

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
Independent Accountants' Report and Financial Statements  
December 31, 2011 and 2010



**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**December 31, 2011 and 2010**

**Contents**

<b>Independent Accountants' Report on Financial Statements and Supplementary Information .....</b>	<b>1</b>
 <b>Financial Statements</b>	
Balance Sheets.....	3
Statements of Revenues, Expenses and Changes in Net Assets.....	4
Statements of Cash Flows .....	5
Notes to Financial Statements .....	7
 <b>Supplementary Information</b>	
Balance Sheets of Decatur Health Systems, Inc.....	22
Statements of Operations of Decatur Health Systems, Inc.....	23

## Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Trustees  
Decatur County Hospital  
Oberlin, Kansas

We have audited the accompanying balance sheets of Decatur County Hospital, a component unit of Decatur County, Kansas, as of December 31, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. 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 Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Decatur County Hospital as of December 31, 2011 and 2010, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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.

Our audits were performed for the purpose of forming an opinion on the financial statements as a whole. The Balance Sheets of Decatur Health Systems, Inc., as of December 31, 2011 and 2010, and the related Statements of Operations of Decatur Health Systems, Inc. for the years then ended listed in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the

financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*BKD, LLP*

April 13, 2012

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Balance Sheets**  
**December 31, 2011 and 2010**

**Assets**

	<u>2011</u>	<u>2010</u>
<b>Current Assets</b>		
Cash and cash equivalents	\$ 550,518	\$ 723,391
Short-term certificates of deposit	6,200	509,948
Cash held for debt service	48,359	-
Patient accounts receivable, net of allowance; 2011 - \$374,000, 2010 - \$402,000	675,669	1,268,570
Current maturities of notes receivable	-	15,654
Other receivables	5,760	19,941
Estimated amounts due from third-party payers	393,000	-
Supplies	106,005	104,962
Prepaid expenses and other	<u>79,745</u>	<u>47,974</u>
Total current assets	<u>1,865,256</u>	<u>2,690,440</u>
<b>Noncurrent Assets</b>		
Held by County for debt service	<u>48,786</u>	<u>48,786</u>
<b>Investments and Long-term Deposit</b>		
Interest in assets of Decatur Health Care Foundation, Inc.	1,783,771	2,041,762
Option deposit	<u>250,000</u>	<u>250,000</u>
	<u>2,033,771</u>	<u>2,291,762</u>
<b>Capital Assets, Net</b>	<u>1,650,961</u>	<u>1,712,995</u>
<b>Other Assets</b>		
Rural Health Clinic acquisition costs, net of accumulated amortization; 2011 - \$27,500, 2010 - \$0	82,500	-
Deferred financing costs	<u>6,375</u>	<u>6,750</u>
	<u>88,875</u>	<u>6,750</u>
Total assets	<u>\$ 5,687,649</u>	<u>\$ 6,750,733</u>

## Liabilities and Net Assets

	<u>2011</u>	<u>2010</u>
<b>Current Liabilities</b>		
Current maturities of long-term debt	\$ 55,937	\$ 54,461
Accounts payable	146,741	165,695
Accrued expenses	426,317	488,404
Estimated amounts due to third-party payers	-	278,834
	<u>628,995</u>	<u>987,394</u>
<b>Long-term Debt</b>	<u>570,569</u>	<u>626,506</u>
Total liabilities	<u>1,199,564</u>	<u>1,613,900</u>
<b>Net Assets</b>		
Invested in capital assets, net of related debt	1,024,455	1,032,028
Restricted - expendable for debt service	97,145	48,786
Unrestricted	<u>3,366,485</u>	<u>4,056,019</u>
	<u>4,488,085</u>	<u>5,136,833</u>
Total liabilities and net assets	<u>\$ 5,687,649</u>	<u>\$ 6,750,733</u>

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Statements of Revenues, Expenses and Changes in Net Assets**  
**Years Ended December 31, 2011 and 2010**

