

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas

Independent Auditor's Report and Financial Statements

December 31, 2012 and 2011



Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas
December 31, 2012 and 2011

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Independent Auditor's Report

Board of Trustees
Trego County-Lemke Memorial Hospital
WaKeeney, Kansas

We have audited the accompanying financial statements of Trego County-Lemke Memorial Hospital (Hospital), a component unit of Trego County, Kansas, 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 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 Trego County-Lemke Memorial Hospital 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 30, 2013

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas

Balance Sheets

December 31, 2012 and 2011

Assets

	<u>2012</u>	<u>2011</u>
Current Assets		
Cash	\$ 377,753	\$ 135
Patient accounts receivable, net of allowance; 2012 – \$602,893, 2011 – \$458,894	1,580,650	1,927,390
Estimated amounts due from third-party payers	268,108	-
Supplies	187,074	172,593
Prepaid expenses and other	<u>97,805</u>	<u>255,254</u>
Total current assets	<u>2,511,390</u>	<u>2,355,372</u>
 Noncurrent Cash and Investments	 <u>277,851</u>	 <u>1,001,023</u>
 Capital Assets, Net	 <u>4,338,251</u>	 <u>4,270,172</u>
 Deferred Financing Costs	 <u>1,659</u>	 <u>3,239</u>
Total assets	<u><u>\$ 7,129,151</u></u>	<u><u>\$ 7,629,806</u></u>

Liabilities and Net Position

	2012	2011
Current Liabilities		
Bank overdraft	\$ -	\$ 50,563
Current maturities of long-term debt	201,308	184,622
Accounts payable	955,796	664,384
Accrued salaries and wages	216,518	212,331
Accrued paid time off	386,633	335,596
Accrued payroll taxes	127,388	108,060
Accrued expenses	51,566	51,542
Estimated amounts due to third-party payers	-	450,000
Total current liabilities	1,939,209	2,057,098
Long-term Debt	471,655	301,743
Total liabilities	2,410,864	2,358,841
Net Position		
Net investment in capital assets	3,665,288	3,783,807
Restricted - expendable for specific operating activities	15,002	9,401
Unrestricted	1,037,997	1,477,757
Total net position	4,718,287	5,270,965
Total liabilities and net position	\$ 7,129,151	\$ 7,629,806

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2012 – \$480,017, 2011 – \$105,861	\$ 14,779,781	\$ 14,359,497
Other	<u>111,074</u>	<u>136,710</u>
Total operating revenues	<u>14,890,855</u>	<u>14,496,207</u>
Operating Expenses		
Salaries and wages	7,226,788	6,831,350
Supplies and other	7,884,372	7,535,692
Depreciation	<u>526,665</u>	<u>504,085</u>
Total operating expenses	<u>15,637,825</u>	<u>14,871,127</u>
Operating Loss	<u>(746,970)</u>	<u>(374,920)</u>
Nonoperating Revenues (Expenses)		
Property taxes	136,500	136,500
Noncapital grants and gifts	50	2,755
Investment income	12,892	19,841
Interest expense	<u>(27,708)</u>	<u>(29,002)</u>
Total nonoperating revenues	<u>121,734</u>	<u>130,094</u>
Deficiency of Revenues Over Expenses Before Capital Grants and Gifts	<u>(625,236)</u>	<u>(244,826)</u>
Capital Grants and Gifts	<u>72,558</u>	<u>50,147</u>
Decrease in Net Position	<u>(552,678)</u>	<u>(194,679)</u>
Net Position, Beginning of Year	<u>5,270,965</u>	<u>5,465,644</u>
Net Position, End of Year	<u><u>\$ 4,718,287</u></u>	<u><u>\$ 5,270,965</u></u>

