

**WINDOM AREA HOSPITAL  
Windom, Minnesota**

**COMBINED FINANCIAL STATEMENTS**

**YEARS ENDED APRIL 30, 2007 AND 2006**

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
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## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Windom Area Hospital and Affiliate  
Windom, Minnesota

We have audited the accompanying combined balance sheets of Windom Area Hospital and its discretely presented component unit as of April 30, 2007 and 2006, and the related combined statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These combined financial statements are the responsibility of the management of Windom Area Hospital. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Windom Area Hospital as of April 30, 2007 and 2006 and the results of its operations, changes in net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 10, 2007 on our consideration of Windom Area Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 2 through 6, is not a required part of the basic combined financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on management's discussion and analysis.

LarsonAllen LLP

Minneapolis, Minnesota  
July 10, 2007



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**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**APRIL 30, 2007 AND 2006**

**Introduction**

The Windom Area Hospital (Hospital) offers readers of our financial statements this narrative overview and analysis of the financial activities of Windom Area Hospital for the fiscal years ended April 30, 2007 and 2006. We encourage readers to consider the information presented here in conjunction with the Hospital's combined financial statements, including the notes thereto.

**Overview of the Financial Statements**

This discussion and analysis is intended to serve as an introduction to Windom Area Hospital's audited combined financial statements. The combined financial statements are composed of the balance sheet, combined statement of revenues, expenses, and changes in net assets, and the statement of cash flows. The combined financial statements also include notes to the combined financial statements that explain in more detail some of the information in the combined financial statements. The combined financial statements are designed to provide readers with a broad overview of the Hospital's finances.

The combined financial statements include the Hospital and Foundation finances. The mission of the Windom Area Foundation is to provide charitable support for medical and educational programs of Windom Area Hospital. Total Foundation funds equal \$80,287 at year end.

**Required Financial Statements**

The Hospital's combined financial statements report information of Windom Area Hospital using accounting methods similar to those used by private sector healthcare organizations. These statements offer short and long-term information about its activities. The combined balance sheet includes all of the Hospital's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to Hospital creditors (liabilities). The combined balance sheet also provides the basis for evaluating the capital structure of the Hospital and assessing the liquidity and financial flexibility of the Hospital.

All of the current year's revenues and expenses are accounted for in the combined statement of revenues, expenses, and changes in net assets. This statement can be used to determine whether the Hospital has successfully recovered all of its costs through its patient service revenue and other revenue sources. Revenues and expenses are reported on an accrual basis, which means the related cash could be received or paid in a subsequent period.

The final required statement is the combined statement of cash flows. The statement reports cash receipts, cash payments and net changes in cash resulting from operations, investing and financing activities. It also provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

**Financial Highlights**

Hospital total assets increased by \$1,611,643 to \$16,235,006 in FY 07 and by \$1,283,261 to \$14,623,363 in FY 06. Net property, plant and equipment increased by \$222,255 in fiscal year 2007 and \$471,083 in fiscal year 2006. Total liabilities increased by \$361,177 in FY 2007 and decreased by \$71,653 in FY 2006. The total margin was 9.3%, 10.0% and 9.9% for the years ended April 30, 2007, 2006 and 2005, respectively.

**WINDOM AREA HOSPITAL**  
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**Financial Analysis of the Hospital**

The combined balance sheet and the combined statement of revenues, expenses, and changes in net assets report the net assets of the Hospital and the changes in them. The Hospital's net assets - the difference between assets and liabilities - is a way to measure financial health or financial position. Over time, sustained increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in economic condition, population growth and new or changed governmental legislation should also be considered.

**Net Assets**

A summary of the Hospital's balance sheets at April 30, 2007, 2006 and 2005 is presented below:

**Table 1**  
**Condensed Combined Balance Sheets (in Thousands)**

	April 30,		
	2007	2006	2005
Current Assets	\$ 3,808	\$ 3,680	\$ 3,044
Assets Limited as to Use	4,669	3,507	3,330
Capital Assets	7,646	7,424	6,953
Other Assets	111	12	13
<b>Total Assets</b>	<b>\$ 16,235</b>	<b>\$ 14,623</b>	<b>\$ 13,340</b>
Current Liabilities	\$ 1,567	\$ 1,203	\$ 1,097
Long-Term Debt Outstanding	2,184	2,186	2,364
<b>Total Liabilities</b>	<b>3,751</b>	<b>3,389</b>	<b>3,461</b>
Invested in Capital Assets, Net of Related Debt	5,367	5,147	4,049
Restricted	2,135	1,329	3,491
Unrestricted	4,983	4,758	2,339
<b>Total Net Assets</b>	<b>12,484</b>	<b>11,234</b>	<b>9,879</b>
<b>Total Liabilities and Net Assets</b>	<b>\$ 16,235</b>	<b>\$ 14,623</b>	<b>\$ 13,340</b>

As can be seen by Table 1, net assets increased by \$1.3 million to \$12.5 million in fiscal year 2007. In fiscal year 2006, net assets increased by \$1.3 million to \$11.2 million. The change in net assets results primarily from operating income.