	<b>2011</b>	<b>2010</b>
<b>Operating Revenues</b>		
Net patient service revenue, net of provision for uncollectible accounts; 2011 - \$153,547, 2010 - \$214,592	\$ 6,196,505	\$ 6,537,306
Other	162,771	113,102
Total operating revenues	6,359,276	6,650,408
<b>Operating Expenses</b>		
Salaries	3,594,470	3,557,707
Employee benefits	889,840	756,354
Purchased services	417,896	442,256
Drugs	299,477	474,583
Medical supplies	204,808	256,200
Food	108,706	110,815
Utilities	284,122	263,633
Repairs and maintenance	65,128	59,642
Professional fees	604,875	386,108
Dues	32,615	30,587
Insurance	61,889	52,465
Supplies and other	371,568	277,484
Depreciation and amortization	254,588	209,624
Total operating expenses	7,189,982	6,877,458
<b>Operating Loss</b>	<b>(830,706)</b>	<b>(227,050)</b>
<b>Nonoperating Revenues (Expenses)</b>		
Intergovernmental revenue	196,399	179,821
Net investment income (loss)	(21,058)	197,405
Interest expense	(25,255)	(34,898)
Noncapital gifts and grants	31,872	28,894
Total nonoperating revenues	181,958	371,222
<b>Increase (Decrease) in Net Assets</b>	<b>(648,748)</b>	<b>144,172</b>
<b>Net Assets, Beginning of Year</b>	<b>5,136,833</b>	<b>4,992,661</b>
<b>Net Assets, End of Year</b>	<b>\$ 4,488,085</b>	<b>\$ 5,136,833</b>

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Statements of Cash Flows**  
**Years Ended December 31, 2011 and 2010**

	<b>2011</b>	<b>2010</b>
<b>Operating Activities</b>		
Receipts from and on behalf of patients	\$ 6,117,572	\$ 6,862,803
Payments to suppliers and contractors	(2,473,017)	(2,389,351)
Payments to or on behalf of employees	(4,545,087)	(4,266,821)
Other receipts, net	162,771	156,565
Net cash provided by (used in) operating activities	(737,761)	363,196
<b>Noncapital Financing Activities</b>		
Intergovernmental revenue	196,399	179,821
Noncapital gifts and grants	31,872	28,894
Principal paid on short-term debt	-	(150,000)
Net cash provided by noncapital financing activities	228,271	58,715
<b>Capital and Related Financing Activities</b>		
Principal paid on long-term debt	(54,461)	(53,044)
Interest paid on note payable to bank	(26,565)	(32,585)
Purchase of capital assets	(164,679)	(259,913)
Net cash used in capital and related financing activities	(245,705)	(345,542)
<b>Investing Activities</b>		
Net investment income	60,973	44,926
Net change in short-term certificates of deposit	503,748	-
Purchase of intangibles associated with RHC acquisition	(110,000)	-
Maturities of investments	200,000	-
Purchase of investments	(24,040)	(7,935)
Net cash provided by investing activities	630,681	36,991
<b>Increase (Decrease) in Cash and Cash Equivalents</b>	(124,514)	113,360
<b>Cash and Cash Equivalents, Beginning of Year</b>	723,391	610,031
<b>Cash and Cash Equivalents, End of Year</b>	\$ 598,877	\$ 723,391

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Statements of Cash Flows (Continued)**  
**Years Ended December 31, 2011 and 2010**

	2011	2010
<b>Reconciliation of Cash to the Balance Sheets</b>		
Cash and cash equivalents	\$ 550,518	\$ 723,391
Cash held for debt service	48,359	-
	\$ 598,877	\$ 723,391
Total cash	\$ 598,877	\$ 723,391
 <b>Reconciliation of Net Operating Revenues (Expenses) to Net Cash Provided by (Used in) Operating Activities</b>		
Operating loss	\$ (830,706)	\$ (227,050)
Depreciation and amortization	254,588	209,624
Loss on disposal of assets	-	43,463
Changes in operating assets and liabilities		
Patient accounts receivable, net	592,901	(433,337)
Estimated amounts due from and to third-party payers	(671,834)	758,834
Supplies and prepaid expenses	(32,814)	(32,847)
Other current and noncurrent assets	29,835	60,159
Accounts payable and accrued expenses	(79,731)	(15,650)
	\$ (737,761)	\$ 363,196
Net cash provided by (used in) operating activities	\$ (737,761)	\$ 363,196

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

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

***Nature of Operations and Reporting Entity***

Decatur County Hospital (Hospital) is an acute care hospital located in Oberlin, Kansas. The Hospital is a component unit of Decatur County, Kansas (County) and the Board of County Commissioners appoints members to the Board of Trustees of the Hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in the Decatur county area. It also operates a long-term care facility, outpatient clinic and home health agency in the same geographic area.

