts receivable	(1,084,325)	(415,856)
Estimated amounts due from and to third-party payers	(163,555)	(212,533)
Supplies	67,362	117,991
Prepaid expenses and other	(114,099)	116,274
Accounts payable	575,569	(10,438)
Accrued expenses	<u>(11,587)</u>	<u>(116,018)</u>
Net cash used in operating activities	<u>\$ (220,755)</u>	<u>\$ (274,566)</u>
Noncash Investing, Capital and Financial Activities		
Amortization of loss on refunding	\$ 37,656	\$ 37,656
Capital assets acquisitions included in accounts payable	\$ -	\$ 39,900

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

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

Nature of Operations and Reporting Entity

Fredonia Regional Hospital (Hospital) is a municipal hospital located in Fredonia, Kansas. The Hospital is a component unit of the City of Fredonia, Kansas (City). The Hospital primarily earns revenues by providing inpatient, outpatient, emergency care and physician services. The Hospital is licensed as a critical access hospital (CAH).

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), property taxes, investment 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.

Cash Equivalents

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

Investments

Investments in U.S. Treasury, agency and instrumentality obligations (money market investments) with a remaining maturity of one year or less at time of acquisition are carried at fair value. Nonnegotiable certificates of deposit are carried at amortized cost.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

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.

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 and leasehold improvements	10 – 40 years
Fixed equipment	5 – 20 years
Major moveable equipment	3 – 10 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, 2019 and 2018.

Deferred Outflows of Resources

The Hospital reports the consumption of net position that is applicable to a future reporting period as deferred outflows of resources in a separate section of its balance sheets.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

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.

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; professional liability; 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.

Net Position

Net position of the Hospital is classified in three components on its balance sheets.

- 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, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings.
- Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets or restricted net position.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

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 to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Noncapital Appropriations – City of Fredonia and Wilson County

The Hospital received approximately 5% in 2019 and 4% in 2018 of its financial support from noncapital appropriations from the City of Fredonia's 1% sales tax and Wilson County property tax levy.

Property taxes are assessed on a calendar basis and are received beginning January 1 of each year. Revenue from noncapital appropriations – City of Fredonia and Wilson County is recognized in full in the year in which use is first permitted.

Income Taxes

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

Note 2: Deposits and Investments

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.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

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, 2019 and 2018, respectively, \$734,244 and \$1,151,463 of the Hospital's bank balances of \$1,170,988 and \$1,626,519 were exposed to custodial credit risk as follows:

	2019	2018
Uninsured and collateral held by pledging financial institution	\$ 734,244	\$ 1,151,463

Investments

The Hospital may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in corporate bonds and equity securities.

All of the Hospital's held by trustee for debt service investments as well as the current portion of restricted cash and investments were invested in short-term U.S. treasuries (money market investments) with a remaining maturity of one year or less at the time of acquisition at December 31, 2019 and 2018, and are carried at fair value.

Summary of Carrying Values

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

	2019	2018
Carrying value		
Deposits	\$ 1,168,566	\$ 1,555,296
Investments	1,066,092	1,023,955
	\$ 2,234,658	\$ 2,579,251

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

Included in the following balance sheet captions:

	<u>2019</u>	<u>2018</u>
Cash	\$ 562,806	\$ 599,407
Restricted cash and investments - current	303,967	265,446
Designated by Board of Trustees	601,839	905,544
Restricted by donors for capital acquisitions and specific operating activities	3,921	50,345
Held by trustee for debt service	<u>762,125</u>	<u>758,509</u>
	<u>\$ 2,234,658</u>	<u>\$ 2,579,251</u>

Note 3: 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>2019</u>	<u>2018</u>
Medicare	\$ 874,913	\$ 561,064
Medicaid	80,973	37,994
Blue Cross	191,869	144,952
Commercial	366,323	230,482
Private pay	695,487	672,228
	<u>2,209,565</u>	<u>1,646,720</u>
Less allowance for uncollectible accounts	<u>(380,843)</u>	<u>(307,238)</u>
	<u>\$ 1,828,722</u>	<u>\$ 1,339,482</u>

