

**Board of Trustees of Kiowa County Memorial Hospital
A Component Unit of Kiowa County, Kansas**

Independent Auditor's Report and Financial Statements

December 31, 2012 and 2011



Board of Trustees of Kiowa County Memorial Hospital
A Component Unit of Kiowa County, Kansas
December 31, 2012 and 2011

Contents

Independent Auditor's Report on Financial Statements and Supplementary Information.....	1
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Financial Statements

Balance Sheets.....	3
Statements of Revenues, Expenses and Changes in Net Position	4
Statements of Cash Flows	5
Notes to Financial Statements	7

Supplementary Information

Insurance Coverage	22
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Independent Auditor's Report on Financial Statements and Supplementary Information

Board of Trustees
Kiowa County Memorial Hospital
Greensburg, Kansas

We have audited the accompanying financial statements of the Board of Trustees of Kiowa County Memorial Hospital (Board of Trustees) and its discretely presented component unit, Great Plains of Kiowa County, Inc. (Hospital), collectively a component unit of Kiowa County, Kansas, which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of revenue, 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 opinions 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 opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Board of Trustees and of its discretely presented component unit, the Hospital, as of December 31, 2012 and 2011, and the respective 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.

Supplementary Information

Our audits were conducted for the purpose of forming opinions on the financial statements as a whole. The supplementary schedule listed in the table of contents is 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 audits 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

Wichita, Kansas
June 10, 2013

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Balance Sheets

December 31, 2012 and 2011

Assets

	Board of Trustees		Hospital	
	2012	2011	2012	2011
Current Assets				
Cash	\$ 1,111,424	\$ 440,590	\$ 570,808	\$ 762,185
Cash held for debt service	-	-	29,716	29,742
Short-term certificates of deposit	67,015	66,439	-	-
Patient accounts receivable, net of allowance; 2012 – \$122,559, 2011 – \$157,556	-	-	729,318	637,318
Property taxes receivable	1,004,115	999,978	-	-
Estimated amounts due from third-party payers	-	-	245,000	180,000
Contribution receivable	500,000	-	-	-
Supplies	-	-	122,306	109,233
Prepaid expenses and other	466	555	143,601	134,206
Total current assets	2,683,020	1,507,562	1,840,749	1,852,684
Noncurrent Cash and Investments				
Certificates of deposit	365,706	360,077	-	-
Cash restricted for capital acquisitions and specific operating activities	-	-	59,573	74,922
	365,706	360,077	59,573	74,922
Capital Assets, Net	-	-	19,738,197	21,409,580
Other Assets				
Noncurrent portion of prepaid maintenance contract	-	-	173,854	253,455
Bond issuance costs, net of amortization	-	-	2,613	2,728
	-	-	176,467	256,183
Total assets	\$ 3,048,726	\$ 1,867,639	\$ 21,814,986	\$ 23,593,369

Liabilities and Net Position

	Board of Trustees		Hospital	
	2012	2011	2012	2011
Current Liabilities				
Current maturities of long-term debt	\$ -	\$ -	\$ 32,747	\$ 1,608,439
Accounts payable	-	-	62,514	121,760
Accrued expenses	-	-	431,346	412,305
Accrued interest payable	-	-	-	209,573
Deferred property tax revenue	1,004,115	999,978	-	-
Total current liabilities	1,004,115	999,978	526,607	2,352,077
Long-term Debt	-	-	2,099,389	2,158,308
Total liabilities	1,004,115	999,978	2,625,996	4,510,385
Net Position				
Net investment in capital assets	-	-	17,606,061	19,242,833
Restricted - expendable for				
Capital acquisitions	-	-	10,458	2,173
Debt service	-	-	29,716	29,742
Specific operating activities	-	-	49,106	76,416
Unrestricted	2,044,611	867,661	1,493,649	(268,180)
Total net position	2,044,611	867,661	19,188,990	19,082,984
Total liabilities and net position	\$ 3,048,726	\$ 1,867,639	\$ 21,814,986	\$ 23,593,369

Board of Trustees of Kiowa County Memorial Hospital
A Component Unit of Kiowa County, Kansas
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2012 and 2011

