# Grisell Memorial Hospital District No. 1

Independent Auditor's Report and Financial Statements

December 31, 2012 and 2011

BKD LLP
CPAs & Advisors

# Grisell Memorial Hospital District No. 1

**December 31, 2012 and 2011**

## Contents

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# Independent Auditor's Report

Board of Directors
Grisell Memorial Hospital District No. 1
Ransom, Kansas

We have audited the accompanying financial statements of Grisell Memorial Hospital District No. 1, which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the provisions of the Kansas Municipal Audit and Accounting Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Grisell Memorial Hospital District No. 1 as of December 31, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Required Supplementary Information***

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. Our opinion on the basic financial statements is not affected by this missing information.

BKD, LLP

Wichita, Kansas
May 28, 2013

# Grisell Memorial Hospital District No. 1
## Balance Sheets
## December 31, 2012 and 2011

## Assets

| | 2012 | 2011 |
|---|---|---|
| **Current Assets** | | |
| Cash | $ 768,533 | $ 377,687 |
| Certificates of deposit | 696,664 | 740,196 |
| Patient accounts receivable, net | 414,511 | 489,021 |
| Estimated amounts due from third-party payers | 50,000 | 280,000 |
| Interest receivable | 2,433 | 4,023 |
| Supplies | 57,614 | 58,196 |
| Prepaid expenses and other | 28,809 | 56,394 |
| Property taxes receivable | 897,955 | 797,966 |
| Total current assets | 2,916,519 | 2,803,483 |
| **Noncurrent Cash and Investments** | 812,995 | 861,357 |
| **Capital Assets** | | |
| Land | 4,000 | 4,000 |
| Depreciable capital assets, net of accumulated depreciation | 1,555,018 | 425,669 |
| Total capital assets, net of accumulated depreciation | 1,559,018 | 429,669 |
| Total assets | $ 5,288,532 | $ 4,094,509 |

*See Notes to Financial Statements*

## Liabilities and Net Position

| | 2012 | 2011 |
|---|---|---|
| **Current Liabilities** | | |
| Current maturities of capital lease obligations | $ 81,075 | $ 10,986 |
| Accounts payable | 99,914 | 103,067 |
| Salaries payable | 137,727 | 141,270 |
| Payroll taxes payable | 50,033 | 48,575 |
| Accrued benefits payable | 85,267 | 82,128 |
| Deferred property tax revenue | 897,955 | 797,966 |
| Total current liabilities | 1,351,971 | 1,183,992 |
| **Capital Lease Obligations** | 707,065 | 38,140 |
| Total liabilities | 2,059,036 | 1,222,132 |
| **Net Position** | | |
| Net investment in capital assets | 770,878 | 380,543 |
| Restricted - expendable for Specific operating activities | 28,885 | 32,485 |
| Unrestricted | 2,429,733 | 2,459,349 |
| Total net position | 3,229,496 | 2,872,377 |
| Total liabilities and net position | $ 5,288,532 | $ 4,094,509 |

# Grisell Memorial Hospital District No. 1

## Statements of Revenues, Expenses and Changes in Net Position

## Years Ended December 31, 2012 and 2011

| | 2012 | 2011 |
|---|---|---|
| **Operating Revenues** | | |
| Net patient service revenue | $ 3,793,447 | $ 3,998,078 |
| Contract services | 47,521 | 53,363 |
| Clinic rentals | 18,000 | 31,200 |
| Ambulance subsidy | 24,000 | 24,000 |
| Other | 62,777 | 57,450 |
| Total operating revenues | 3,945,745 | 4,164,091 |
| **Operating Expenses** | | |
| Salaries and wages | 2,334,812 | 2,319,004 |
| Supplies and other | 1,975,498 | 2,038,735 |
| Depreciation | 91,172 | 92,403 |
| Total operating expenses | 4,401,482 | 4,450,142 |
| **Operating Loss** | (455,737) | (286,051) |
| **Nonoperating Revenues (Expenses)** | | |
| Property taxes | 777,960 | 736,346 |
| Interest income | 15,204 | 20,539 |
| Noncapital grants and gifts | 23,176 | 43,553 |
| Interest expense | (3,534) | (2,444) |
| Gain (loss) on disposal of capital assets | 50 | (1,772) |
| Total nonoperating revenues (expenses) | 812,856 | 796,222 |
| **Increase in Net Position** | 357,119 | 510,171 |
| **Net Position, Beginning of Year** | 2,872,377 | 2,362,206 |
| **Net Position, End of Year** | $ 3,229,496 | $ 2,872,377 |