**WINDOM AREA HOSPITAL**  
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**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**APRIL 30, 2007 AND 2006**

**Revenues, Expenses, and Changes in Net Assets**

The following table presents a summary of the Hospital's historical revenues and expenses for the fiscal years ended April 30, 2007, 2006 and 2005.

**Table 2**  
**Condensed Combined Statements of Revenue, Expenses, and Changes in Net Assets (in Thousands)**

	Year Ended April 30,		
	2007	2006	2005
Operating Revenues	\$ 12,060	\$ 11,546	\$ 11,002
Operating Expenses	11,104	10,465	9,922
Operating Income	956	1,081	1,080
Non-Operating Income	217	120	29
Excess of Revenues over Expenses	1,173	1,201	1,109
Capital Grants and Contributions	77	154	8
Changes in Net Assets	1,250	1,355	1,117
Total Net Assets, Beginning of Year	11,234	9,879	8,762
Total Net Assets, End of Year	<u>\$ 12,484</u>	<u>\$ 11,234</u>	<u>\$ 9,879</u>

**Operating and Financial Performance**

**Volume:** Inpatient admissions (excluding newborns) for fiscal year 2007 were 788 compared to 748 in fiscal year 2006 and 824 in fiscal year 2005. This is an increase of 40 or 5% between 2007 and 2006 and a decrease of 76 or 9% between 2006 and 2005. Patient days (excluding newborns) for fiscal year 2007 were 2,129 compared to 1,989 in fiscal year 2006 and 2,262 in fiscal year 2005. This is an increase of 140 or 7% from 2006 and a decrease of 273 or 12% between 2006 and 2005. The length of stay decreased from 2.8 days in 2005 to 2.6 days in 2006 and increased to 2.7 days in 2007. Emergency department visits increased to 3,163 in fiscal year 2007 from 2,772 in fiscal year 2006. This is an increase of 391 visits or 14%. They increased from 2,616 in 2005, which is an increase of 156 or 6%. All other outpatient visits for 2007 were 17,337 compared to 17,917 in 2006 and 17,996 in 2005. This is a decrease of 580 visits from 2006 to 2007 and a decrease of 47 visits from 2005 to 2006. Total surgeries increased to 1,436 from 1,234 in the previous fiscal year. This is an increase of 202 surgeries or 16%. In fiscal year 2006 surgeries decreased from 1,330 which is a decrease of 96 surgeries or 24%.

**Net Patient Service Revenue:** Effective May 1, 2006, an 8% rate increase was implemented. As a result of the rate increase, net patient service revenue increased \$454,795 or 4% compared to fiscal year 2006. Revenue deductions, the amount of patient service revenue uncollectible due to contractual agreements, government reimbursement policies, and bad debts increased to \$5,545,684 from \$4,514,927, a 23% increase.

**Other Operating Revenue:** Other operating revenue increased \$58,901 and \$69,153 in fiscal years 2007 and 2006, respectively, from the previous year. The increase is due to an increase in Wellness Center income, miscellaneous income and laboratory other income.

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APRIL 30, 2007 AND 2006

**Nursing Services:** Nursing service expenses increased \$485,249 and decreased \$10,509 in fiscal years 2007 and 2006, respectively, from the previous year. This increase is a result of a process change in payroll. Under a new payroll system, implemented in fiscal 2007, the accrued benefits are now expensed to the respective departments.

**Other Professional Services:** Other professional services increased \$50,573 and \$51,976 in fiscal years 2007 and 2006, respectively, from the previous year. Pharmacy drug costs continue to escalate. ER professional fees increased in 2007 due to 24/7 coverage by emergency room contract physicians.

**General Services:** General services increased \$54,857 and \$37,493 in fiscal years 2007 and 2006, respectively, when compared to the previous year. Expenses relating to updates to the facility account for most of this increase.