	Board of Trustees		Hospital	
	2012	2011	2012	2011
Operating Revenues				
Net patient service revenue, net of provision for uncollectible accounts; 2012 – \$291,060, 2011 – \$240,480	\$ -	\$ -	\$ 5,050,275	\$ 4,731,343
Property taxes to support operations	972,863	862,086	165,149	149,623
Other	-	60	49,783	52,324
Total operating revenues	972,863	862,146	5,265,207	4,933,290
Operating Expenses				
Salaries and wages	-	-	2,935,860	2,733,129
Supplies and other	236	255	2,669,976	3,163,425
Depreciation and amortization	-	-	1,836,770	1,792,117
Total operating expenses	236	255	7,442,606	7,688,671
Operating Income (Loss)	972,627	861,891	(2,177,399)	(2,755,381)
Nonoperating Revenues (Expenses)				
Interest income	9,512	4,172	1,814	3,928
Interest expense	-	-	(114,184)	(150,733)
Noncapital grants and gifts	501,830	-	22,880	14,583
Forgiveness of accrued interest on FEMA note	-	-	239,713	-
Transfer to City	-	-	-	(19,368)
Contribution from County	-	360,077	-	-
Noncapital contributions between Board of Trustees and Hospital	(331,805)	(1,167,675)	331,805	1,167,675
Total nonoperating revenues (expenses)	179,537	(803,426)	482,028	1,016,085
Excess (Deficiency) of Revenues Over Expenses Before Capital Grants, Gifts and Contributions	1,152,164	58,465	(1,695,371)	(1,739,296)
Capital Grants and Gifts	226,163	1,270,333	-	41,400
Forgiveness of Principal on FEMA Note	-	-	1,600,000	-
Capital Contributions Between Board of Trustees and Hospital	(201,377)	(890,215)	201,377	890,215
Increase (Decrease) in Net Position	1,176,950	438,583	106,006	(807,681)
Net Position, Beginning of Year	867,661	429,078	19,082,984	19,890,665
Net Position, End of Year	\$ 2,044,611	\$ 867,661	\$ 19,188,990	\$ 19,082,984

Board of Trustees of Kiowa County Memorial Hospital
A Component Unit of Kiowa County, Kansas
Statements of Cash Flows
Years Ended December 31, 2012 and 2011

	Board of Trustees		Hospital	
	2012	2011	2012	2011
Operating Activities				
Receipts from and on behalf of patients	\$ -	\$ -	\$ 4,893,275	\$ 4,900,254
Payments to suppliers and contractors	(236)	(255)	(2,647,060)	(3,177,208)
Payments to and on behalf of employees	-	-	(2,916,819)	(2,681,617)
Cash received from County	972,863	862,086	165,149	149,623
Other receipts, net	-	-	51,944	57,209
	<u>972,627</u>	<u>861,831</u>	<u>(453,511)</u>	<u>(751,739)</u>
Net cash provided by (used in) operating activities				
Noncapital Financing Activities				
Noncapital grants and gifts	1,830	-	22,880	14,583
Transfer to City	-	-	-	(19,368)
Noncapital contributions between Board of Trustees and Hospital	(331,805)	(1,167,675)	331,805	1,167,675
	<u>(329,975)</u>	<u>(1,167,675)</u>	<u>354,685</u>	<u>1,162,890</u>
Net cash provided by (used in) noncapital financing activities				
Capital and Related Financing Activities				
Principal paid on long-term debt	-	-	(34,611)	(24,841)
Interest paid on long-term debt	-	-	(84,044)	(86,777)
Funds received from Kansas Division of Emergency Management	-	20,207	-	-
Capital contributions between Board of Trustees and Hospital	(201,377)	(890,215)	201,377	890,215
Capital grants and gifts	226,163	1,270,393	-	41,400
Purchase of capital assets	-	-	(193,100)	(979,640)
Proceeds on disposal of capital assets	-	-	638	-
	<u>24,786</u>	<u>400,385</u>	<u>(109,740)</u>	<u>(159,643)</u>
Net cash provided by (used in) capital and related financing activities				