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

Note 4: Capital Assets

Capital assets activity for the years ended December 31 was:

	2019			
	Beginning Balance	Additions	Deletions	Ending Balance
Land	\$ 25,474	\$ -	\$ -	\$ 25,474
Land improvements	843,452	-	-	843,452
Buildings	11,526,149	-	-	11,526,149
Fixed equipment	1,427,645	-	-	1,427,645
Moveable equipment	3,875,836	78,769	(17,412)	3,937,193
	<u>17,698,556</u>	<u>78,769</u>	<u>(17,412)</u>	<u>17,759,913</u>
Less accumulated depreciation				
Land improvements	(574,244)	(29,915)	-	(604,159)
Buildings	(6,968,937)	(406,350)	-	(7,375,287)
Fixed equipment	(1,012,352)	(39,585)	-	(1,051,937)
Moveable equipment	(3,175,194)	(276,766)	17,412	(3,434,548)
	<u>(11,730,727)</u>	<u>(752,616)</u>	<u>17,412</u>	<u>(12,465,931)</u>
Capital assets, net	<u>\$ 5,967,829</u>	<u>\$ (673,847)</u>	<u>\$ -</u>	<u>\$ 5,293,982</u>
	2018			
	Beginning Balance	Additions	Deletions	Ending Balance
Land	\$ 25,474	\$ -	\$ -	\$ 25,474
Land improvements	843,452	-	-	843,452
Buildings	11,526,149	-	-	11,526,149
Fixed equipment	1,380,677	46,968	-	1,427,645
Moveable equipment	3,896,776	245,050	(265,990)	3,875,836
	<u>17,672,528</u>	<u>292,018</u>	<u>(265,990)</u>	<u>17,698,556</u>
Less accumulated depreciation				
Land improvements	(540,833)	(33,411)	-	(574,244)
Buildings	(6,454,057)	(514,880)	-	(6,968,937)
Fixed equipment	(943,472)	(68,880)	-	(1,012,352)
Moveable equipment	(3,160,032)	(281,152)	265,990	(3,175,194)
	<u>(11,098,394)</u>	<u>(898,323)</u>	<u>265,990</u>	<u>(11,730,727)</u>
Capital assets, net	<u>\$ 6,574,134</u>	<u>\$ (606,305)</u>	<u>\$ -</u>	<u>\$ 5,967,829</u>

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

Note 5: Long-term Obligations

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

	2019					
	Beginning Balance	Additions	Deletions	Ending Balance	Current Portion	Long-term Portion
Series 2016 Refunding						
Revenue Bonds	\$ 9,460,000	\$ -	\$ 385,000	\$ 9,075,000	\$ 395,000	\$ 8,680,000
Capital leases	222,781	-	116,987	105,794	101,996	3,798
	<u>\$ 9,682,781</u>	<u>\$ -</u>	<u>\$ 501,987</u>	<u>\$ 9,180,794</u>	<u>\$ 496,996</u>	<u>\$ 8,683,798</u>

	2018					
	Beginning Balance	Additions	Deletions	Ending Balance	Current Portion	Long-term Portion
Series 2016 Refunding						
Revenue Bonds	\$ 9,830,000	\$ -	\$ 370,000	\$ 9,460,000	\$ 385,000	\$ 9,075,000
Capital leases	329,370	-	106,589	222,781	111,338	111,443
	<u>\$ 10,159,370</u>	<u>\$ -</u>	<u>\$ 476,589</u>	<u>\$ 9,682,781</u>	<u>\$ 496,338</u>	<u>\$ 9,186,443</u>

Series 2016 Refunding Revenue Bonds

In February 2016, the Hospital issued \$10,360,000 City of Fredonia, Kansas Hospital Refunding Revenue Bonds, Series 2016 (2016 Bonds). The 2016 Bonds are payable in annual installments through August 15, 2036, and bear interest at rates of 3.00% to 4.90%. The 2016 Bonds are secured by the net revenues of the Hospital.