**Administrative and Fiscal Services:** Expenses in this category increased by \$83 and \$271,216 in fiscal years 2007 and 2006, respectively, when compared to the previous year. Employee benefit costs, primarily health insurance continue to rise.

**Interest and Amortization:** Interest and amortization decreased \$2,288 and \$43,500 in fiscal years 2007 and 2006, respectively, when compared to the previous year. This increase is attributed to interest expense for the 2003 gross revenue bonds.

**Depreciation:** Depreciation increased \$50,904 and \$150,105 in fiscal years 2007 and 2006, respectively, when compared to the previous year. This is a reflection of the updates to facilities and equipment.

**Non-Operating Revenue and Expenses:** The total in this category increased \$98,028 and increased \$69,153 in fiscal years 2007 and 2006, respectively, when compared to the previous year. The increase is due to a rise in investment interest rates.

#### **Capital Assets**

At the end of fiscal years 2007, 2006 and 2005, the Hospital had invested \$7,646,215, \$7,423,960 and \$7,008,877, respectively, in net capital assets. The \$222,255 increase in capital assets in fiscal year 2007 is primarily a result of a computer system upgrade and Operating Room Imaging equipment.

#### **Capital Leases**

At the end of fiscal years 2007, 2006 and 2005, the Hospital had a total of \$0, \$0 and \$21,379, respectively, in capital lease obligations. Further detailed information is presented in the Notes to the Financial Statements.

#### **Capital Grants and Contributions**

For the years ended 2007, 2006 and 2005, the Hospital had a total of \$77,271, \$154,065 and \$8,086, respectively, in capital grants and contributions. The 2007 balance is made up of smaller grants and an estate gift.

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**Economic and Other Factors and Next Year's Budget**

The Windom Area Hospital Board of Directors and management considered many factors when setting the fiscal year 2008 budget. Of primary importance in setting the 2008 budget is the status of the economy, which takes into account market forces and environmental factors such as:

- Medicare and Medicaid reimbursement rates continued decline
- Health Insurance Portability and Accountability Act (HIPAA)
- Increased expectations for quality at a lower price
- Workforce shortages
- Cost of supplies
- Surging drug costs

**Contacting the Hospital's Finance Department**

Windom Area Hospital's combined financial statements are designed to present users with a general overview of the Hospital's finances and to demonstrate the Windom Area Hospital's accountability. If you have questions about the report or need additional financial information, please contact Administration at Windom Area Hospital, 2150 Hospital Drive, PO Box 339, Windom, MN 56101.

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**COMBINED BALANCE SHEET**  
**APRIL 30, 2007**

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
<b>ASSETS</b>			
<b>CURRENT ASSETS</b>			
Cash and Cash Equivalents	\$ 1,297,075	\$ 45,966	\$ 1,343,041
Assets Limited as to Use, Current Portion	142,298	-	142,298
Patient Accounts Receivable, Net	1,930,490	-	1,930,490
Accrued Interest Receivable	39,600	-	39,600
Supplies	265,340	-	265,340
Prepaid Expenses	87,280	-	87,280
Total Current Assets	3,762,083	45,966	3,808,049
<b>ASSETS LIMITED AS TO USE</b>			
Debt Service Account Under Bond Indenture	2,051,984	-	2,051,984
Board Designated for Capital Improvements	2,677,213	-	2,677,213
Restricted By Donor	48,199	34,321	82,520
Subtotal	4,777,396	34,321	4,811,717
Less: Current Portion	(142,298)	-	(142,298)
Total Assets Limited as to Use	4,635,098	34,321	4,669,419
<b>CAPITAL ASSETS</b>			
Capital Assets	13,151,530	-	13,151,530
Less: Accumulated Depreciation	(5,505,315)	-	(5,505,315)
Net Capital Assets	7,646,215	-	7,646,215
<b>OTHER ASSETS</b>			
Investment in Partnership	100,000	-	100,000
Deferred Debt Acquisition Costs, Net	11,323	-	11,323
Total Other Assets	111,323	-	111,323
Total Assets	\$ 16,154,719	\$ 80,287	\$ 16,235,006

See accompanying Notes to Combined Financial Statements.