Board of Trustees of Kiowa County Memorial Hospital
A Component Unit of Kiowa County, Kansas
Statements of Cash Flows (Continued)
Years Ended December 31, 2012 and 2011

	Board of Trustees		Hospital	
	2012	2011	2012	2011
Investing Activities				
Interest income received	\$ 9,601	\$ 4,172	\$ 1,814	\$ 3,928
Net (increase) decrease in certificates of deposit	(6,205)	(835)	-	-
Net cash provided by investing activities	3,396	3,337	1,814	3,928
Increase (Decrease) in Cash	670,834	97,878	(206,752)	255,436
Cash, Beginning of Year	440,590	342,712	866,849	611,413
Cash, End of Year	<u>\$ 1,111,424</u>	<u>\$ 440,590</u>	<u>\$ 660,097</u>	<u>\$ 866,849</u>
Reconciliation of Cash to the Balance Sheets				
Cash	\$ 1,111,424	\$ 440,590	\$ 570,808	\$ 762,185
Cash held for debt service	-	-	29,716	29,742
Cash restricted for capital acquisitions and specific operating activities	-	-	59,573	74,922
Total cash	<u>\$ 1,111,424</u>	<u>\$ 440,590</u>	<u>\$ 660,097</u>	<u>\$ 866,849</u>
Reconciliation of Net Operating Revenues (Expenses) to Net Cash Provided by (Used in) Operating Activities				
Operating income (loss)	\$ 972,627	\$ 861,891	\$ (2,177,399)	\$ (2,755,381)
Depreciation and amortization	-	-	1,836,770	1,792,117
Loss on disposal of capital assets	-	-	2,161	4,885
Other	-	(60)	115	115
Changes in operating assets and liabilities				
Patient accounts receivable, net	-	-	(92,000)	(176,089)
Estimated amounts due from and to third-party payers	-	-	(65,000)	345,000
Accounts payable and accrued expenses	-	-	(15,291)	(67,454)
Supplies and prepaid expenses and other	-	-	57,133	105,068
Net cash provided by (used in) operating activities	<u>\$ 972,627</u>	<u>\$ 861,831</u>	<u>\$ (453,511)</u>	<u>\$ (751,739)</u>
Supplemental Cash Flows Information				
Capital lease obligations incurred for capital assets	\$ -	\$ -	\$ -	\$ 26,639
Capital asset acquisitions included in accounts payable	\$ -	\$ -	\$ -	\$ 24,914

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

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

The Board of Trustees of Kiowa County Memorial Hospital (Board of Trustees) is a component unit of Kiowa County, Kansas (County) and was organized by the Kiowa County Commissioners to operate Kiowa County Memorial Hospital (KCMH) and to control the use of tax appropriations. The Board of Trustees is elected by the voters of the County.

The Board of Trustees leases KCMH to Great Plains of Kiowa County, Inc. (Hospital or GPKC). The Hospital is located in Greensburg, Kansas, and provides acute, swing-bed and physician clinic services. The Hospital is licensed as a Critical Access Hospital (CAH) and is managed by Great Plains Health Alliance, Inc. (GPHA) (*Note 10*). During January 2010, the County issued Hospital Revenue Bonds Series 2010-A. The bond obligations are payable from and secured by the revenues of the Hospital (*Note 7*). As the Board of Trustees can access the resources of the Hospital to pay the bond obligations, the Hospital is considered a component unit of the Board of Trustees and thus included in the financial statements of the Board of Trustees using discrete presentation. Prior to 2009, the Hospital and the Board of Trustees issued separate financial statements.

Basis of Accounting and Presentation

The financial statements of the Board of Trustees and 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 (principally federal and state grants and county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Interest income, interest on capital assets-related debt and noncapital grants and gifts are included in nonoperating revenues and expenses. The Board of Trustees and Hospital first apply restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position are available.

The Board of Trustees 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.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Cash Equivalents

The Board of Trustees and Hospital consider 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.

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.

Intergovernmental Revenue

The Board of Trustees and Hospital received approximately 16% in 2012 and 14% in 2011 of its financial support from intergovernmental revenue derived from property taxes levied by the County in both 2012 and 2011. One hundred percent of these funds were used to support operations in both years.