# Grisell Memorial Hospital District No. 1

## Statements of Cash Flows

## Years Ended December 31, 2012 and 2011

| | 2012 | 2011 |
|---|---|---|
| **Operating Activities** | | |
| Receipts from and on behalf of patients | $ 4,097,957 | $ 3,804,824 |
| Payments to employees | (2,335,216) | (2,302,500) |
| Payments to suppliers and contractors | (1,949,026) | (2,026,144) |
| Other receipts, net | 152,298 | 166,013 |
| Net cash used in operating activities | (33,987) | (357,807) |
| **Noncapital Financing Activities** | | |
| Property taxes supporting operations | 777,960 | 736,346 |
| Noncapital grants and gifts | 23,176 | 43,553 |
| Net cash provided by noncapital financing activities | 801,136 | 779,899 |
| **Capital and Related Financing Activities** | | |
| Purchase of capital assets | (470,521) | (90,163) |
| Principal paid on capital lease obligations | (10,986) | (8,617) |
| Interest paid on capital lease obligations | (3,534) | (2,444) |
| Proceeds on sale of capital assets | 50 | 300 |
| Net cash used in capital and related financing activities | (484,991) | (100,924) |
| **Investing Activities** | | |
| Interest income received | 17,931 | 23,183 |
| Net change in certificates of deposit | 43,532 | (157,203) |
| Net change in noncurrent investments | 42,675 | (160,366) |
| Net cash provided by (used in) investing activities | 104,138 | (294,386) |
| **Increase in Cash** | 386,296 | 26,782 |
| **Cash, Beginning of Year** | 407,422 | 380,640 |
| **Cash, End of Year** | $ 793,718 | $ 407,422 |
| **Reconciliation of Cash to the Balance Sheets** | | |
| Cash in current assets | $ 768,533 | $ 377,687 |
| Cash in noncurrent cash and investments | 25,185 | 29,735 |
| | $ 793,718 | $ 407,422 |

# Grisell Memorial Hospital District No. 1
## Statements of Cash Flows (Continued)
## Years Ended December 31, 2012 and 2011

| | 2012 | 2011 |
|---|---|---|
| **Reconciliation of Net Operating Revenue to Net Cash Used in Operating Activities** | | |
| Operating loss | $ (455,737) | $ (286,051) |
| Depreciation | 91,172 | 92,403 |
| Provision for uncollectible accounts | 16,170 | 34,184 |
| Changes in operating assets and liabilities | | |
| Patient accounts receivable, net | 58,340 | (152,438) |
| Estimated amounts due from/to third-party payers | 230,000 | (75,000) |
| Supplies | 582 | (4,021) |
| Prepaid expenses and other current assets | 27,585 | 1,855 |
| Accounts payable and accrued expenses | (2,099) | 31,261 |
| Net cash used in operating activities | $ (33,987) | $ (357,807) |
| **Supplemental Cash Flows Information** | | |
| Capital lease obligations incurred for capital assets | $ 750,000 | $ 24,328 |

# Grisell Memorial Hospital District No. 1
## Notes to Financial Statements
## December 31, 2012 and 2011

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

### *Nature of Operations and Reporting Entity*

Grisell Memorial Hospital District No. 1 (Hospital District), located in Ransom, Kansas, is organized and operating under Kansas law and is governed by a Board of Directors. The Hospital District operates a hospital which provides acute and long-term care services and operates outpatient clinics.