<b>LIABILITIES AND NET ASSETS</b>	<u>Primary Enterprise</u>	<u>Component Unit (Foundation)</u>	<u>Total Reporting Entity (Memorandum Only)</u>
<b>CURRENT LIABILITIES</b>			
Current Maturities of Long-Term Debt	\$ 95,000	\$ -	\$ 95,000
Accounts Payable	468,975	-	468,975
Due to Third-Party Payors	400,000	-	400,000
Accrued Expenses	602,710	-	602,710
Total Current Liabilities	<u>1,566,685</u>	<u>-</u>	<u>1,566,685</u>
<b>LONG-TERM DEBT, Net of Current Maturities</b>	2,184,026	-	2,184,026
<b>NET ASSETS</b>			
Invested in Capital Assets Net of Related Debt	5,367,189	-	5,367,189
Restricted:			
Expendable for Bond Indenture	2,051,984	-	2,051,984
Expendable for Specific Donor Restrictions	48,199	34,321	82,520
Unrestricted	4,936,636	45,966	4,982,602
Total Net Assets	<u>12,404,008</u>	<u>80,287</u>	<u>12,484,295</u>
Total Liabilities and Net Assets	<u>\$ 16,154,719</u>	<u>\$ 80,287</u>	<u>\$ 16,235,006</u>

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**COMBINED BALANCE SHEET**  
**APRIL 30, 2006**

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
<b>ASSETS</b>			
<b>CURRENT ASSETS</b>			
Cash and Cash Equivalents	\$ 1,267,748	\$ 46,116	\$ 1,313,864
Assets Limited as to Use	90,000	-	90,000
Patient Accounts Receivable, Net	1,760,199	-	1,760,199
Accrued Interest Receivable	22,353	-	22,353
Supplies	272,235	-	272,235
Prepaid Expenses	96,827	-	96,827
Total Current Assets	3,509,362	46,116	3,555,478
<b>ASSETS LIMITED AS TO USE</b>			
Debt Service Account Under Bond Indenture	1,183,280	-	1,183,280
Board Designated for Capital Improvements	2,392,973	-	2,392,973
Restricted By Donor	124,144	21,532	145,676
Subtotal	3,700,397	21,532	3,721,929
Less: Current Portion	(90,000)	-	(90,000)
Total Assets Limited as to Use	3,610,397	21,532	3,631,929
<b>CAPITAL ASSETS</b>			
Capital Assets	12,813,222	-	12,813,222
Less: Accumulated Depreciation	(5,389,262)	-	(5,389,262)
Net Capital Assets	7,423,960	-	7,423,960
<b>OTHER ASSETS</b>			
Deferred Debt Acquisition Costs	11,996	-	11,996
Total Assets	\$ 14,555,715	\$ 67,648	\$ 14,623,363

See accompanying Notes to Combined Financial Statements.

<b>LIABILITIES AND NET ASSETS</b>	<u>Primary Enterprise</u>	<u>Component Unit (Foundation)</u>	<u>Total Reporting Entity (Memorandum Only)</u>
<b>CURRENT LIABILITIES</b>			
Current Maturities of Long-Term Debt	\$ 90,000	\$ -	\$ 90,000
Accounts Payable	300,162	-	300,162
Due to Third-Party Payors	300,000	-	300,000
Accrued Expenses	512,792	-	512,792
Total Current Liabilities	<u>1,202,954</u>	<u>-</u>	<u>1,202,954</u>
<b>LONG-TERM DEBT, Net of Current Maturities</b>	2,186,580	-	2,186,580
<b>NET ASSETS</b>			
Invested in Capital Assets Net of Related Debt	5,147,380	-	5,147,380
Restricted:			
Expendable for Bond Indenture	1,183,280	-	1,183,280
Expendable for Specific Donor Restrictions	124,144	21,532	145,676
Unrestricted	4,711,377	46,116	4,757,493
Total Net Assets	<u>11,166,181</u>	<u>67,648</u>	<u>11,233,829</u>
Total Liabilities and Net Assets	<u>\$ 14,555,715</u>	<u>\$ 67,648</u>	<u>\$ 14,623,363</u>

WINDOM AREA HOSPITAL  
Windom, Minnesota  
COMBINED STATEMENT OF REVENUES, EXPENSES  
AND CHANGES IN NET ASSETS  
YEAR ENDED APRIL 30, 2007