Property taxes are assessed by the County in November and are received beginning in January of the following 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. 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 collectability 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 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.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

For receivables associated with services provided to patients who have third-party coverage, the Hospital 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 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's allowance for uncollectible accounts estimated at December 31, 2012, is based on 100% of self-pay account balances greater than 90 days outstanding from the date of discharge or service and 100% of all other payer class account balances other than Medicare greater than 120 days 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:

Land improvements	5 – 20 years
Buildings	5 – 30 years
Fixed equipment	5 – 20 years
Major moveable equipment	3 – 20 years

Maintenance, repairs and renewals which neither materially add to the value of the property nor appreciably prolong its life are charged to expense as incurred. Gains or losses on dispositions of property and equipment are included in operations.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Bond Issuance Costs

Bond issuance 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.

Compensated Absences

Hospital policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off. Expense and the related liability are recognized as vacation benefits are earned. 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 is classified into three components. Net investment in capital assets consist of capital assets net of accumulated depreciation and reduced by any outstanding borrowings and related accounts used to finance the purchase or construction of those assets. Restricted expendable net position are noncapital assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors, including amounts as required by bond indentures. Unrestricted net position are remaining assets less remaining liabilities that do not meet the definition of net investment in capital assets or restricted expendable.

Board of Trustees' net position are unrestricted, but by nature, are to be used solely for the benefit of the Hospital. The funds are used by the Hospital for capital purchases and for operations as approved by action of the Board of Trustees.

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.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Income Taxes

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

The Hospital files tax returns in the U.S. federal jurisdiction. With a few exceptions, the Hospital is no longer subject to U.S. federal examinations by tax authorities for years before 2009.

Excess (Deficiency) of Revenues Over Expenses

The accompanying statements of revenues, expenses and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues result from the receipt of tax appropriations and exchange transactions associated with providing health care services. Nonexchange revenues, including interest income and contributions and grants received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services other than financing costs.

Reclassifications

Certain reclassifications have been made to the 2011 financial statements to conform to the 2012 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 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 Board of Trustees' 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.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

At December 31, 2012 and 2011, respectively, \$1,250,255 and \$575,444 of the Board of Trustees' bank balances of \$1,544,145 and \$867,106 were exposed to custodial credit risk as follows:

	2012	2011
Uninsured and uncollateralized	\$ -	\$ 50,791
Uninsured and collateral held by pledging financial institution's trust department or agent in other than the Board of Trustees' name	1,250,255	524,653
	<u>\$ 1,250,255</u>	<u>\$ 575,444</u>

Summary of Carrying Values

The carrying values of deposits shown above are included in the balance sheets at December 31, 2012 and 2011, as follows:

	2012	2011
Carrying value Deposits	<u>\$ 1,544,145</u>	<u>\$ 867,106</u>
Included in the following balance sheet captions		
Cash	\$ 1,111,424	\$ 440,590
Short-term certificates of deposit	67,015	66,439
Noncurrent certificates of deposit	365,706	360,077
	<u>\$ 1,544,145</u>	<u>\$ 867,106</u>

Note 3: Patient Accounts Receivable

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31, 2012 and 2011, consisted of:

	2012	2011
Medicare	\$ 457,802	\$ 385,382
Medicaid	12,981	51,950
Blue Cross	55,085	63,799
Other third-party payers	107,162	99,241
Self-pay	218,847	194,502
	<u>851,877</u>	<u>794,874</u>
Less allowance for uncollectible accounts	122,559	157,556
Patient accounts receivable, net	<u>\$ 729,318</u>	<u>\$ 637,318</u>

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

The mix of net receivables from patients and third-party payers at December 31, 2012 and 2011, is:

	<u>2012</u>	<u>2011</u>
Medicare	63%	60%
Medicaid	2%	4%
Other third-party payers	21%	23%
Self-pay	14%	13%
	<u>100%</u>	<u>100%</u>

Note 4: 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 who 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 uncollectible accounts 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 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 costs 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. The clinics are recognized as Rural Health Clinics (RHC). Under RHC rules, clinic services are paid based on allowable costs subject to certain limitations. Tentative reimbursement and final settlement are determined in a similar manner as for hospital services.