The Board of Trustees of Decatur County Hospital (Lessor) leases the Hospital's operations to Decatur Health Systems, Inc. (Lessee) (DHS) as a Section 501(c)(3) organization. The lease extends through December 31, 2028. Board members of the Lessor act as the Board of Trustees for the Lessee. At the conclusion of the lease, custody of all assets and liabilities reverts to the Lessor. Rent expense under this lease is \$5 per year plus any amounts due on debt incurred by the Lessor on Lessee's behalf for equipment or for operating purposes.

The financial statements include the accounts of the Hospital and DHS as a blended component unit of the Hospital. All significant intercompany accounts and transactions have been eliminated.

***Basis of Accounting and Presentation***

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

The Hospital prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

***Use of Estimates***

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

***Cash Equivalents***

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2011 and 2010, cash equivalents consisted of certificates of deposit with maturities of less than 90 days.

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to \$250,000.

Pursuant to legislation enacted in 2010, the FDIC will fully insure all noninterest-bearing transaction accounts beginning December 31, 2010 through December 31, 2012, at all FDIC-insured institutions.

***Intergovernmental Revenue***

The Hospital received approximately 3% in both 2011 and 2010, of its financial support from property taxes levied by the County and shared with the Hospital for hospital purposes. One hundred percent of these funds were used to support operations in both years.

Taxes are assessed by the County in November and are received beginning in January of each year. Intergovernmental revenue is recognized in full in the year in which use is first permitted.

***Risk Management***

The Hospital is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than health benefits and workers' compensation. A partially self-funded health insurance plan covers medical services up to a certain amount after which point commercial insurance coverage provides the remaining coverage. Management believes adequate reserves are in place to cover claims incurred but not reported at year-end. Workers' compensation coverage is provided through a fund managed by the KHA Worker's Compensation Fund, Inc. The workers' compensation premiums are subject to retrospective adjustment based upon the overall performance of the fund. Management believes adequate reserves are in place to cover claims incurred but not reported for workers' compensation.

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

The partially self-insured health and dental insurance plan covers medical and dental services up to \$30,000 per individual. Claims in excess of \$30,000 per individual are covered through a reinsurance policy. Management believes adequate accruals are in place to cover claims under \$30,000 which have been incurred but not reported.

***Patient Accounts Receivable***

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the Hospital analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid, or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely).

For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Hospital records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or provided by the policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

***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. The following estimated useful lives are being used by the Hospital:

Land improvements	5 - 20 years
Buildings and building improvements	3 - 21 years
Fixed equipment	8 - 20 years
Major moveable equipment	3 - 15 years

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

***Compensated Absences***

Hospital policies permit most employees to accumulate vacation, holiday, personal and sick leave benefits that may be realized as paid time off or as a cash payment. Expense and the related liability are recognized as benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay rate 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.

***Deferred Revenue***

Deferred revenue consists of grant monies received for specific purposes. Revenue is recognized on deferred grant revenue when specific purpose of grant is met.

***Net Assets***

Net assets of the Hospital are classified in three components. Net assets invested in capital assets, net of related debt, consist 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 assets are 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 assets are remaining assets less remaining liabilities that do not meet the definition of invested in capital assets, net of related debt or restricted expendable.

***Net Patient Service Revenue***

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

***Charity Care***

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

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

***Income Taxes***

As an essential government function of the County, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. DHS is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, DHS is subject to federal income tax on any unrelated business taxable income.

***Reclassifications***

Certain reclassifications have been made to the 2010 financial statements to conform to the 2011 presentation. The reclassifications had no effect on the changes in financial position.

