

Board of Trustees and Management
Gove County Medical Center
Quinter, Kansas

As part of our audit of the financial statements of Gove County Medical Center as of and for the year ended December 31, 2009, we wish to communicate the following to you.

AUDIT SCOPE AND RESULTS

Auditor's Responsibility Under Auditing Standards Generally Accepted in the United States of America

An audit performed in accordance with auditing standards generally accepted in the United States of America is designed to obtain reasonable, rather than absolute, assurance about the financial statements. In performing auditing procedures, we establish scopes of audit tests in relation to the financial statements taken as a whole. Our engagement does not include a detailed audit of every transaction. Our engagement letter more specifically describes our responsibilities.

These standards require communication of significant matters related to the financial statement audit that are relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. Such matters are communicated in the remainder of this letter or have previously been communicated during other phases of the audit. The standards do not require the auditor to design procedures for the purpose of identifying other matters to be communicated with those charged with governance.

An audit of the financial statements does not relieve management or those charged with governance of their responsibilities. Our engagement letter more specifically describes your responsibilities.

Qualitative Aspects of Significant Accounting Policies and Practices

Significant Accounting Policies

The Hospital's significant accounting policies are described in *Note 1* of the audited financial statements.

No matters are reportable.

Alternative Accounting Treatments

We had discussions with management regarding alternative accounting treatments within accounting principles generally accepted in the United States of America for policies and practices for material items, including recognition, measurement and disclosure considerations related to the accounting for specific transactions as well as general accounting policies, as follows:

No matters are reportable.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of financial statement preparation by management, based on its judgments. The following areas involve significant areas of such estimates for which we are prepared to discuss management's estimation process and our procedures for testing the reasonableness of those estimates:

- Allowances for contractual adjustments
- Allowances for uncollectible accounts
- Amounts due to or from Medicare

Financial Statement Disclosures

The following areas involve particularly sensitive financial statement disclosures for which we are prepared to discuss the issues involved and related judgments made in formulating those disclosures:

No matters are reportable.

Audit Adjustments

During the course of any audit, an auditor may propose adjustments to financial statement amounts. Management evaluates our proposals and records those adjustments which, in its judgment, are required to prevent the financial statements from being materially misstated.

Areas in which adjustments were proposed include:

Proposed Audit Adjustments Recorded

- Net assets

Proposed Audit Adjustments Not Recorded

- No matters are reportable

Auditor's Judgments About the Quality of the Entity's Accounting Principles

During the course of the audit, we made the following observations regarding the Hospital's application of accounting principles:

No matters are reportable.

Disagreements with Management

The following matters involved disagreements which if not satisfactorily resolved would have caused a modified auditor's opinion on the financial statements:

No matters are reportable.

Consultation with Other Accountants

During our audit, we became aware that management had consulted with other accountants about the following auditing or accounting matters:

No matters are reportable.

Significant Issues Discussed with Management

Prior to Retention

During our discussion with management prior to our engagement, the following issues regarding application of accounting principles or auditing standards were discussed:

No matters are reportable.

During the Audit Process

During the audit process, the following issues were discussed or were the subject of correspondence with management:

No matters are reportable.

Difficulties Encountered in Performing the Audit

Our audit requires cooperative effort between management and the audit team. During our audit, we found significant difficulties in working effectively on the following matters:

No matters are reportable.

Other Material Written Communications

Listed below are other material written communications between management and us related to the audit:

- Management representation letter (attached)

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements of Gove County Medical Center as of and for the year ended December 31, 2009, in accordance with auditing standards generally accepted in the United States of America, we considered the Hospital's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified.

A deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements of the Hospital's financial statements on a timely basis. A deficiency in design exists when a control necessary to meet a control objective is missing or an existing control is not properly designed so that, even if the control operates as designed, a control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Hospital's financial statements will not be prevented or detected and corrected on a timely basis.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

We observed the following matters that we consider to be deficiencies. Previously we made observations as a result of our 2008 audit engagement in a letter dated April 9, 2009.

Deficiencies

The Hospital has control deficiencies in its payroll, purchases, accounts payable/cash disbursements and accounts receivable/revenue/cash receipts cycles. In each of these cycles, certain employees have the primary responsibility for performing the access, recording, and monitoring functions. Management has procedures in place to oversee these conflicts; however, a periodic evaluation of their effectiveness should be made. While we have previously communicated these matters to the Board and management, it is important that you remain aware of these risks and assure that management reports on their efforts to maintain an appropriate internal control structure.

