

Ness County Hospital District No. 2

Independent Accountants' Report and Financial Statements

December 31, 2011 and 2010



Ness County Hospital District No. 2
December 31, 2011 and 2010

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Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Directors
Ness County Hospital District No. 2
Ness City, Kansas

We have audited the accompanying balance sheets of Ness County Hospital District No. 2 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 Ness County Hospital District No. 2 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 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 Comparison of Revenues and Expenses (Cash Basis) – Actual and Tax Budget listed in the table of contents is presented for purposes of additional analysis and is 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 19, 2012

Ness County Hospital District No. 2
Balance Sheets
December 31, 2011 and 2010

Assets

	<u>2011</u>	<u>2010</u>
Current Assets		
Cash	\$ 322,031	\$ 187,904
Short-term certificates of deposit	228,237	646,302
Restricted cash	22,183	30,866
Patient accounts receivable, net of allowance; 2011 - \$269,000, 2010 - \$259,000	1,098,705	715,142
Property taxes receivable	1,174,304	937,376
Estimated amounts due from Medicaid	90,000	65,000
Due from Medicare for electronic health records incentive	393,747	-
Supplies	132,504	139,055
Prepaid expenses and other	<u>8,141</u>	<u>18,900</u>
Total current assets	<u>3,469,852</u>	<u>2,740,545</u>
Capital Assets, Net	<u>2,839,970</u>	<u>2,718,224</u>
Other Assets		
Deferred financing costs	-	1,601
Farm land	<u>156,142</u>	<u>156,142</u>
	<u>156,142</u>	<u>157,743</u>
Total assets	<u><u>\$ 6,465,964</u></u>	<u><u>\$ 5,616,512</u></u>

Liabilities and Net Assets

	<u>2011</u>	<u>2010</u>
Current Liabilities		
Notes payable to banks, unsecured	\$ 369,340	\$ -
Current maturities of long-term debt	264,606	434,653
Accounts payable	518,743	235,071
Accrued expenses	420,389	367,976
Deferred property tax revenue	1,174,304	937,376
Estimated amounts due to Medicare	<u>100,000</u>	<u>90,000</u>
Total current liabilities	2,847,382	2,065,076
Long-term Debt	<u>149,548</u>	<u>414,154</u>
Total liabilities	<u>2,996,930</u>	<u>2,479,230</u>
Net Assets		
Invested in capital assets, net of related debt	2,392,566	1,869,417
Restricted – expendable for specific operating activities	19,267	23,983
Unrestricted	<u>1,057,201</u>	<u>1,243,882</u>
Total net assets	<u>3,469,034</u>	<u>3,137,282</u>
Total liabilities and net assets	<u>\$ 6,465,964</u>	<u>\$ 5,616,512</u>

Ness County Hospital District No. 2
Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2011 and 2010

	2011	2010
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2011 - \$49,472, 2010 - \$132,221	\$ 6,904,381	\$ 6,519,825
Electronic health records incentive	393,747	-
Other	167,568	209,211
Total operating revenues	7,465,696	6,729,036
Operating Expenses		
Salaries and wages	3,786,282	3,711,935
Employee benefits	1,276,912	1,053,803
Purchased services and professional fees	1,259,206	1,270,334
Supplies and other	1,540,349	1,503,608
Depreciation and amortization	340,744	276,196
Total operating expenses	8,203,493	7,815,876
Operating Loss	(737,797)	(1,086,840)
Nonoperating Revenues (Expenses)		
Property taxes	1,026,890	1,001,950
Interest income	25,216	15,713
Interest expense	(48,913)	(22,551)
Noncapital grants and gifts	38,673	31,369
Oil lease royalties	10,400	-
Farm income	10,207	3,201
Farm expense	(85)	(3,441)
Total nonoperating revenues	1,062,388	1,026,241
Capital Grants and Gifts	7,161	-
Increase (Decrease) in Net Assets	331,752	(60,599)
Net Assets, Beginning of Year	3,137,282	3,197,881
Net Assets, End of Year	\$ 3,469,034	\$ 3,137,282

Ness County Hospital District No. 2
Statements of Cash Flows
Years Ended December 31, 2011 and 2010