***Subsequent Events***

Subsequent events have been evaluated through the date of the Independent Accountants' Report, which is the date the financial statements were available to be issued.

**Note 2: Net Patient Service Revenue**

The Hospital recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital records a significant provision for bad debts related to uninsured patients in the period the services are provided.

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

*Medicare.* The Hospital is recognized as a Critical Access Hospital (CAH). 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. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor.

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

*Medicaid.* The Medicaid State Plan provides for a cost reimbursement methodology for inpatient and outpatient services rendered to beneficiaries who are not part of a Medicaid managed care network. The Hospital is reimbursed at tentative rates with final settlements determined after submission of annual cost reports and reviews thereof by the Kansas Department of Health and Environment. The Hospital is reimbursed on a prospective payment methodology for inpatient and outpatient services rendered to beneficiaries who are part of a Medicaid managed care network.

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under a prospective reimbursement methodology. Medicaid reimbursement for long-term care facility residents is based on a cost-based prospective reimbursement methodology. The Hospital is reimbursed at a prospective rate with annual cost reports submitted to the Medicaid program. Rates are computed each calendar quarter using an average of the 2005, 2006 and 2007 cost reports and changes in the Medicaid resident case mix index. The Medicaid cost reports are subject to audit by the State and adjustments to rates can be made retroactively. As part of a provider assessment program approved by CMS on February 2, 2011, rates were updated retroactively to July 1, 2010, using 2007, 2008 and 2009 cost report data. Additional net revenues relative to the provider assessment program for the period from July 1, 2010 through June 30, 2011 (the State's fiscal year), were approximately \$100,000 and are included in 2011 net income. Effective July 1, 2011, rates were updated using 2008, 2009 and 2010 cost report data.

Approximately 68% and 64% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2011 and 2010, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

**Note 3: Deposits and Interest Income**

***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.

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

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, 2011 and 2010, respectively, \$218,612 and \$411,050 of the Hospital's bank balances of \$474,885 and \$917,288 were exposed to custodial credit risk as follows:

	<b>2011</b>	<b>2010</b>
Uninsured and collateral held by pledging financial institution's trust department or agent in other than the Hospital's name	<u>\$ 218,612</u>	<u>\$ 411,050</u>

**Summary of Carrying Values**

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

	<b>2011</b>	<b>2010</b>
Carrying value		
Deposits	\$ 474,697	\$ 920,885
Deposits held by a nongovernmental entity - DHS	<u>130,380</u>	<u>312,454</u>
	<u>\$ 605,077</u>	<u>\$ 1,233,339</u>
Included in the following balance sheet captions		
Cash and cash equivalents	\$ 550,518	\$ 723,391
Cash held for debt service	48,359	-
Short-term certificates of deposit	<u>6,200</u>	<u>509,948</u>
	<u>\$ 605,077</u>	<u>\$ 1,233,339</u>

Total investment return is comprised of the following:

	<b>2011</b>	<b>2010</b>
Interest and dividend income	\$ 33,128	\$ 41,401
Realized gains (losses)	27,845	3,525
Unrealized gain (loss) on investments	<u>(82,031)</u>	<u>152,479</u>
	<u>\$ (21,058)</u>	<u>\$ 197,405</u>

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

**Note 4: Patient Accounts Receivable**

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31, 2011 and 2010, consisted of:

	<b>2011</b>	<b>2010</b>
Medicare	\$ 342,061	\$ 846,298
Medicaid	71,753	105,336
Blue Cross	46,779	111,731
Other third-party payers	125,332	137,000
Patients	463,744	470,205
	1,049,669	1,670,570
Less allowance for uncollectible accounts	374,000	402,000
	<u>\$ 675,669</u>	<u>\$ 1,268,570</u>

**Note 5: Investments and Long-term Deposit**

***Interest in Assets of Decatur Health Care Foundation, Inc.***

The Hospital has transferred assets (cash) to the Decatur Health Care Foundation, Inc. (Foundation) and retained a beneficial interest in those assets. Earnings on the funds held by the Foundation are to be remitted to the Hospital, and the principal can be invaded in extreme financial circumstances as determined jointly by the boards of both organizations. Currently, the funds held by the Foundation are invested in certificates of deposit and mutual funds.