Upon issuance and delivery of the Series 2016 Bonds, the Hospital defeased its outstanding Series 2010 and 2007 bonds. Funds were deposited in trust under an escrow agreement sufficient in amount to pay future principal and interest on the defeased bonds. This advance refunding transactions resulted in an extinguishment of debt since the Hospital was legally defeased from its obligation on the Series 2010 and 2007 bonds at the time of defeasance. The advance refunding of the Series 2010 and 2007 bonds resulted in an overall future economic benefit for the Hospital. However, an accounting loss of \$778,100 on the extinguishment of the long-term debt was recorded in 2016. This loss on refunding is shown as a deferred outflow of resources in the balance sheets and is being amortized using the straight-line method over the life of the Series 2016 Bonds.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

The indenture agreements require that certain funds be established with the trustee. Accordingly, these funds are included as assets held by trustee for debt service and restricted cash and investments - current in the balance sheets. The indenture agreements also require the Hospital to comply with certain restrictive covenants including maintaining a historical debt-service coverage of at least 1.10 or maintaining a minimum days' cash on hand of 75 days, which includes the Fredonia Regional Health Care Foundation, Inc.'s cash.

Capital Lease Obligations

The Hospital is obligated under leases for equipment that are accounted for as capital leases. The capital leases are secured by the related assets as collateral. Capital assets include the following property under capital leases at December 31, 2019 and 2018:

	2019	2018
Moveable equipment	\$ 532,989	\$ 532,989
Less accumulated depreciation	447,556	353,921
	\$ 85,433	\$ 179,068

Debt Service Requirements

Debt service requirements on long-term debt, including capital lease obligations, as of December 31, 2019, are as follows:

Year Ending December 31,	Long-term Debt		Capital Lease	
	Principal	Interest	Principal	Interest
2020	\$ 395,000	\$ 392,935	\$ 101,996	\$ 2,951
2021	410,000	379,505	3,798	154
2022	420,000	367,205	-	-
2023	435,000	353,555	-	-
2024	450,000	338,330	-	-
2025-2029	2,535,000	1,408,010	-	-
2030-2034	3,160,000	788,070	-	-
2035-2036	1,270,000	88,935	-	-
	\$ 9,075,000	\$ 4,116,545	\$ 105,794	\$ 3,105

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

Note 6: Professional Liability Claims

The Hospital purchases professional liability 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 professional liability 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: 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. 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 cost subject to certain limitations. Inpatient geriatric psych services rendered to Medicare program beneficiaries are paid based on a blend of prospective payment rates and cost subject to certain limitations. The Hospital is reimbursed for most services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor.

Medicaid. 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.

Approximately 74% and 72% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2019 and 2018, 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.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

Note 8: Charity Care

The costs of charity care provided under the Hospital's charity care policy were approximately \$18,000 and \$7,000 for 2019 and 2018, respectively. The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges.

Note 9: Management/Services Agreement

The Board of Trustees has contracted with Great Plains Health Alliance, Inc. (GPHA) for various services, including management, data processing and accounting 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 the Hospital for the years ended December 31, 2019 and 2018, were \$662,439 and \$672,024, respectively. Amounts included in accounts payable related to these services totaled \$230,648 and \$106,179 at December 31, 2019 and 2018, respectively.

Note 10: Pension Plan

The Hospital maintains a defined contribution plan (401(a) plan) covering all employees. Employer and mandated employee contributions are computed at 4% and 3% of the covered payroll, respectively. The contributions are invested as each employee directs. Each participant chooses which accounts to use and may change the election once each calendar year. Contributions actually made by plan members and the Hospital aggregated \$107,332 and \$142,758 during 2019 and \$110,585 and \$151,239 during 2018, respectively.