We ask that management consider the following additional procedures to further enhance the control structure:

- Cross training of staff to perform duties when primary staff are on vacation or sick should be accomplished. Password access should be granted to the backup staff only when they need access to perform duties when primary staff are absent.
- The CEO should obtain and review a copy of the bank statements each month. He should also review the cash account reconciliations performed by the CFO each month. These reviews should be documented and performed in a timely manner.
- Signed checks should be given to somebody outside of the accounts payable process to stuff and mail.
- Checks should be restrictively endorsed when received.

- The vendor master file should be reviewed by the CEO and vendors which are no longer approved should be removed. New vendors should be approved by the CEO, in writing, before being added to the file.
- Someone other than the purchasing agent should be involved in receipting goods ordered.

OTHER MATTERS

Although not considered material weaknesses, significant deficiencies or deficiencies in internal control over financial reporting, we observed the following matters and offer these comments and suggestions with respect to matters which came to our attention during the course of the audit of the financial statements. Our audit procedures are designed primarily to enable us to form an opinion on the financial statements and, therefore, may not bring to light all weaknesses in policies and procedures that may exist. However, these matters are offered as constructive suggestions for the consideration of management as part of the ongoing process of modifying and improving accounting controls and the financial and administrative practices and procedures. We can discuss these matters further at your convenience and may provide implementation assistance for changes or improvements if you require.

Fixed Assets

During 2009, no physical count of fixed assets was completed. It would be beneficial to implement a regular count of fixed assets to ensure all schedules are properly reflecting current activity. This will further assist in preventing and detecting misstatements in a more timely manner.

Information Technology Operations

We ask management to consider the following regarding system operations:

- A disaster recovery plan should be developed specifically for the information technology department (including all software and hardware). This would include details of how all electronic data operations would be restored in the event of a natural or other disaster.
- The IT director should periodically review audit logs for security violations and report to management regarding those results no less than quarterly.
- Currently, the IT director is reviewing access privileges one to two times per year. We ask that you consider documenting this review.

Stark Compliance

The current contract for rental space with the physicians is over 12 years old. While the rental agreement may still be compliant with the Stark law, now may be a good time to review it along with all other contracts currently in place for both compliance and financial issues.

Depositories

Kansas statutes allow several types of financial institutions to be designated as depositories, however, credit unions are not included. Although there is deposit insurance provided by the National Credit Union Association (NCUA) which covers the balances the Hospital has on deposit, the deposits are not in compliance with the statute. We recommend moving the funds to an allowed depository as soon as is possible.

Debt Service Accounts

The loan documents for the revenue bonds related to the construction of a therapy pool include several covenants to be met each year. A short review of those items is as follows:

- One-twelfth of the next amounts due for interest and principal must be set aside each month. Starting from November 1, 2009, approximately \$2,500 each month should be recorded in an account identified as bond principal and interest account.
- Maintain an efficient and economical operation.
- Maintain a debt service coverage ratio of 110% for parity bond debts.
- Maintain appropriate insurance for a hospital.
- Maintain books and records on the appropriate basis of accounting.
- Prepare a budget annually for review by the Board.
- Have an audit annually.
- A Hospital employee must inspect the facility annually and report on the condition. Once every five years this inspection must be completed by a consulting engineer.

The covenant related to the principal and interest reserve has not been met during 2009. We recommend action be taken to set up the appropriately titled accounts and reclassify funds to assure they will be available by each November 1 to pay the principal amounts due.

Electronic Health Records

The proposed rule issued earlier this year contains several key issues which the Hospital must address to receive payments as part of the American Reinvestment and Recovery Act. They are as follows:

- The reporting period in the first payment year must be at least a 90-day period beginning no earlier than the first day of that year and ending no less than 90 days afterward. Subsequent reporting periods will be the entire year for each payment period. Key performance thresholds must be met during these reporting periods in order to be eligible for payments.

- Stage 1 criteria must be met to demonstrate meaningful use in the first payment year. Those criteria include implementation of drug/allergy checks, maintain up-to-date problem list of diagnoses, maintain active medication list, etc. These must be included within the electronic health record and consistently maintained over the reporting period.
- Initial reporting of meaningful use will be based on self-attestations filed with CMS. These will be audited/tested by yet to be named groups that will be accredited to certify meaningful use.
- Medicare Part A and Part C days will be included in determining the allowable percentage of payment. Part C days must be billed as no-pay claims to CMS in order to be included.
- Charity care can positively impact the Medicare percent of payment. Identification of accounts that qualify for charity care and documentation of criteria to be allowed as such must be maintained. Any account for which there is no insurance, including those deductibles and coinsurance not paid, are eligible for charity status if they meet the Hospital's criteria. This does not include accounts which are claimed as Medicare bad debts.