Medicaid. The Medicaid State Plan provides for a cost reimbursement methodology for inpatient and outpatient services rendered to Medicaid program beneficiaries who are not part of a Medicaid managed care network. Services rendered to Medicaid managed care patients are reimbursed under a prospective reimbursement methodology. Medicaid RHC services are reimbursed under a cost-based methodology. The Hospital and RHC are 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.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Approximately 79% and 84% of net patient service revenue was 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 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.

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 currently indicated it will not expand the Medicaid program, which may result in revenues from newly covered individuals not offsetting the Hospital's reduced revenue from other Medicare/Medicaid programs.

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's net patient service revenue. Additionally, it is possible the Hospital will experience payment delays and other operational challenges during the PPACA's implementation.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

The Hospital's net patient service revenue is computed as follows for the years ended December 31, 2012 and 2011:

	2012	2011
Gross patient service revenue	\$ 4,052,981	\$ 3,031,905
Plus (less)		
Medicare contractual adjustments	1,559,193	2,124,490
Medicaid contractual adjustments	2,534	20,594
Other contractual adjustments	(220,838)	(160,423)
Charity care	(20,464)	(36,104)
Administrative discounts	(32,071)	(8,639)
Provision for uncollectible accounts	(291,060)	(240,480)
Net patient service revenue	<u>\$ 5,050,275</u>	<u>\$ 4,731,343</u>

Note 5: Capital Assets

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

	2012				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 115,100	\$ -	\$ -	\$ -	\$ 115,100
Buildings and improvements	20,539,109	-	(5,085)	56,428	20,590,452
Fixed equipment	1,445,848	-	-	12,784	1,458,632
Major moveable equipment	2,570,876	154,757	-	-	2,725,633
Construction in progress	55,783	13,429	-	(69,212)	-
	<u>24,726,716</u>	<u>168,186</u>	<u>(5,085)</u>	<u>-</u>	<u>24,889,817</u>
Less accumulated depreciation					
Buildings and improvements	2,303,506	1,259,364	(2,286)	-	3,560,584
Fixed equipment	217,454	119,892	-	-	337,346
Major moveable equipment	796,176	457,514	-	-	1,253,690
	<u>3,317,136</u>	<u>1,836,770</u>	<u>(2,286)</u>	<u>-</u>	<u>5,151,620</u>
Capital Assets, Net	<u>\$ 21,409,580</u>	<u>\$ (1,668,584)</u>	<u>\$ (2,799)</u>	<u>\$ -</u>	<u>\$ 19,738,197</u>

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

	2011				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land	\$ 115,100	\$ -	\$ -	\$ -	\$ 115,100
Buildings and improvements	20,512,398	20,151	-	6,560	20,539,109
Fixed equipment	1,036,886	408,962	-	-	1,445,848
Major moveable equipment	2,152,737	431,468	(13,329)	-	2,570,876
Construction in progress	6,560	55,783	-	(6,560)	55,783
	<u>23,823,681</u>	<u>916,364</u>	<u>(13,329)</u>	<u>-</u>	<u>24,726,716</u>
Less accumulated depreciation					
Buildings and improvements	1,047,351	1,256,155	-	-	2,303,506
Fixed equipment	100,292	117,162	-	-	217,454
Major moveable equipment	385,820	418,800	(8,444)	-	796,176
	<u>1,533,463</u>	<u>1,792,117</u>	<u>(8,444)</u>	<u>-</u>	<u>3,317,136</u>
Capital Assets, Net	<u>\$ 22,290,218</u>	<u>\$ (875,753)</u>	<u>\$ (4,885)</u>	<u>\$ -</u>	<u>\$ 21,409,580</u>

Note 6: 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.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Note 7: Long-term Debt

The following is a summary of long-term debt transactions for the Hospital for the years ended December 31, 2012 and 2011:

2012					
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt					
Note payable, FEMA	\$ 1,600,000	\$ -	\$ 1,600,000	\$ -	\$ -
Revenue bonds payable	2,130,200	-	26,485	2,103,715	27,452
Capital lease obligations	36,547	-	8,126	28,421	5,295
	<u>\$ 3,766,747</u>	<u>\$ -</u>	<u>\$ 1,634,611</u>	<u>\$ 2,132,136</u>	<u>\$ 32,747</u>
Total long-term debt					
	<u>\$ 3,766,747</u>	<u>\$ -</u>	<u>\$ 1,634,611</u>	<u>\$ 2,132,136</u>	<u>\$ 32,747</u>

2011					
	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Long-term debt					
Note payable, FEMA	\$ 1,600,000	\$ -	\$ -	\$ 1,600,000	\$ 1,600,000
Revenue bonds payable	2,130,200	-	-	2,130,200	-
Capital lease obligations	34,749	26,639	24,841	36,547	8,439
	<u>\$ 3,764,949</u>	<u>\$ 26,639</u>	<u>\$ 24,841</u>	<u>\$ 3,766,747</u>	<u>\$ 1,608,439</u>
Total long-term debt					
	<u>\$ 3,764,949</u>	<u>\$ 26,639</u>	<u>\$ 24,841</u>	<u>\$ 3,766,747</u>	<u>\$ 1,608,439</u>

Note Payable, FEMA

In 2007, the Hospital entered into an agreement with the Federal Emergency Management Agency (FEMA) to issue a Community Disaster Loan to help assist with operations of the Hospital. The note bears interest at 4%, principal and interest were due October 2012. The loan was issued in installments with \$800,000 being issued in each of 2008 and 2009. The Community Disaster Loan program has a provision for loan cancellation if the governmental entity to which it was issued has insufficient revenues during the full three fiscal years following the disaster to meet the operating budget of said governmental entity. The Hospital sustained operating losses in each of 2008, 2009 and 2010 and applied for loan cancellation in 2011. The loan principal and related interest payable cancellation request was approved in June 2012. At December 31, 2012, there is no outstanding balance due on the FEMA note payable.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Revenue Bonds Payable

In 2010, the County entered into an agreement with the United States Department of Agriculture (USDA) to issue bonds to assist with the financing of the new hospital construction. The bonds bear interest at 4%, are due semi-annually in increasing principal amounts with final bonds maturing January 2049. The Hospital, acting as its own trustee, is required by the USDA to maintain specific principal, interest and bond reserve accounts. The actual principal and interest payments are then made to the bondholders from the Kansas State Treasurer, acting as the paying agent. The financed assets and related bond indebtedness have been included in the accompanying financial statements as assets and liabilities of the Hospital. The bonds are secured by a first and prior lien upon the gross revenues of the Hospital.

Bonds may be redeemed in advance of their maturity at 100% of face value.

The bond indentures require certain covenants, including financial, to be met. The financial covenants include a rate covenant that requires a debt service coverage ratio of 1.0 to be met and through 2011, monthly deposits to be made to separate accounts for debt service payments and to fund a debt service reserve. During 2012, the debt service reserve account was transferred to the County and the County became responsible for making monthly deposits as stipulated in the bond agreement. During 2012 and 2011, the Hospital did not meet the debt service coverage ratio of 1.0. In the case of the rate covenant not being met, the bond indenture requires that the Board of Trustees and Hospital employ a consultant to make recommendations with respect to the Hospital's rates and charges, with the Hospital to follow the recommendations, if feasible.

The debt service requirements for the revenue bonds payable as of December 31, 2012, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2013	\$ 111,601	\$ 27,452	\$ 84,149
2014	111,601	28,550	83,051
2015	111,601	29,692	81,909
2016	111,376	30,655	80,721
2017	111,601	32,106	79,495
2018-2022	557,791	180,623	377,168
2023-2027	557,808	219,765	338,043
2028-2032	557,677	267,242	290,435
2033-2037	557,878	325,366	232,512
2038-2042	557,909	395,886	162,023
2043-2047	557,946	481,693	76,253
2048-2049	88,072	84,685	3,387
	<u>\$ 3,992,861</u>	<u>\$ 2,103,715</u>	<u>\$ 1,889,146</u>