The Hospital provides one additional defined contribution plan (457 plan). The Hospital does not make contributions to the 457 plan. Contributions made by plan members totaled \$51,439 and \$65,264 during 2019 and 2018, respectively. The plan year begins on January 1 and ends December 31.

Note 11: Fredonia Regional Health Care Foundation, Inc.

The Fredonia Regional Health Care Foundation, Inc. (Foundation) is a nonprofit organized to perpetuate the advancement of health, health care and medical education, research and welfare services for residents of Fredonia, Kansas and its outlying regions. The Foundation is not considered a component unit of the Hospital. The Foundation contributed \$32,009 and \$276,482 to the Hospital in 2019 and 2018, respectively, which is included in both capital grants and gifts and noncapital grants and gifts on the statements of revenues, expenses and changes in net position.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

Note 12: Contingencies

General Litigation

The Hospital is subject to claims and lawsuits that arose primarily in the ordinary course of its activities. The Hospital evaluates allegations by conducting investigations to determine the validity of each potential claim. It is the opinion of management the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the balance sheets, change in net assets and cash flows of the Hospital. Events could occur that would change this estimate materially in the near term.

Note 13: Subsequent Events

As a result of the spread of the COVID-19 coronavirus, economic uncertainties have arisen which may negatively affect the financial position, results of operations and cash flows of the Hospital. The duration of these uncertainties and the ultimate financial effects cannot be reasonably estimated at this time.

On April 10, 2020, the Hospital received approximately \$376,000 of stimulus funds from the Department of Health and Human Services (HHS). Certain conditions are required to be met to retain these funds. If the conditions are met, the funds will be retained by the Hospital with no repayment obligations. Management has attested to the requirements and believes the Hospital will retain the stimulus payments.

On April 16, 2020, Kansas Governor Laura Kelly announced a special emergency grant funding program for Kansas hospitals. This emergency funding was requested by the Kansas Hospital Association (KHA) on behalf of the hospitals and was distributed to help offset current financial strains caused by the COVID-19 pandemic. To facilitate the timely release of funds, hospitals were not required to complete an application. There are no specific requirements tied to utilization of the funds. The intent is for the grant payments to serve as a bridge to aid hospitals in meeting their basic operational expenditures. The Hospital received \$100,000 on April 24, 2020, related to this special emergency grant.

On May 6, 2020, the Hospital received approximately \$3,394,000 of additional stimulus funds from HHS. Certain conditions are required to be met to retain these funds. If the conditions are met, the funds will be retained by the Hospital with no repayment obligations. Management has attested to the requirements and believes the Hospital will retain a portion, if not all, of the stimulus payments.

Fredonia Regional Hospital
A Component Unit of the City of Fredonia, Kansas
Notes to Financial Statements
December 31, 2019 and 2018

On May 7, 2020, the Hospital obtained a loan through a local bank that is fully guaranteed by the U.S. Small Business Administration (SBA) through the Paycheck Protection Program (PPP). The amount borrowed is approximately \$1,068,000 at 1.00% interest with a maturity date of May 7, 2022. Under the PPP, if certain conditions are met, up to 100% of the principal amount may be forgiven. Management believes all, or nearly all, of the amount borrowed will meet the conditions for loan forgiveness.

Note 14: Future Change in Accounting Principle

Leases

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.

In response to the challenges arising from COVID-19, on May 7, 2020, GASB approved Statement 95, *Postponement of the Effective Dates of Certain Authoritative Guidance*. While the proposal included an extra year to implement all guidance, GASB, in a unanimous vote, approved an 18-month postponement for GASB 87. All statements and implementation guides with a current effective date of reporting periods beginning after June 15, 2018, and later will have a one-year postponement. This change is effective immediately. GASB 87 is effective for financial statements for fiscal years beginning after June 15, 2021. Earlier application is permitted. 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.