The final rule for electronic health records is expected to be issued by June and may yet change the proposed rule significantly, especially as it relates to the timing requirements regarding when each stage's criteria must be met.

Additional proposed rules have been issued related to testing and certification of electronic health records and will likely impact vendors, hospitals and testing organizations as they move forward.

We urge management to keep abreast of these issues as they develop in order to be prepared to implement electronic health records at the earliest possible time to receive the maximum allowable reimbursement.

Current Economic Conditions

The current protracted economic decline continues to present difficult circumstances and challenges for the health care industry. As a result, hospitals are facing declines in the fair values of investments and other assets, declines in contributions, constraints on liquidity and difficulty obtaining financing. The values of the assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments to asset values, the allowance for accounts receivable, etc. that could negatively impact the Hospital's ability to maintain sufficient liquidity. Now, more than ever, we recommend that management and the Board of Trustees vigilantly monitor and aggressively manage all of these matters.

This communication is intended solely for the information and use of management, the Board of Trustees and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

March 24, 2010

Gove County Medical Center

520 West 5th Street, P.O. Box 129

Quinter, Kansas 67752

March 24, 2010

BKD, LLP

Certified Public Accountants

1551 North Waterfront Parkway, Suite 300

Wichita, Kansas 67206

We are providing this letter in connection with your audits of our financial statements as of and for the years ended December 31, 2009 and 2008. We confirm that we are responsible for the fair presentation of the financial statements in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining effective internal control over financial reporting, operations and compliance, and preventing and detecting fraud.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, the following:

1. The financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America and the Kansas Municipal Audit Guide. We have omitted management's discussion and analysis that the Governmental Accounting Standards Board has determined necessary to supplement, although not required to be a part of, the basic financial statements.
2. We have reviewed and approved a draft of the financial statements and related notes referred to above, which you prepared in connection with your audit of our financial statements. We acknowledge that we are responsible for the fair presentation of the financial statements and related notes.
3. We have made available to you:
 - (a) All financial records and related data.
 - (b) All minutes of trustees' meetings held through the date of this letter.
 - (c) All significant contracts and grants.

- (d) All peer review organizations, fiscal intermediary and third-party payer reports and information.
4. We have informed you of all current risks of a material amount that are not adequately prevented or detected by Hospital procedures with respect to:
 - (a) Misappropriation of assets.
 - (b) Misrepresented or misstated assets or liabilities.
 5. We acknowledge our responsibility for the design and implementation of programs and controls to prevent and detect fraud.
 6. We have no knowledge of any known or suspected:
 - (a) Fraudulent financial reporting or misappropriation of assets involving management or employees who have significant roles in internal control.
 - (b) Fraudulent financial reporting or misappropriation of assets involving others that could have a material effect on the financial statements.
 - (c) Communications from regulatory agencies, governmental representatives, employees or others concerning investigations or allegations of noncompliance with laws and regulations, deficiencies in financial reporting practices or other matters that could have a material adverse effect on the financial statements.
 7. We have no knowledge of any allegations of fraud or suspected fraud affecting the Hospital received in communications from employees, customers, regulators, suppliers or others.
 8. Except as reflected in the financial statements, there are no:
 - (a) Plans or intentions that may materially affect carrying values or classifications of assets and liabilities.
 - (b) Material transactions omitted or improperly recorded in the financial records.
 - (c) Material gain/loss contingencies requiring accrual or disclosure, including those arising from environmental remediation obligations.
 - (d) Events occurring subsequent to the balance sheet date requiring adjustment or disclosure in the financial statements.
 - (e) Related party transactions, balances, arrangements, or guarantees.
 - (f) Agreements to purchase assets previously sold.
 - (g) Violations of law, regulations or requirements of regulatory agencies for which losses should be accrued or matters disclosed in the financial statements.

- (h) Unasserted claims or assessments that are probable of assertion and must be disclosed as a loss contingency.
 - (i) Restrictions on cash balances or compensating balance agreements.
 - (j) Guarantees, whether written or oral, under which the Hospital is contingently liable.
9. We have informed you of all pending or completed investigations by regulatory authorities of which we are aware. There are no known circumstances that could jeopardize the Hospital's participation in the Medicare or other governmental health care programs.
10. Adequate provisions and allowances have been accrued for any material losses from:
- (a) Uncollectible receivables.
 - (b) Medicare/Medicaid and other third-party payer contractual, audit or other adjustments.
 - (c) Reducing obsolete or excess inventories to estimated net realizable value.
 - (d) Purchase commitments in excess of normal requirements or above prevailing market prices.
11. Except as disclosed in the financial statements, the Hospital has:
- (a) Satisfactory title to all recorded assets, and they are not subject to any liens, pledges or other encumbrances.
 - (b) Complied with all aspects of contractual agreements, for which noncompliance would materially affect the financial statements.
12. With respect to the Hospital's possible exposure to past or future medical malpractice assertions:
- (a) We have disclosed to you all incidents known to us that could possibly give rise to an assertion of malpractice.
 - (b) All known incidents have been reported to the appropriate medical malpractice insurer.
 - (c) There is no known lapse in coverage, including any lapse subsequent to the fiscal year-end, that would result in any known incidents being uninsured.
 - (d) Management does not expect any claims to exceed malpractice insurance limits.