### *Basis of Accounting and Presentation*

The financial statements of the Hospital District 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 (principally tax appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific (such as tax appropriations), investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital District first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net positions are available.

The Hospital District prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB).

### *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 District considers all liquid investments with original maturities of three months or less to be cash equivalents. There were no cash equivalents at December 31, 2012 and 2011.

At December 31, 2012, the Hospital District's cash accounts did not exceed federally insured limits.

Pursuant to legislation enacted in 2010, the FDIC fully insured all noninterest-bearing transaction accounts beginning December 31, 2010 through December 31, 2012, at all FDIC-insured institutions. This legislation expired on December 31, 2012. Beginning January 1, 2013, noninterest-bearing transaction accounts are subject to the $250,000 limit on FDIC insurance per covered institution.

### *Budgetary Principles*

The Hospital District is required by state statutes to adopt an annual budget for its general funds on or before August 25 for the ensuing year. The Hospital District's Board of Directors may amend the budget by transferring budgeted amounts from one object or purpose to another within the same fund. Expenditures may not legally exceed the total amount of the adopted budget of individual funds.

### *Property Taxes*

The Hospital District received approximately 16% and 15% of its financial support from property taxes in 2012 and 2011, respectively. One hundred percent of these funds were used to support operations in both years.

In accordance with governing state statutes, property taxes levied during the current year are a revenue source to be used to finance the budget of the ensuing year. Taxes are assessed on a calendar year tax basis and become a lien on the property on November 1 of each year. The county treasurer is the tax collection agent for all taxing entities within the County. Property owners have the option of paying one-half or the full amount of the taxes levied on or before December 20 during the year levied with the balance to be paid on or before May 10 of the ensuing year. State statutes prohibit the county treasurer from distributing taxes collected in the year levied prior to January 1 of the ensuing year. Consequently, for revenue recognition purposes, the taxes levied during the current year are not due and receivable until the ensuing year. At December 31, such taxes are a lien on the property and are recorded as property taxes receivable, net of anticipated delinquencies, with a corresponding amount recorded as deferred property tax revenue on the balance sheets.

### *Risk Management*

The Hospital District 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*

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

For receivables associated with services provided to patients who have third-party coverage, the Hospital District analyzes contractually due amounts and provides an allowance for uncollectible accounts and a provision for uncollectible accounts, 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 District records a significant provision for uncollectible accounts 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 policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for uncollectible accounts.

The Hospital District's allowance for uncollectible accounts is based on 100% of account balances in excess of 150 days (excluding Medicare accounts) outstanding from the date of discharge or service.

### *Supplies*

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

### *Capital Assets*

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital District:

| | |
|---|---|
| Land improvements | 8-15 years |
| Buildings | 10-40 years |
| Fixed equipment | 5-20 years |
| Moveable equipment | 5-20 years |

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. When depreciable property is retired or otherwise disposed of, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is reflected in nonoperating revenues (expenses).

### *Compensated Absences*

Hospital District 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. 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 rates in effect at the balance sheet date.

### *Net Position*

Net position of the Hospital District is classified in three components. Net investment in capital assets, consist of capital assets, net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase of those assets. Restricted expendable net position represents noncapital assets that must be used for a particular purpose as specified by grantors or donors external to the Hospital District. Unrestricted net position represents remaining assets less remaining liabilities that do not meet the above conditions.

### *Net Patient Service Revenue*

The Hospital District has agreements with third-party payers that provide for payments to the Hospital District at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and include estimated retroactive revenue adjustments 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 District 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 District 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 District is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Hospital District 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 District'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 (CMS). 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 District will recognize 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.

The Hospital District has not received or recognized any revenue for the incentive payments in the accompanying financial statements.

### *Subsequent Events*

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

## Note 2: 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 District'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, 2012 and 2011, none of the Hospital District's deposits (checking and savings accounts and certificates of deposit) were exposed to custodial credit risk.

All certificates of deposit have maturities of one year or less and are reported at cost, which approximates fair value.