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Capital Lease Obligations

The Hospital is obligated under leases for equipment that are accounted for as capital leases. Assets under capital leases at December 31, 2012 and 2011, totaled \$26,570 and \$44,900, respectively, net of accumulated depreciation of \$13,069 and \$92,739, respectively. The following is a schedule by year of future minimum lease payments under the capital leases including interest at rates of 8.00% to 8.17% together with the present value of the future minimum lease payments as of December 31, 2012:

Year Ending December 31,	
2013	\$ 7,701
2014	4,143
2015	3,878
2016	3,878
2017	3,878
2018-2021	15,515
Total minimum lease payments	38,993
Less amount representing interest	10,572
Present value of future minimum lease payments	\$ 28,421

Note 8: Pension Plan

Hospital employees are eligible to participate in the GPHA defined contribution pension and tax deferred annuity plans. All employees, to be eligible for employer contributions, must have completed one year of service, with a minimum of 1,000 paid hours of service and must be at least 18 years of age. Employee contributions are mandatory beginning with the first day of service if 18 years of age or older. Benefits are funded by an annuity contract with an insurance company. Employer contributions are computed at a rate of 5% of annual compensation plus 10% of the excess over \$16,000. Employee contributions are computed at the rate of 2.5% of annual compensation plus 5.0% of the excess over \$16,000. The plan is funded for past service on an installment basis over the estimated remaining duration of employment from the effective date of the plan to the employee's normal retirement date. Employer contributions vest at 20% per year of service with 100% vesting after five years of service. Contributions actually made by plan members and the Hospital aggregated \$137,734 and \$193,317 during 2012 and \$143,869 and \$186,107 during 2011, respectively.

Board of Trustees of Kiowa County Memorial Hospital
A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Note 9: Functional Expenses

Functional expenses for the years ended December 31, 2012 and 2011, are as follows:

	<u>2012</u>	<u>2011</u>
Health care services	\$ 5,735,859	\$ 6,052,209
General and administrative	<u>1,820,931</u>	<u>1,787,195</u>
	<u>\$ 7,556,790</u>	<u>\$ 7,839,404</u>

Note 10: Related Party Transactions

The Board of Trustees entered into an agreement to lease hospital facilities to GPKC for one dollar. The lease provides that GPKC will assume and continue operations of the Hospital and maintain all property and equipment in good condition. The lease term is for a period of five years through January 2016.

GPKC has an agreement with GPHA, the sole member of GPKC, for management services. In addition, the Hospital has entered into agreements with GPHA for other services, including data processing and billing services. Fees incurred for services provided by GPHA to the Hospital totaled \$349,591 and \$305,567 in 2012 and 2011, respectively. Amounts included in accounts payable, related to these services, totaled \$31,191 and \$33,867 as of 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 4*.

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Litigation

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. 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 12: 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.

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

Board of Trustees of Kiowa County Memorial Hospital

A Component Unit of Kiowa County, Kansas

Insurance Coverage

December 31, 2012

CHUBB Insurance Group

Policy No. 3585-70-96KCO, expiring February 1, 2013:

Property	\$ 18,000,000
Boiler	6,412,200
Business interruption	3,200,000

Cincinnati Insurance Company

Policy No. BCP-0004687, expiring November 19, 2013:

Directors and officers	1,000,000
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Conrade Insurance Group

Policy No. CAP5155662, expiring February 1, 2013:

Trailer coverage	4,000,000
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Allied Insurance

Policy No. bd7900594274, expiring June 1, 2015:

Employee pension plan	200,000
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KHA Workers' Compensation Fund, Inc.

Policy No. 8111, expiring January 1, 2013:

Workers' compensation:

Per accident	500,000
Per employee disease	500,000
Policy limit	500,000

Kansas Medical Mutual Insurance Company

Policy No. HPL 0015367, expiring January 1, 2013:

Professional liability	200,000/600,000
Kansas Healthcare Stabilization Fund	300,000/900,000
General liability	1,000,000/3,000,000
Additional insureds	1,000,000/3,000,000
Employee benefits	250,000

QBE Insurance Corporation

Policy No. AHH004823, expiring November 24, 2013:

Accident coverage - volunteers	100,000
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Policies expiring in January and February 2013 were renewed for another policy term.