***Option Deposit***

On February 4, 2004, DHS entered into an agreement with Decatur County Retirement Housing, Inc. (DCRHI) to manage the Wheat Ridge Terrace independent living units. The management agreement calls for DHS to provide meals, maintenance, housekeeping and administrative services for a fee. Actual costs are used to determine the fees charged. As part of the agreement, DHS invested \$250,000 to assist DCRHI in restructuring its debt. In return, DHS has the option of acquiring the assets of DCRHI when all outstanding debt of DCRHI is paid.



**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

**Note 7: Accounts Payable and Accrued Expenses**

Accounts payable and accrued expenses included in current liabilities at December 31, 2011 and 2010, consisted of:

	<u>2011</u>	<u>2010</u>
Payable to suppliers and contractors	\$ 146,741	\$ 165,695
Payable to employees (including payroll taxes and benefits)	419,156	488,404
Other	7,161	-
	<u>\$ 573,058</u>	<u>\$ 654,099</u>

**Note 8: Self-insured Health Insurance**

Substantially all of the Hospital's employees and their dependents are eligible to participate in the Hospital's employee health insurance plan. The Hospital was self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$30,000 per covered employee. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Hospital's estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability during 2011 and 2010 is summarized as follows:

	<u>2011</u>	<u>2010</u>
Balance, beginning of year	\$ 64,054	\$ 64,054
Current year claims incurred and changes in estimates for claims incurred in prior years	467,555	329,314
Claims and expenses paid	<u>(501,609)</u>	<u>(329,314)</u>
Balance, end of year	<u>\$ 30,000</u>	<u>\$ 64,054</u>

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

**Note 9: Medical Malpractice Claims**

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

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

**Note 10: Long-term Debt**

The following is a summary of long-term debt transactions for the Hospital for the years ended December 31, 2011 and 2010:

	<b>2011</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Payments</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Note payable - county - 2002 (A)	\$ 40,000	\$ -	\$ (20,000)	\$ 20,000	\$ 20,000
Note payable - county - 2003 (B)	34,872	-	(11,103)	23,769	11,616
Note payable - county - 2008 (C)	606,095	-	(23,358)	582,737	24,321
Total long-term debt	<u>\$ 680,967</u>	<u>\$ -</u>	<u>\$ (54,461)</u>	<u>\$626,506</u>	<u>\$ 55,937</u>

	<b>2010</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Payments</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Note payable - county - 2002 (A)	\$ 60,000	\$ -	\$ (20,000)	\$ 40,000	\$ 20,000
Note payable - county - 2003 (B)	45,484	-	(10,612)	34,872	11,103
Note payable - county - 2008 (C)	628,527	-	(22,432)	606,095	23,358
Total long-term debt	<u>\$ 734,011</u>	<u>\$ -</u>	<u>\$ (53,044)</u>	<u>\$680,967</u>	<u>\$ 54,461</u>

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

**Note Payable – County – 2002 (A)**

The note payable – county – 2002 consists of an agreement with the County to repay on its behalf the General Obligation Bonds, Series 2002-A (Bonds) in the original amount of \$200,000 dated July 2, 2002. These Bonds were purchased in their entirety by Prairie Land Electric Cooperative, Inc. at their par value with no interest due on these Bonds pursuant to a Rural Economic Development Loan and Grant Program. The proceeds from this loan were used to finance equipment purchases. The Bonds are payable in annual installments through July 17, 2012. The Hospital is required to make annual payments of \$20,000 to the debt service fund held by the trustee.