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas

Statements of Cash Flows

Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Operating Activities		
Receipts from and on behalf of patients	\$ 14,408,413	\$ 14,388,772
Payments to suppliers and contractors	(7,448,388)	(7,375,019)
Payments to employees	(7,152,236)	(6,789,540)
Other receipts, net	<u>105,115</u>	<u>136,660</u>
Net cash provided by (used in) operating activities	<u>(87,096)</u>	<u>360,873</u>
Noncapital Financing Activities		
Property taxes	136,500	136,500
Bank overdraft	(50,563)	(205,341)
Noncapital grants and gifts	<u>50</u>	<u>2,755</u>
Net cash provided by (used in) noncapital financing activities	<u>85,987</u>	<u>(66,086)</u>
Capital and Related Financing Activities		
Capital grants and gifts	72,558	50,147
Principal paid on long-term debt	(244,631)	(175,005)
Interest paid on long-term debt	(27,708)	(29,002)
Proceeds from disposal of equipment	23,143	50
Purchases of capital assets	<u>(180,699)</u>	<u>(57,563)</u>
Net cash used in capital and related financing activities	<u>(357,337)</u>	<u>(211,373)</u>
Investing Activities		
Net change in noncurrent cash and investments	325,000	300,000
Investment income received	<u>12,892</u>	<u>19,841</u>
Net cash provided by investing activities	<u>337,892</u>	<u>319,841</u>
Increase (Decrease) in Cash and Cash Equivalents	(20,554)	403,255
Cash and Cash Equivalents, Beginning of Year	<u>676,158</u>	<u>272,903</u>
Cash and Cash Equivalents, End of Year	<u><u>\$ 655,604</u></u>	<u><u>\$ 676,158</u></u>

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas
Statements of Cash Flows (Continued)
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Reconciliation of Cash and Cash Equivalents to the Balance Sheets		
Cash in current assets	\$ 377,753	\$ 135
Cash in noncurrent cash and investments	<u>277,851</u>	<u>676,023</u>
Total cash	<u><u>\$ 655,604</u></u>	<u><u>\$ 676,158</u></u>
Reconciliation of Net Operating Loss to Net Cash		
Provided by (Used in) Operating Activities		
Operating loss	\$ (746,970)	\$ (374,920)
Depreciation	526,665	504,085
Provision for uncollectible accounts	480,017	105,861
Amortization of deferred financing costs	1,580	2,119
Gain on disposal of equipment	(5,959)	(50)
Change in operating assets and liabilities		
Patient accounts receivable	(133,277)	(659,586)
Estimated amounts due from third-party payers	(718,108)	583,000
Supplies	(14,481)	(15,168)
Prepaid expenses and other	157,449	(33,162)
Accounts payable	291,412	201,013
Accrued expenses	<u>74,576</u>	<u>47,681</u>
Net cash provided by (used in) operating activities	<u><u>\$ (87,096)</u></u>	<u><u>\$ 360,873</u></u>
Supplemental Cash Flows Information		
Capital lease obligations incurred for capital assets	\$ 431,229	\$ 71,042

Trego County-Lemke Memorial Hospital

A Component Unit of Trego 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

Trego County-Lemke Memorial Hospital (Hospital) provides acute, long-term care services, rural health clinic services and assisted living services. The Hospital was created by statute and its Board of Trustees is appointed by the Trego County Board of Commissioners. The Hospital is located in WaKeeney, Kansas and is considered a component unit of Trego County.

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 and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific such as county appropriations, property taxes, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position 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).

Use of Estimates

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

Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less other than board designated assets to be cash equivalents. There were no cash equivalents at December 31, 2012 and 2011.

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas
Notes to Financial Statements
December 31, 2012 and 2011

Property Taxes

The Hospital received approximately 1% of its financial support from property taxes in both 2012 and 2011. One hundred percent of these funds were used to support operations in both years.

Property taxes are levied by the county on the Hospital's behalf on January 1 and are intended to finance the Hospital's activities of the same calendar year. Amounts levied are based on assessed property values as of the preceding July 1. Revenue from property taxes is recognized in the year for which the taxes are levied.

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.

Investments and Investment Income

Investments in nonnegotiable certificates of deposit are carried at amortized cost.

Investment income includes dividend and interest income.

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.

Trego County-Lemke Memorial Hospital

A Component Unit of Trego County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

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	10-15 years
Buildings	15-40 years
Fixed equipment	5-20 years
Moveable equipment	5-20 years

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 effective interest method.

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. 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 Position

Net position of the Hospital 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 is noncapital assets that must be used for a particular purpose as specified by donors external to the Hospital. Unrestricted net position is remaining assets less remaining liabilities that do not meet the above conditions.

Trego County-Lemke Memorial Hospital

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Notes to Financial Statements

December 31, 2012 and 2011

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.