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
<b>REVENUE</b>			
Net Patient Service Revenue	\$ 11,883,828	\$ -	\$ 11,883,828
Other Revenue	146,191	30,077	176,268
Total Revenue	<u>12,030,019</u>	<u>30,077</u>	<u>12,060,096</u>
<b>EXPENSES</b>			
Nursing Services	3,376,265	-	3,376,265
Other Professional Services	3,542,919	-	3,542,919
General Services	968,046	-	968,046
Administrative and Fiscal Services	2,408,604	30,227	2,438,831
Interest and Amortization	117,550	-	117,550
Depreciation	660,694	-	660,694
Total Expenses	<u>11,074,078</u>	<u>30,227</u>	<u>11,104,305</u>
<b>INCOME (LOSS) FROM OPERATIONS</b>	955,941	(150)	955,791
<b>NONOPERATING REVENUE AND EXPENSES</b>			
Interest Income and Donations	210,308	-	210,308
Noncapital Grants and Contributions	-	9,005	9,005
Loss on Disposal of Assets	(1,909)	-	(1,909)
Total Nonoperating Revenue and Expenses	<u>208,399</u>	<u>9,005</u>	<u>217,404</u>
<b>EXCESS OF REVENUE OVER EXPENSES</b>	1,164,340	8,855	1,173,195
Capital Grants and Contributions	<u>73,487</u>	<u>3,784</u>	<u>77,271</u>
<b>INCREASE IN NET ASSETS</b>	1,237,827	12,639	1,250,466
<b>NET ASSETS</b>			
Beginning of Year	<u>11,166,181</u>	<u>67,648</u>	<u>11,233,829</u>
End of Year	<u>\$ 12,404,008</u>	<u>\$ 80,287</u>	<u>\$ 12,484,295</u>

See accompanying Notes to Combined Financial Statements.

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**COMBINED STATEMENT OF REVENUES, EXPENSES**  
**AND CHANGES IN NET ASSETS**  
**YEAR ENDED APRIL 30, 2006**

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
<b>REVENUE</b>			
Net Patient Service Revenue	\$ 11,429,033	\$ -	\$ 11,429,033
Other Revenue	91,980	25,387	117,367
Total Revenue	<u>11,521,013</u>	<u>25,387</u>	<u>11,546,400</u>
<b>EXPENSES</b>			
Nursing Services	2,891,016	-	2,891,016
Other Professional Services	3,492,346	-	3,492,346
General Services	913,189	-	913,189
Administrative and Fiscal Services	2,421,074	17,674	2,438,748
Interest and Amortization	119,838	-	119,838
Depreciation	609,790	-	609,790
Total Expenses	<u>10,447,253</u>	<u>17,674</u>	<u>10,464,927</u>
<b>INCOME FROM OPERATIONS</b>	1,073,760	7,713	1,081,473
<b>NONOPERATING REVENUE AND EXPENSES</b>			
Interest Income and Donations	122,035	-	122,035
Loss on Disposal of Assets	(2,659)	-	(2,659)
Total Nonoperating Revenue and Expenses	<u>119,376</u>	<u>-</u>	<u>119,376</u>
<b>EXCESS OF REVENUE OVER EXPENSES</b>	1,193,136	7,713	1,200,849
Capital Grants and Contributions	<u>151,260</u>	<u>2,805</u>	<u>154,065</u>
<b>INCREASE IN NET ASSETS</b>	1,344,396	10,518	1,354,914
<b>NET ASSETS</b>			
Beginning of Year	<u>9,821,785</u>	<u>57,130</u>	<u>9,878,915</u>
End of Year	<u>\$ 11,166,181</u>	<u>\$ 67,648</u>	<u>\$ 11,233,829</u>

See accompanying Notes to Combined Financial Statements.

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**COMBINED STATEMENT OF CASH FLOWS**  
**YEAR ENDED APRIL 30, 2007**

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Receipts from and on Behalf of Patients	\$ 11,796,290	\$ -	\$ 11,796,290
Payments to Suppliers and Contractors	(6,340,053)	(30,227)	(6,370,280)
Payments to Employees	(3,794,607)	-	(3,794,607)
Other Receipts and Payments, Net	258,281	39,082	297,363
Net Cash Provided by Operating Activities	<u>1,919,911</u>	<u>8,855</u>	<u>1,928,766</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>			
Capital Grants and Contributions	<u>73,487</u>	<u>3,784</u>	<u>77,271</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Capital Expenditures	(882,949)	-	(882,949)
Cash Payments for Interest	<u>(111,553)</u>	<u>-</u>	<u>(111,553)</u>
Net Cash Used by Capital and Related Financing Activities	(994,502)	-	(994,502)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchases of Investments	(2,221,537)	(12,789)	(2,234,326)
Sale of Investments	1,144,538	-	1,144,538
Capital Contribution for Investment in Partnership	(100,000)	-	(100,000)
Change in Other Assets	(2,878)	-	(2,878)
Interest Income and Donations	210,308	-	210,308
Net Cash Used by Investing Activities	<u>(969,569)</u>	<u>(12,789)</u>	<u>(982,358)</u>
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	29,327	(150)	29,177
Cash and Cash Equivalents - Beginning	<u>1,267,748</u>	<u>46,116</u>	<u>1,313,864</u>
<b>CASH AND CASH EQUIVALENTS - ENDING</b>	<u>\$ 1,297,075</u>	<u>\$ 45,966</u>	<u>\$ 1,343,041</u>

See accompanying Notes to Combined Financial Statements.