The debt service requirements as of December 31, 2011, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2012	<u>\$ 20,000</u>	<u>\$ 20,000</u>	<u>\$ -</u>

**Note Payable – County – 2003 (B)**

The note payable – county – 2003 consists of an agreement with the County to repay on its behalf the General Obligation Bonds, Series 2003, (Bonds) in the original amount of \$100,000 dated March 18, 2003, which bear interest at 4.625%. The proceeds from this loan were used to finance equipment purchases. The Bonds are payable in annual installments through April 1, 2013. The Hospital is required to make annual payments of approximately \$12,716 to the debt service fund held by the trustee. The Bonds are secured by the net revenues and accounts receivable of the Hospital. The debt service requirements as of December 31, 2011, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2012	\$ 12,716	\$ 11,616	\$ 1,100
2013	<u>12,714</u>	<u>12,153</u>	<u>561</u>
	<u>\$ 25,430</u>	<u>\$ 23,769</u>	<u>\$ 1,661</u>

**Note Payable – County – 2008 (C)**

The note payable – county – 2008 consists of an agreement with the County to repay on its behalf the Revenue Bonds, Series 2008, (Bonds) in the original amount of \$650,000 dated February 22, 2008, which bear interest at 4.125%. The proceeds from this loan were used to finance construction of a specialty clinic. The Bonds are payable in annual installments through February 22, 2028. The Hospital is required to make annual payments of approximately \$48,359 to

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

the debt service fund held by the trustee. The Bonds are secured by the net revenues and accounts receivable of the Hospital. The agreement also includes certain financial covenants which, among other things, require monthly deposits of principal and interest payments into a separate Debt Service Account, to the extent necessary to meet on each payment date the payment of all interest and principal. The Hospital did not meet the required deposit covenants during 2011.

The bond document requires the Hospital to comply with certain restrictive covenants including maintaining a debt service coverage ratio of 110% on revenue bonds. As of December 31, 2011, the Hospital did not meet the debt service requirement covenant. Pursuant to the bond resolution the Hospital is required to hire a consultant to make recommendations with respect to charges and rates.

The debt service requirements as of December 31, 2011, are as follows:

<b>Year Ending December 31,</b>	<b>Total to be Paid</b>	<b>Principal</b>	<b>Interest</b>
2012	\$ 48,359	\$ 24,321	\$ 24,038
2013	48,359	25,261	23,098
2014	48,359	26,366	21,993
2015	48,359	27,454	20,905
2016	48,359	28,586	19,773
2017-2021	241,795	161,527	80,268
2022-2026	241,795	197,782	44,013
2027-2028	97,145	91,440	5,705
	<u>\$ 822,530</u>	<u>\$ 582,737</u>	<u>\$ 239,793</u>

**Note 11: Restricted and Designated Net Assets**

At December 31, 2011 and 2010, restricted expendable net assets of \$48,786 were available for debt service.

At December 31, 2011 and 2010, respectively, \$51,897 and \$73,717 of unrestricted net assets have been designated by the Hospital's Board of Trustees for capital acquisitions. Designated net assets remain under the control of the Board of Trustees, which may at its discretion later use these net assets for other purposes.

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

**Note 12: Related Party Transactions**

An officer of a local financial institution is also a member of the Board of Trustees. At December 31, 2011 and 2010, the Hospital had cash balances of approximately \$548,000 and \$597,000 respectively, on deposit with this financial institution.

**Note 13: Pension Plan**

The Hospital contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's required contributions, determined in accordance with the terms of the plan. The plan is administered by the Hospital Board of Trustees. The plan provides retirement benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Hospital's governing body. Contribution rates for plan members and the Hospital expressed as a percentage of covered payroll were 3.9% and 2.1% for 2011, 4.4% and 2.3% for 2010, and 4.1% and 2.2% for 2009, respectively. Contributions actually made by plan members and the Hospital aggregated \$138,447 and \$76,381 during 2011, \$156,775 and \$82,161 during 2010, and \$143,465 and \$77,995 during 2009, respectively.

**Note 14: Contingencies**

***Litigation***

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

**Note 15: Significant Estimates and Concentrations**

***Current Economic Conditions***

The current protracted economic decline continues to present hospitals with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in assets, large declines in contributions, constraints on liquidity and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to the Hospital.