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.

Note 2: Deposits and Investments

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.

Trego County-Lemke Memorial Hospital

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Notes to Financial Statements

December 31, 2012 and 2011

The Hospital had the following bank balances at December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Insured (FDIC)	\$ 514,609	\$ 523,722
Collateralized by securities held by pledging institutions in the Hospital's name	<u>324,549</u>	<u>461,991</u>
	<u><u>\$ 839,158</u></u>	<u><u>\$ 985,713</u></u>
Carrying amount	<u><u>\$ 655,604</u></u>	<u><u>\$ 1,001,158</u></u>

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

	<u>2012</u>	<u>2011</u>
Cash	\$ 377,753	\$ 135
Noncurrent cash and investments	<u>277,851</u>	<u>1,001,023</u>
	<u><u>\$ 655,604</u></u>	<u><u>\$ 1,001,158</u></u>

Investments

The Hospital may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in corporate bonds and equity securities.

The Hospital's investments consist entirely of certificates of deposit, which are included in the above tables. All certificates of deposit have maturities of one year or less.

Note 3: 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 licensed as a Critical Access Hospital, and is paid for inpatient acute care, skilled swing-bed and outpatient services rendered to Medicare program beneficiaries at one hundred one percent (101%) of actual cost subject to certain limitations. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of an annual cost report by the Hospital and audit thereof by the Medicare administrative contractor.

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Notes to Financial Statements

December 31, 2012 and 2011

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. Medicaid Rural Health Clinic services are reimbursed under a cost-based methodology. The Hospital and Rural Health Clinic 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. Medicaid reimbursement for long-term care facility residents is based on a cost-based prospective reimbursement methodology. The Hospital is reimbursed at a prospective rate with annual cost reports submitted to the Medicaid program. 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 \$138,000 and are included in 2011 net income. 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 54% and 53% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2012 and 2011. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

Net patient service revenue consists of the following for the years ended December 31:

	2012	2011
Gross patient service revenue	\$ 22,282,238	\$ 21,404,477
Contractual adjustments		
Medicare	(5,252,126)	(5,362,082)
Medicaid	(93,417)	(32,809)
Blue Cross	(1,185,261)	(1,049,621)
Other	(399,665)	(322,318)
Administrative adjustments	(83,606)	(160,368)
Charity care	(8,365)	(11,921)
Provision for uncollectible accounts	(480,017)	(105,861)
	<u><u>\$ 14,779,781</u></u>	<u><u>\$ 14,359,497</u></u>

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

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:

	2012	2011
Medicare	\$ 1,066,483	\$ 1,547,506
Medicaid	150,570	84,304
Blue Cross	270,628	411,035
Other third-party payers	204,958	172,460
Self-pay	969,915	840,162
	<u>2,662,554</u>	<u>3,055,467</u>
Less allowance for uncollectible accounts	(602,893)	(458,894)
Less allowance for contractual adjustments	<u>(479,011)</u>	<u>(669,183)</u>
	<u><u>\$ 1,580,650</u></u>	<u><u>\$ 1,927,390</u></u>

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

	2012	2011
Medicare	48%	55%
Medicaid	6	2
Blue Cross	13	16
Other third-party payers	8	6
Self-pay	<u>25</u>	<u>21</u>
	<u><u>100%</u></u>	<u><u>100%</u></u>

Trego County-Lemke Memorial Hospital
A Component Unit of Trego County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Note 5: Capital Assets

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

2012				
	Beginning Balance	Additions	Disposals	Ending Balance
Land	\$ 2,500	\$ -	\$ -	\$ 2,500
Land improvements	112,109	-	-	112,109
Buildings	6,798,593	-	-	6,798,593
Fixed equipment	2,810,367	-	-	2,810,367
Moveable equipment	3,029,394	611,928	(456,370)	3,184,952
	<u>12,752,963</u>	<u>611,928</u>	<u>(456,370)</u>	<u>12,908,521</u>
Less accumulated depreciation				
Land improvements	(95,169)	(4,802)	-	(99,971)
Buildings	(3,546,526)	(257,086)	-	(3,803,612)
Fixed equipment	(2,446,511)	(29,962)	-	(2,476,473)
Moveable equipment	(2,394,585)	(234,815)	439,186	(2,190,214)
	<u>(8,482,791)</u>	<u>(526,665)</u>	<u>439,186</u>	<u>(8,570,270)</u>
Capital assets, net	<u>\$ 4,270,172</u>	<u>\$ 85,263</u>	<u>\$ (17,184)</u>	<u>\$ 4,338,251</u>