The carrying amounts of deposits are included in the Hospital District's balance sheet captions as follows at December 31, 2012 and 2011:

| | 2012 | 2011 |
|---|---|---|
| Cash | $ 768,283 | $ 377,437 |
| Certificates of deposit | 696,664 | 740,196 |
| Noncurrent cash and investments | 807,478 | 855,653 |
| | $ 2,272,425 | $ 1,973,286 |

## Note 3: Patient Accounts Receivable, Net/Net Patient Service Revenue

The Hospital District 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 District recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of the Hospital District's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital District records a significant provision for uncollectible accounts related to uninsured patients in the period the services are provided. This provision for uncollectible accounts is presented as a component of net patient service revenue.

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

*Medicare.* The Hospital District is recognized as a Critical Access Hospital (CAH). Under CAH rules, inpatient acute care and skilled swing-bed and certain outpatient services rendered to Medicare program beneficiaries are paid at one hundred one percent (101%) of allowable cost subject to certain limitations. Other outpatient services related to Medicare beneficiaries are paid based on fee schedules and cost reimbursement methodologies, subject to certain limitations. The Hospital District is reimbursed for most services at tentative rates with final settlement determined after submission of an annual cost report by the Hospital District and audits thereof by the Medicare administrative contractor.

*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 District is reimbursed for inpatient (excluding long-term care) and outpatient services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital District with audit thereof by the Kansas Department of Health and Environment. The Hospital District 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. The Hospital District is reimbursed at a prospective rate, with annual cost reports submitted to the Medicaid program. Prior to 2011 rates were computed each calendar quarter using an average of the 2005, 2006 and 2007 cost reports and changes in the Medicaid resident case mix index. 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 $116,000 and are included in 2011 operating revenues. Effective July 1, 2011, rates were updated using 2008, 2009 and 2010 cost report data. Rates were not rebased or inflated as of July 1, 2012. The Medicaid cost reports are subject to audit by the state and adjustments to rates can be made retroactively.

Approximately 75% and 76% of net patient service revenues are from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2012 and 2011, 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 District has also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Hospital District under these agreements includes prospectively determined case rates and discounts from established charges.

Accounts receivable are recorded net of the allowance for uncollectible accounts and allowance for contractual adjustments at December 31, 2012 and 2011, as follows:

| | 2012 | 2011 |
|---|---|---|
| Gross patient accounts receivable | | |
| Medicare | $ 126,805 | $ 192,472 |
| Medicaid | 77,271 | 77,032 |
| Blue Cross | 69,507 | 39,484 |
| Other third-party payers | 43,235 | 35,785 |
| Self-pay | 244,589 | 232,768 |
| | 561,407 | 577,541 |
| Less allowance for uncollectible accounts | (180,454) | (182,237) |
| Plus allowance for contractual adjustments | 33,558 | 93,717 |
| Patient accounts receivable, net | $ 414,511 | $ 489,021 |

Net patient service revenue for the years ended December 31, 2012 and 2011, are as follows:

| | 2012 | 2011 |
|---|---|---|
| Gross patient service revenue | $ 3,102,280 | $ 3,174,723 |
| Plus (less): | | |
| Contractual adjustments | | |
| Medicare | 697,152 | 763,805 |
| Medicaid | 182,837 | 229,219 |
| Blue Cross | (127,870) | (78,296) |
| Other | (25,855) | (24,844) |
| Administrative adjustments | (9,042) | (21,859) |
| Charity care | (9,885) | (10,486) |
| Provision for uncollectible accounts | (16,170) | (34,184) |
| Net patient service revenue | $ 3,793,447 | $ 3,998,078 |

### *Patient Protection and Affordable Care Act*

The *Patient Protection and Affordable Care Act* (PPACA) will substantially reform the United States health care system. The legislation impacts multiple aspects of the health care system, including many provisions that change payments from Medicare, Medicaid and insurance companies. Starting in 2014, the legislation requires the establishment of health insurance exchanges, which will provide individuals without employer provided health care coverage the opportunity to purchase insurance. It is anticipated that some employers currently offering insurance to employees will opt to have employees seek insurance coverage through the insurance exchanges. It is possible that the reimbursement rates paid by insurers participating in the insurance exchanges may be substantially different than rates paid under current health insurance products. Another significant component of the PPACA is the expansion of the Medicaid program to a wide range of newly eligible individuals. In anticipation of this expansion, payments under certain existing programs, such as Medicare disproportionate share, will be substantially decreased. Each state's participation in an expanded Medicaid program is optional.