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Notes to Financial Statements**  
**December 31, 2011 and 2010**

Current economic conditions, including the rising unemployment rate, have made it difficult for certain patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net patient service revenue, which could have an adverse impact on the Hospital's future operating results. Further, the effect of economic conditions on the government may have an adverse effect on cash flows related to the Medicare and Medicaid programs.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in allowances for accounts receivable that could negatively impact the Hospital's ability to maintain sufficient liquidity.

## **Supplementary Information**

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Balance Sheets of Decatur Health Systems, Inc.**  
**December 31, 2011 and 2010**

**Assets**

	<u>2011</u>	<u>2010</u>
<b>Current Assets</b>		
Cash	\$ 130,380	\$ 312,454
Patient accounts receivable, net of allowance; 2011 - \$374,000, 2010 - \$402,000	675,669	1,268,570
Other receivables	3,010	17,191
Estimated amounts due from third-party payers	393,000	-
Supplies	106,005	104,962
Prepaid expenses and other	<u>79,745</u>	<u>47,974</u>
Total current assets	<u>1,387,809</u>	<u>1,751,151</u>
<b>Option Deposit</b>	<u>250,000</u>	<u>250,000</u>
<b>Rural Health Clinic acquisition costs, net of accumulated amortization; 2011 - \$27,500, 2010 - \$0</b>	<u>82,500</u>	<u>-</u>
<b>Capital Assets, At Cost</b>		
Property and equipment	1,118,083	1,057,453
Less accumulated depreciation	<u>903,442</u>	<u>874,950</u>
	<u>214,641</u>	<u>182,503</u>
Total assets	<u>\$ 1,934,950</u>	<u>\$ 2,183,654</u>

## Liabilities and Net Assets

	<u>2011</u>	<u>2010</u>
<b>Current Liabilities</b>		
Accounts payable	\$ 146,741	\$ 155,695
Accrued payroll and related deductions	232,968	243,617
Accrued vacation pay	132,300	155,535
Accrued expenses	30,000	64,054
Estimated amounts due to third-party payers	-	278,834
Deferred revenue	7,161	-
	<u>549,170</u>	<u>897,735</u>
<b>Due to Lessor</b>	<u>1,385,780</u>	<u>1,285,919</u>
Total liabilities	<u>1,934,950</u>	<u>2,183,654</u>
<b>Unrestricted Net Assets</b>	<u>-</u>	<u>-</u>
Total liabilities and net assets	<u>\$ 1,934,950</u>	<u>\$ 2,183,654</u>

**Decatur County Hospital**  
**A Component Unit of Decatur County, Kansas**  
**Statements of Operations of Decatur Health Systems, Inc.**  
**Years Ended December 31, 2011 and 2010**

	<u>2011</u>	<u>2010</u>
<b>Revenues, Gains and Other Support</b>		
Net patient service revenue	\$ 6,350,052	\$ 6,751,898
Other revenue	<u>159,771</u>	<u>101,102</u>
	<u>6,509,823</u>	<u>6,853,000</u>
<b>Expenses</b>		
Salaries and wages	3,594,470	3,557,707
Employee benefits	889,840	756,354
Purchased services	417,896	442,256
Drugs	299,477	474,583
Medical supplies	204,808	256,200
Food	108,706	110,815
Utilities	284,122	263,633
Repairs and maintenance	58,032	51,925
Professional fees	604,875	383,950
Dues	32,615	30,587
Insurance	58,261	48,930
Other supplies and expenses	249,672	211,962
Interest	-	4,617
Depreciation and amortization	95,760	62,308
Provision for uncollectible accounts	<u>153,547</u>	<u>214,592</u>
	<u>7,052,081</u>	<u>6,870,419</u>
<b>Operating Loss</b>	<u>(542,258)</u>	<u>(17,419)</u>
<b>Other Income</b>		
Interest income	7,439	5,994
Noncapital gifts and grants	<u>707,588</u>	<u>56,819</u>
	<u>715,027</u>	<u>62,813</u>
<b>Increase in Net Assets</b>	172,769	45,394
<b>Change in Amount Due to Lessor</b>	<u>(172,769)</u>	<u>(45,394)</u>
<b>Change in Unrestricted Net Assets</b>	<u>\$ -</u>	<u>\$ -</u>