	2011	2010
Operating Activities		
Receipts from and on behalf of patients	\$ 6,505,818	\$ 6,747,313
Payments to suppliers and contractors	(2,510,918)	(2,742,186)
Payments to and on behalf of employees	(5,011,686)	(4,788,700)
Other receipts, net	179,448	300,997
Net cash used in operating activities	(837,338)	(482,576)
Noncapital Financing Activities		
Property taxes supporting operations	1,026,890	1,001,950
Noncapital grants and gifts	38,673	31,369
Proceeds from issuance of notes payable	373,700	-
Principal paid on notes payable to banks	(4,360)	(189,000)
Interest paid on notes payable and no fund warrants	(16,319)	(4,272)
Net cash provided by noncapital financing activities	1,418,584	840,047
Capital and Related Financing Activities		
Capital grants and gifts	7,161	-
Proceeds from issuance of long-term debt	-	100,000
Principal paid on long-term debt	(434,653)	(413,644)
Interest paid on long-term debt	(32,594)	(18,279)
Purchase of capital assets	(460,234)	(385,886)
Proceeds from sale of capital assets	715	1,285
Net cash used in capital and related financing activities	(919,605)	(716,524)
Investing Activities		
Interest income received	25,216	15,713
Purchase of certificates of deposit	(130,752)	(115,190)
Maturities of certificates of deposit	548,817	47,526
Oil lease income received	10,400	-
Farm income received	10,207	3,201
Farm expenses paid	(85)	(3,441)
Net cash provided by (used in) investing activities	463,803	(52,191)
Increase (Decrease) in Cash	125,444	(411,244)
Cash, Beginning of Year	218,770	630,014
Cash, End of Year	\$ 344,214	\$ 218,770

Ness County Hospital District No. 2
Statements of Cash Flows (Continued)
Years Ended December 31, 2011 and 2010

	2011	2010
Reconciliation of Cash to the Balance Sheets		
Cash	\$ 322,031	\$ 187,904
Restricted cash	22,183	30,866
Total cash	\$ 344,214	\$ 218,770
Reconciliation of Net Operating Revenues (Expenses) to Net Cash Used in Operating Activities		
Operating loss	\$ (737,797)	\$ (1,086,840)
Depreciation and amortization	340,744	276,196
Loss on disposal of assets	11,880	91,786
Changes in operating assets and liabilities		
Patient accounts receivable, net	(383,563)	243,488
Estimated amounts due from and to Medicare	(408,747)	(16,000)
Accounts payable and accrued expenses	322,835	13,534
Other assets and liabilities	17,310	(4,740)
Net cash used in operating activities	\$ (837,338)	\$ (482,576)
Supplemental Cash Flows Information		
Capital asset additions included in accounts payable	\$ 13,250	\$ -

Ness County Hospital District No. 2

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

Ness County Hospital District No. 2 (Hospital) is an acute care hospital located in Ness City, Kansas. The Hospital is operated by a Board of Directors elected by the qualified voters of the District. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in the Ness County area. It also operates a home health agency in the same geographic area.

The Ness County Health Foundation, Inc. (Foundation) is a legally separate, tax-exempt, not-for-profit organization whose purpose is to raise and hold funds to support the Hospital and its programs. The Board of Directors of the Hospital appoints a voting majority of the Board of the Foundation resulting in the Hospital being financially accountable for the Foundation with the Foundation being included in the Hospital's financial statements as a blended component unit.

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 property taxes, interest 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.

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.

Ness County Hospital District No. 2
Notes to Financial Statements
December 31, 2011 and 2010

Property Taxes

The Hospital received approximately 12% in 2011 and 13% in 2010 of its financial support from property taxes. One hundred percent of these funds were used to support operations.

Property taxes are levied in November of one year and are received beginning in January of the following year. Property tax revenue is recognized in full in the year following the year the taxes were levied, which is the year in which use is first permitted.

Risk Management

The Hospital is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

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 market.

Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements 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	10 – 40 years
Fixed equipment	5 – 25 years
Major moveable equipment	5 – 15 years

Ness County Hospital District No. 2

Notes to Financial Statements

December 31, 2011 and 2010

Deferred Financing Costs

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt using the interest method of amortization.