2011				
	Beginning Balance	Additions	Disposals	Ending Balance
Land	\$ 2,500	\$ -	\$ -	\$ 2,500
Land improvements	112,109	-	-	112,109
Buildings	6,798,593	-	-	6,798,593
Fixed equipment	2,793,667	16,700	-	2,810,367
Moveable equipment	2,925,087	111,905	(7,598)	3,029,394
	<u>12,631,956</u>	<u>128,605</u>	<u>(7,598)</u>	<u>12,752,963</u>
Less accumulated depreciation				
Land improvements	(89,997)	(5,172)	-	(95,169)
Buildings	(3,284,616)	(261,910)	-	(3,546,526)
Fixed equipment	(2,418,296)	(28,215)	-	(2,446,511)
Moveable equipment	(2,193,395)	(208,788)	7,598	(2,394,585)
	<u>(7,986,304)</u>	<u>(504,085)</u>	<u>7,598</u>	<u>(8,482,791)</u>
Capital assets, net	<u>\$ 4,645,652</u>	<u>\$ (375,480)</u>	<u>\$ -</u>	<u>\$ 4,270,172</u>

Trego County-Lemke Memorial Hospital

A Component Unit of Trego County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Note 6: Medical Malpractice Coverage and Claims

The Hospital 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's claim experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

Note 7: Long-term Obligations

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

2012						
	Beginning Balance	Additions	Deductions	Ending Balance	Amounts Due Within One Year	Long-term Portion
Capital leases	\$ 186,230	\$ 431,229	\$ (158,686)	\$ 458,773	\$ 113,152	\$ 345,621
Revenue bonds	300,135	-	(85,945)	214,190	88,156	126,034
	<u>\$ 486,365</u>	<u>\$ 431,229</u>	<u>\$ (244,631)</u>	<u>\$ 672,963</u>	<u>\$ 201,308</u>	<u>\$ 471,655</u>
2011						
	Beginning Balance	Additions	Deductions	Ending Balance	Amounts Due Within One Year	Long-term Portion
Capital leases	\$ 206,370	\$ 71,042	\$ (91,182)	\$ 186,230	\$ 98,677	\$ 87,553
Revenue bonds	383,958	-	(83,823)	300,135	85,945	214,190
	<u>\$ 590,328</u>	<u>\$ 71,042</u>	<u>\$ (175,005)</u>	<u>\$ 486,365</u>	<u>\$ 184,622</u>	<u>\$ 301,743</u>

Series 2005 Revenue Bonds

Trego County (County) issued \$400,000 zero interest hospital revenue bonds in December 2005 on behalf of the Hospital to assist in financing certain hospital improvements. Imputed interest has been computed on these bonds at a rate of 5% and is being amortized over the term of the bonds. The bonds are secured by the net revenues of the Hospital.

Trego County-Lemke Memorial Hospital

A Component Unit of Trego County, Kansas

Notes to Financial Statements

December 31, 2012 and 2011

Series A 2009 Revenue Bonds

The County issued \$125,000 zero interest hospital revenue bonds in December 2009 on behalf of the Hospital to assist in financing certain hospital improvements. The bonds are secured by the net revenues of the Hospital.

Series B 2009 Revenue Bonds

The County issued \$140,000 two percent interest hospital revenue bonds in December 2009 on behalf of the Hospital to assist in financing certain hospital improvements. The bonds are secured by the net revenues of the Hospital.

The indenture agreements require the Hospital to comply with certain restrictive covenants including maintaining a historical debt-service coverage ratio of at least 1.10. The Hospital was in violation of this covenant at December 31, 2012. As a result, the Hospital is required to hire a consultant and file a copy of the consultant's report and recommendations with the clerk and purchaser of the bonds and be furnished to any owner of the bonds requesting a copy of the same.