13. With regard to deposit and investment activities:
 - (a) All deposit, repurchase and reverse repurchase agreements and investment transactions have been made in accordance with legal and contractual requirements.
 - (b) Disclosures of deposit and investment balances and risks in the financial statements are consistent with our understanding of the applicable laws regarding enforceability of any pledges of collateral.
 - (c) We understand that your audit does not represent an opinion regarding the enforceability of collateral pledges.

14. With respect to any nonattest services you have provided us during the year, including preparation of the Medicare cost report and drafting of the financial statements and related notes:
 - (a) We have designated a qualified management-level individual to be responsible and accountable for overseeing the nonattest services.
 - (b) We have established and monitored the performance of the nonattest services to ensure that they meet our objectives.
 - (c) We have made any and all decisions involving management functions with respect to the nonattest services and accept full responsibility for such decisions.
 - (d) We have evaluated the adequacy of the services performed and any findings that resulted.

15. We are an organization exempt from income tax under Section 115 of the Internal Revenue Code and a similar provision of state law and, except as disclosed in the financial statements, there are no activities that would jeopardize our tax-exempt status or subject us to income tax on unrelated business income or excise tax on prohibited transactions and events.

16. We acknowledge that we are responsible for compliance with applicable laws, regulations and provisions of contracts and grant agreements.

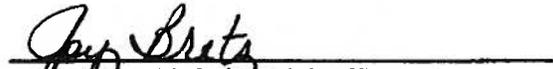
17. We have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that have a direct and material effect on the determination of amounts in our financial statements or other financial data significant to the audit objectives.

18. We have identified and disclosed to you any violations or possible violations of laws, regulations and provisions of contracts and grant agreements whose effects should be considered for recognition and/or disclosure in the financial statements.

19. We have not been designated as a potentially responsible party (PRP or equivalent status) by the Environmental Protection Agency (EPA) or other cognizant regulatory agency with authority to enforce environmental laws and regulations.
20. Billings to third-party payers comply in all material respects with applicable coding guidelines, laws and regulations. Billings reflect only charges for goods and services that were medically necessary; properly approved by regulatory bodies, if required; and properly rendered.
21. With regard to cost reports filed with Medicare, Medicaid or other third parties:
 - (a) All required reports have been properly filed.
 - (b) Management is responsible for the accuracy and propriety of those reports.
 - (c) All costs reflected on such reports are appropriate and allowable under applicable reimbursement rules and regulations and are patient-related and properly allocated to applicable payers.
 - (d) The reimbursement methodologies and principles employed are in accordance with applicable rules and regulations.
 - (e) All items required to be disclosed, including disputed costs that are being claimed to establish a basis for a subsequent appeal, have been fully disclosed in the cost report.
 - (f) Recorded allowances for third-party settlements are necessary and are based on historical experience or new or ambiguous regulations that may be subject to differing interpretations.
22. With respect to the Hospital's possible exposure to past or future workers' compensation assertions:
 - (a) We have disclosed to you all incidents known to us that could possibly give rise to workers' compensation assertion.
 - (b) All known incidents have been reported to the appropriate workers' compensation insurer.
 - (c) There is no known lapse in coverage, including any lapse subsequent to the fiscal year-end, that would result in any known incidents being uninsured.
 - (d) Management does not expect any claims to exceed workers' compensation insurance limits.
23. We acknowledge the current protracted economic decline continues to present difficult circumstances and challenges for the health care industry. Hospitals are facing declines in the fair values of investments and other assets, declines in contributions, constraints on liquidity and difficulty obtaining financing. We

understand the values of the assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments to asset values, allowances for accounts receivable, etc. that could negatively impact the Hospital's ability to maintain sufficient liquidity. We acknowledge that you have no responsibility for future changes caused by the current economic environment and the resulting impact on the Hospital's financial statements. Further, management and the Board are solely responsible for all aspects of managing the Hospital, including questioning the quality and valuation of investments and other assets, reviewing allowances for uncollectible amounts and evaluating capital needs and liquidity plans.


Richard Bergling, Chief Executive Officer


Joy Bretz, Chief Financial Officer