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.

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.

Ness County Hospital District No. 2

Notes to Financial Statements

December 31, 2011 and 2010

Charity Care

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

Income Taxes

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

Electronic Health Records Incentive Program

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records technology (EHR). Critical access hospitals are eligible to receive incentive payments for up to four years under the Medicare program for its reasonable costs of the purchase of certified EHR technology multiplied by the Hospital's Medicare utilization plus 20%, limited to 100% of the costs incurred. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs are contingent on the hospital continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year under both programs is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Hospital recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

In 2011, the Hospital completed the first-year requirements under both the Medicare and Medicaid programs and has recorded revenue of \$393,747, which is included within operating revenues in the statement of revenues, expenses and changes in net assets.

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.

Ness County Hospital District No. 2

Notes to Financial Statements

December 31, 2011 and 2010

Note 2: Net Patient Service Revenue

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

Medicare. The Hospital is recognized as a Critical Access Hospital (CAH) and is paid at one hundred one percent (101%) of allowable costs for certain inpatient and outpatient services. The Hospital is reimbursed for certain services and cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare administrative contractor. Home health services are paid on a per-episode basis using clinical diagnostic and other factors.

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 by the Hospital 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. Medicaid reimbursement for long-term care facility residents is based on a cost-based prospective reimbursement methodology. 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 \$117,000 and are included in the 2011 net income. Effective July 1, 2011, rates were updated using 2008, 2009 and 2010 cost report data.

Approximately 57% and 59% 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, 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.

Ness County Hospital District No. 2

Notes to Financial Statements

December 31, 2011 and 2010

Note 3: Deposits

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State law requires collateralization of all deposits with federal depository insurance; bonds and other obligations of the U.S. Treasury, U.S. agencies or instrumentalities or the state of Kansas; bonds of any city, county, school district or special road district of the state of Kansas; bonds of any state; or a surety bond having an aggregate value at least equal to the amount of the deposits.

At December 31, 2011 and 2010, respectively, \$192,150 and \$342,011 of the Hospital's bank balance of \$442,410 and \$771,411 was exposed to custodial credit risk as follows:

	2011	2010
Uninsured and collateral held by pledging financial institution's trust department or agent in other than the Hospital's name	\$ 192,150	\$ 342,011

Summary of Carrying Values

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

	2011	2010
Carrying value		
Deposits – Hospital	\$ 423,266	\$ 736,187
Petty cash	345	345
	423,611	736,532
Deposits – Foundation	148,840	128,540
	\$ 572,451	\$ 865,072
Included in the following balance sheet captions:		
Cash	\$ 322,031	\$ 187,904
Short-term certificates of deposit	228,237	646,302
Restricted cash	22,183	30,866
	\$ 572,451	\$ 865,072

Ness County Hospital District No. 2

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 consisted of:

	2011	2010
Medicare	\$ 584,355	\$ 310,118
Medicaid	118,103	76,844
Blue Cross	191,835	129,121
Other third-party payers	146,186	116,322
Patients	327,226	341,737
	1,367,705	974,142
Less allowance for uncollectible accounts	269,000	259,000
	\$ 1,098,705	\$ 715,142

Note 5: Capital Assets

Capital assets activity for the years ended December 31 was:

	2011				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 115,387	\$ -	\$ -	\$ -	\$ 115,387
Land improvements	204,515	-	-	-	204,515
Buildings	4,826,646	42,273	-	30,275	4,899,194
Fixed equipment	779,720	29,703	-	-	809,423
Major moveable equipment	1,333,769	400,793	(18,757)	100,000	1,815,805
Construction in progress	130,275	-	-	(130,275)	-
	7,390,312	472,769	(18,757)	-	7,844,324
Less accumulated depreciation					
Land improvements	195,307	3,510	-	-	198,817
Buildings	3,018,588	123,778	-	-	3,142,366
Fixed equipment	375,559	46,089	-	-	421,648
Major moveable equipment	1,082,634	165,766	(6,877)	-	1,241,523
	4,672,088	339,143	(6,877)	-	5,004,354
Capital Assets, Net	\$ 2,718,224	\$ 133,626	\$ (11,880)	\$ -	\$ 2,839,970