The state of Kansas has not yet indicated whether or not it will participate in the expansion of the Medicaid program. The legislature has passed HCR 5013 indicating it does not intend to pursue Medicaid expansion, however, that is not yet law as of the date of this report. The impact of that decision on the overall reimbursement of the Hospital District cannot be quantified at this point.

The PPACA is extremely complex and may be difficult for the federal government and each state to implement. While the overall impact of the PPACA cannot currently be estimated, it is possible that it will have a negative impact on the Hospital District's net patient service revenue. Additionally, it is possible the Hospital District will experience payment delays and other operational challenges during the PPACA's implementation.

## Note 4: Concentration of Credit Risk

The Hospital District grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer arrangements. The mix of accounts receivable net of allowance for uncollectible accounts and contractual allowances at December 31, 2012 and 2011, were as follows:

| | 2012 | 2011 |
|---|---|---|
| Medicare | 47% | 61% |
| Medicaid | 20 | 17 |
| Blue Cross | 12 | 6 |
| Other third-party payers | 4 | 5 |
| Self-pay | 17 | 11 |
| | 100% | 100% |

## Note 5: Noncurrent Cash and Investments

Noncurrent cash and investments include 1) funds internally designated by the Board of Directors to be used for physician recruitment and replacement of capital assets or for the purchase of additional capital assets and 2) funds externally restricted by donors and grantors for student scholarships/loans and other specific purposes. The internally designated funds may be used for other purposes by action of the Board of Directors. Noncurrent cash and investments consist of certificates of deposit, savings accounts and interest receivable.

The externally restricted assets totaled $28,885 and $32,485 at December 31, 2012 and 2011, respectively.

### Note 6: Capital Assets

Capital assets activity for the years ended December 31, 2012 and 2011, was:

| | 2012 | | | |
|---|---|---|---|---|
| | Beginning Balance | Additions | Disposals | Ending Balance |
| Land | $ 4,000 | $ - | $ - | $ 4,000 |
| Land improvements | 45,537 | - | - | 45,537 |
| Buildings | 1,430,083 | - | - | 1,430,083 |
| Fixed equipment | 200,250 | 1,175,300 | (589) | 1,374,961 |
| Moveable equipment | 713,126 | 45,221 | (5,893) | 752,454 |
| | 2,392,996 | 1,220,521 | (6,482) | 3,607,035 |
| Less accumulated depreciation | | | | |
| Land improvements | 39,582 | 803 | - | 40,385 |
| Buildings | 1,193,306 | 30,277 | - | 1,223,583 |
| Fixed equipment | 195,500 | 776 | (589) | 195,687 |
| Moveable equipment | 534,939 | 59,316 | (5,893) | 588,362 |
| | 1,963,327 | 91,172 | (6,482) | 2,048,017 |
| Capital Assets, Net | $ 429,669 | $ 1,129,349 | $ - | $ 1,559,018 |

| | 2011 | | | |
|---|---|---|---|---|
| | Beginning Balance | Additions | Disposals | Ending Balance |
| Land | $ 4,000 | $ - | $ - | $ 4,000 |
| Land improvements | 45,537 | - | - | 45,537 |
| Buildings | 1,430,083 | - | - | 1,430,083 |
| Fixed equipment | 205,537 | - | (5,287) | 200,250 |
| Moveable equipment | 724,624 | 114,490 | (125,988) | 713,126 |
| | 2,409,781 | 114,490 | (131,275) | 2,392,996 |
| Less accumulated depreciation | | | | |
| Land improvements | 38,779 | 803 | - | 39,582 |
| Buildings | 1,161,311 | 31,995 | - | 1,193,306 |
| Fixed equipment | 199,963 | 824 | (5,287) | 195,500 |
| Moveable equipment | 600,077 | 58,781 | (123,919) | 534,939 |
| | 2,000,130 | 92,403 | (129,206) | 1,963,327 |
| Capital Assets, Net | $ 409,651 | $ 22,087 | $ (2,069) | $ 429,669 |