Scheduled debt service requirements on long-term debt are as follows:

Year Ending December 31,	Revenue Bonds		Capital Leases	
	Principal	Interest	Principal	Interest
2013	\$ 88,156	\$ 6,290	\$ 113,152	\$ 25,567
2014	87,938	3,986	118,843	17,267
2015	38,096	1,905	92,443	11,081
2016	-	-	80,549	6,155
2017	-	-	40,793	1,980
2018-2021	-	-	12,993	2,233
	<u>\$ 214,190</u>	<u>\$ 12,181</u>	<u>\$ 458,773</u>	<u>\$ 64,283</u>

The following is an analysis of the financial presentation of the capital leases at December 31:

	2012	2011
Equipment	\$ 1,187,778	\$ 485,543
Accumulated depreciation	<u>(349,224)</u>	<u>(273,669)</u>
	<u>\$ 838,554</u>	<u>\$ 211,874</u>

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Note 8: Pension Plans

Defined Contribution Plans

The Hospital maintains a contributory pension plan for eligible employees. Eligibility is established by all employees 21 years of age or older and have completed one year of service. Employer contributions are computed at the rate of 4.5% of annual compensation plus 9% of the excess over \$7,800. Employee contributions are computed at the rate of 2.5% of annual compensation plus 5% of the excess over \$7,800. Benefits are funded by an annuity contract with an insurance company. 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. Benefits vest after one year of service with 100% vesting after five years of service. In case of the death or termination of an employee prior to retirement, all funds contributed by the Hospital, which are not vested, will be returned to the Hospital. Contributions actually made by plan members totaled \$378,710 and \$357,646 in 2012 and 2011, respectively. Hospital contributions totaled \$458,810 and \$415,517 in 2012 and 2011, respectively.

The Hospital provides a 403(b) plan to substantially all employees of the Hospital. The employees' total salary deferral is limited by the Internal Revenue Service (IRS) annually. Employees are always 100% vested in the contributions they choose to defer. If an employee is 50 years old or older and has met the annual IRS deferral limit, the employee may contribute a catch-up deferral that is also limited by the IRS annually. The Hospital does not make contributions to the 403(b) plan.

Deferred Compensation Plan

The Hospital maintains a 457 plan for all eligible employees. Eligibility is established by all employees who elect to participate in the plan by executing a written participation agreement. The employee may contribute up to \$7,500 of their gross compensation per year. Employee contributions to all benefit plans cannot exceed 25% of their gross compensation per year. Benefits are funded by fixed and variable annuities with an insurance company. The Hospital does not make contributions to the 457 plan.

Note 9: Management/Services Agreement

The Board of Trustees of the Hospital has contracted with Great Plains Health Alliance, Inc. (GPHA) for various services, including management and data processing services. The terms of the agreements vary from one to seven years and can be canceled with 60 days' notice. The agreements can be renewed after the initial term has expired on a year-to-year basis. Fees incurred for the various services provided by GPHA to the Hospital totaled \$240,517 and \$152,916 in 2012 and 2011, respectively. Amounts included in accounts payable related to these services totaled \$78,888 and \$27,342 at December 31, 2012 and 2011, respectively.

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Note 10: Trego Hospital Endowment Foundation, Inc.

The Trego Hospital Endowment Foundation, Inc. (Foundation) is a not-for-profit corporation established to improve medical services to the patients in the area served by the Hospital. The Foundation is not considered a component unit of the Hospital. Foundation contributions to the Hospital of \$41,197 and \$14,778 in 2012 and 2011, respectively, have been included in the Hospital's statements of revenues, expenses and changes in net position as capital grants and gifts.

Note 11: 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 to the Hospital 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's net patient service revenue. Additionally, it is possible the Hospital will experience payment delays and other operational challenges during PPACA's implementation.

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Note 12: 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.

Current economic conditions have made it difficult for certain patients to pay for services rendered. 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 investment values and allowances for accounts receivable that could negatively impact the Hospital's ability to meet debt covenants and maintain sufficient liquidity.

Note 13: Subsequent Events

In April 2013, the County voters passed a 1% sales tax increase, which is estimated to generate approximately \$500,000 additional tax revenue per year. The proceeds are to be used to promote health care in Trego County, which includes the direct support of the Hospital.

In April 2013, the County obtained \$1,800,000 in no fund warrants. The County transferred \$1,785,000 to the Hospital to support operating expenses and to pay down payables.

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.