Ness County Hospital District No. 2

Notes to Financial Statements

December 31, 2011 and 2010

	2010				Ending Balance
	Beginning Balance	Additions	Disposals	Transfers	
Land	\$ 115,387	\$ -	\$ -	\$ -	\$ 115,387
Land improvements	204,515	-	-	-	204,515
Buildings	4,841,111	130,478	(144,943)	-	4,826,646
Fixed equipment	725,885	53,835	-	-	779,720
Major moveable equipment	1,310,852	70,013	(47,096)	-	1,333,769
Construction in progress	-	130,275	-	-	130,275
	7,197,750	384,601	(192,039)	-	7,390,312
Less accumulated depreciation					
Land improvements	191,714	3,593	-	-	195,307
Buildings	2,953,132	120,174	(54,718)	-	3,018,588
Fixed equipment	329,142	46,417	-	-	375,559
Major moveable equipment	1,026,024	102,145	(45,535)	-	1,082,634
	4,500,012	272,329	(100,253)	-	4,672,088
Capital Assets, Net	\$ 2,697,738	\$ 112,272	\$ (91,786)	\$ -	\$ 2,718,224

Note 6: Notes Payable to Banks

The Hospital periodically borrows funds from banks to finance operations on an interim basis. The notes payable bear interest at approximately 6.0%, are secured by a certificate of deposit and mature in less than one year from issuance. The following is a summary of short-term notes payable to banks transactions for the years ended December 31:

	2011	2010
Beginning balance	\$ -	\$ 189,000
Additions	373,700	-
Deductions	(4,360)	(189,000)
Ending balance	\$ 369,340	\$ -

Ness County Hospital District No. 2
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 consisted of:

	2011	2010
Payable to suppliers and contractors	\$ 534,371	\$ 249,794
Payable to employees (including payroll taxes and benefits)	404,761	353,253
	\$ 939,132	\$ 603,047

Note 8: Medical Malpractice Coverage and 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 \$300,000 of coverage for each medical incident and \$900,000 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 future.

Ness County Hospital District No. 2
Notes to Financial Statements
December 31, 2011 and 2010

Note 9: Long-term Debt

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

	2011				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt					
Certificates of participation - Series 2008	\$ 560,000	\$ -	\$ 360,000	\$ 200,000	\$ 200,000
Western Cooperative Electric Loan - 2006	105,000	-	17,500	87,500	17,500
Western Cooperative Electric Loan - 2010	100,000	-	20,000	80,000	20,000
Capital lease obligations	83,807	-	37,153	46,654	27,106
Total long-term debt	\$ 848,807	\$ -	\$ 434,653	\$ 414,154	\$ 264,606
	2010				
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt					
Certificates of participation - Series 2008	\$ 910,000	\$ -	\$ 350,000	\$ 560,000	\$ 360,000
Western Cooperative Electric Loan - 2006	122,500	-	17,500	105,000	17,500
Western Cooperative Electric Loan - 2010	-	100,000	-	100,000	20,000
Capital lease obligations	129,951	-	46,144	83,807	37,153
Total long-term debt	\$ 1,162,451	\$ 100,000	\$ 413,644	\$ 848,807	\$ 434,653

Ness County Hospital District No. 2
Notes to Financial Statements
December 31, 2011 and 2010

Certificates of Participation

The certificates of participation consist of Lease Purchase Agreement Refunding Certificates of Participation (Certificates) in the original amount of \$2,845,000 dated January 15, 1999, which bear interest at 4.1% to 5.0%. The Certificates were refinanced on April 1, 2008, in the amount of \$1,378,000 dated March 28, 2008, which bear interest at 2.715%. The Certificates are payable in semi-annual installments through October 1, 2012.

Western Cooperative Electric Loan – 2006

This note payable consists of an agreement with Western Cooperative Electric Association, Inc. in the original amount of \$175,000 dated August 24, 2006, which bears no interest due pursuant to a Rural Economic Development Loan and Grant Program. The proceeds from this loan were used to finance building improvements. The bonds are payable in semi-annual installments through 2016. The Hospital is required to make semi-annual payments of \$8,750 to the debt service fund held by the trustee.