### Note 7: Capital Lease Obligations

Capital lease obligation activity for the years ended December 31, 2012 and 2011, was:

| | 2012 | | | | |
|---|---|---|---|---|---|
| | Beginning Balance | Additions | Deductions | Ending Balance | Amounts Due Within One Year |
| Capital lease obligations | $ 49,126 | $ 750,000 | $ (10,986) | $ 788,140 | $ 81,075 |

| | 2011 | | | | |
|---|---|---|---|---|---|
| | Beginning Balance | Additions | Deductions | Ending Balance | Amounts Due Within One Year |
| Capital lease obligations | $ 33,415 | $ 24,328 | $ (8,617) | $ 49,126 | $ 10,986 |

A schedule of the cost and accumulated depreciation on equipment under capital leases at December 31, 2012 and 2011, is as follows:

| | 2012 | 2011 |
|---|---|---|
| Fixed and moveable equipment | $ 811,799 | $ 61,799 |
| Accumulated amortization | (26,836) | (15,035) |
| | $ 784,963 | $ 46,764 |

The following is a schedule by year of future minimum lease payments under the capital lease including interest rates of 2.75% to 6.96% together with the present value of the future minimum lease payments:

| | | |
|---|---|---|
| Year ending December 31, | | |
| 2013 | $ | 100,441 |
| 2014 | | 94,952 |
| 2015 | | 89,463 |
| 2016 | | 89,463 |
| 2017 | | 89,463 |
| 2018 - 2022 | | 443,774 |
| Total minimum lease payments | | 907,556 |
| Less amount representing interest | | 119,416 |
| Present value of future minimum lease payments | $ | 788,140 |

## Note 8: Medical Malpractice Coverage and Claims

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

## Note 9: Pension Plan

The Hospital District maintains a contributory defined contribution pension plan for all eligible employees. Eligibility is established by all employees 18 years of age or older who have completed one year of service. The plan provides elective employee contributions of 2.5% of the first $16,000 of annual compensation and 5% of annual compensation in excess of $16,000. Matching employer contributions are computed at 5% of the first $16,000 of annual compensation and 10% of annual compensation in excess of $16,000.

Benefits are funded by a tax deferred annuity contract issued by an insurance company. The plan is funded for past service on an installment basis over the remaining duration of employment from the effective date of the plan to the employee's normal retirement date. Benefits begin to vest after one year of service with 100% vesting after five years of service. All funds contributed by the Hospital District, which are not vested, will be returned to the plan and remain in the plan to reduce future employer contributions to the plan. Contributions actually made by plan members totaled $125,241 and $105,723 in 2012 and 2011, respectively. Hospital District contributions totaled $164,575 and $144,882 in 2012 and 2011, respectively.

## Note 10: Management Agreement

The Board of Directors of the Hospital District has a management agreement with Great Plains Health Alliance, Inc. (GPHA), whereby GPHA agreed to administer operations of the Hospital District and shared services for a fee. Fees incurred under the management agreement were $69,907 and $67,218 for 2012 and 2011, respectively. Accounts payable to GPHA related to the agreement were $6,450 and $6,297 at December 31, 2012 and 2011, respectively.

## Note 11: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

### *Allowance for Net Patient Service Revenue Adjustments*

Estimates of allowances for adjustments included in net patient service revenue are described in *Notes 1* and *3*.

### *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 District.

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 District'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 District's ability to maintain sufficient liquidity.