Western Cooperative Electric Loan – 2010

This note payable consists of an agreement with Western Cooperative Electric Association, Inc. in the original amount of \$100,000 dated November 15, 2010, which bears no interest due pursuant to a Rural Economic Development Loan and Grant Program. The proceeds from this loan were used to finance software. The bonds are payable in quarterly installments through 2015. The Hospital is required to make quarterly payments of \$5,000 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,	Certificates of Participation	Western Cooperative Electric Loan 2006	Western Cooperative Electric Loan 2010
2012	\$ 200,000	\$ 17,500	\$ 20,000
2013	-	17,500	20,000
2014	-	17,500	20,000
2015	-	17,500	20,000
2016	-	17,500	-
	\$ 200,000	\$ 87,500	\$ 80,000

Ness County Hospital District No. 2
Notes to Financial Statements
December 31, 2011 and 2010

Capital Lease Obligations

The Hospital is obligated under leases for equipment that are accounted for as a capital lease. Assets under capital lease at December 31, 2011 and 2010, totaled \$53,289 and \$86,690, respectively, net of accumulated depreciation of \$113,713 and \$80,313, respectively. The following is a schedule by year of future minimum lease payments under the capital lease including interest at the rates of 4.50% to 4.54% together with the present value of the future minimum lease payments as of December 31, 2011:

Year Ending December 31,	
2012	\$ 27,106
2013	22,490
Total minimum lease payments	<u>49,596</u>
Less amount representing interest	<u>2,942</u>
Present value of future minimum lease payments	<u><u>\$ 46,654</u></u>

Note 10: Operating Lease

The Hospital entered into a noncancellable operating lease for a CT scanner expiring on April 30, 2013. Rental payments include minimum rentals, plus additional fee per scan above minimum number of scans.

Future minimum lease payments at December 31, 2011, were:

2012	\$ 79,500
2013	<u>26,500</u>
Future minimum lease payments	<u><u>\$ 106,000</u></u>

Rental expense was \$95,765 and \$115,065 for December 31, 2011 and 2010, respectively.

Ness County Hospital District No. 2
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Note 11: 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. The plan provides retirement and death 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 4% each for 2011 and 2010, plus any voluntary contributions up to the federal Internal Revenue Service limit established at an annual basis. Contributions actually made by plan members and the Hospital aggregated \$132,449 and \$96,448 during 2011 and \$154,274 and \$103,974 during 2010, respectively.

Note 12: 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 the fair value of investments and other 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.

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 meet debt covenants or maintain sufficient liquidity.

Supplementary Information

Ness County Hospital District No. 2
Comparison of Revenues and Expenses (Cash Basis) – Actual and Tax Budget
December 31, 2011

	Actual	Tax Budget	Actual Over (Under) Budget
Net patient service revenue	\$ 6,530,818	\$ 6,750,000	\$ (219,182)
Other revenue	<u>167,568</u>	<u>150,000</u>	<u>17,568</u>
Total operating revenue	<u>6,698,386</u>	<u>6,900,000</u>	<u>(201,614)</u>
Operating expenses	8,326,315	8,460,000	(133,685)
Capital expenditures	<u>472,769</u>	<u>780,000</u>	<u>(307,231)</u>
Operating expenses	<u>8,799,084</u>	<u>9,240,000</u>	<u>(440,916)</u>
Operating loss	<u>(2,100,698)</u>	<u>(2,340,000)</u>	<u>239,302</u>
Property tax revenue	1,026,890	1,020,211	6,679
Other nonoperating revenues	<u>63,804</u>	<u>38,500</u>	<u>25,304</u>
Total nonoperating revenues	<u>1,090,694</u>	<u>1,058,711</u>	<u>31,983</u>
Deficiency of revenue over expenses	<u><u>\$ (1,010,004)</u></u>	<u><u>\$ (1,281,289)</u></u>	<u><u>\$ 271,285</u></u>

Note: The above schedule reflects a comparison of current year operations and the tax budget.