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**COMBINED STATEMENT OF CASH FLOWS (CONTINUED)**  
**YEAR ENDED APRIL 30, 2007**

	<u>Primary Enterprise</u>	<u>Component Unit (Foundation)</u>	<u>Total Reporting Entity (Memorandum Only)</u>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>			
Income (Loss) from Operations	\$ 955,941	\$ (150)	\$ 955,791
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:			
Depreciation Expense	660,694	-	660,694
Interest Expense Considered a Capital Financing Activity	113,999	-	113,999
Amortization	3,551	-	3,551
Loss on Disposal of Assets	(1,909)	-	(1,909)
Provision for Bad Debts	351,348	-	351,348
Noncapital Grants and Contributions	-	9,005	9,005
(Increase) Decrease in:			
Patient Accounts Receivable	(521,639)	-	(521,639)
Accrued Interest Receivable	(17,247)	-	(17,247)
Supplies and Prepaid Expenses	16,442	-	16,442
Increase (Decrease) in:			
Accounts Payable	168,813	-	168,813
Due to Third-Party Payors	100,000	-	100,000
Accrued Expenses	89,918	-	89,918
Net Cash Provided by Operating Activities	<u>\$ 1,919,911</u>	<u>\$ 8,855</u>	<u>\$ 1,928,766</u>

See accompanying Notes to Combined Financial Statements.

**WINDOM AREA HOSPITAL**  
**Windom, Minnesota**  
**COMBINED STATEMENT OF CASH FLOWS**  
**YEAR ENDED APRIL 30, 2006**

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Receipts from and on Behalf of Patients	\$ 11,731,210	\$ -	\$ 11,731,210
Payments to Suppliers and Contractors	(6,457,172)	(17,674)	(6,474,846)
Payments to Employees	(3,505,737)	-	(3,505,737)
Other Receipts and Payments, Net	205,608	25,387	230,995
Net Cash Provided by Operating Activities	<u>1,973,909</u>	<u>7,713</u>	<u>1,981,622</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>			
Capital Grants and Contributions	<u>151,260</u>	<u>2,805</u>	<u>154,065</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Capital Expenditures	(1,080,873)	-	(1,080,873)
Cash Payments for Interest	(116,287)	-	(116,287)
Principal Payments on Long-Term Debt	(198,933)	-	(198,933)
Net Cash Used by Capital and Related Financing Activities	<u>(1,396,093)</u>	<u>-</u>	<u>(1,396,093)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchases of Investments	(1,249,652)	(2,805)	(1,252,457)
Sale of Investments	1,020,473	-	1,020,473
Decrease in Other Assets	(2,849)	-	(2,849)
Interest Income and Donations	122,035	-	122,035
Net Cash Used by Investing Activities	<u>(109,993)</u>	<u>(2,805)</u>	<u>(112,798)</u>
<b>INCREASE IN CASH AND CASH EQUIVALENTS</b>	619,083	7,713	626,796
Cash and Cash Equivalents - Beginning	<u>648,665</u>	<u>38,403</u>	<u>687,068</u>
<b>CASH AND CASH EQUIVALENTS - ENDING</b>	<u>\$ 1,267,748</u>	<u>\$ 46,116</u>	<u>\$ 1,313,864</u>

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
COMBINED STATEMENT OF CASH FLOWS (CONTINUED)  
YEAR ENDED APRIL 30, 2006

	Primary Enterprise	Component Unit (Foundation)	Entity (Memorandum Only)
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>			
Income from Operations	\$ 1,073,760	\$ 7,713	\$ 1,081,473
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:			
Depreciation Expense	609,790	-	609,790
Interest Expense Considered a Capital Financing Activity	116,287	-	116,287
Amortization	3,551	-	3,551
Loss on Disposal of Assets	(2,659)	-	(2,659)
Provision for Bad Debts	84,690	-	84,690
Increase in:			
Patient Accounts Receivable	1,627	-	1,627
Accrued Interest Receivable	(9,140)	-	(9,140)
Supplies and Prepaid Expenses	(31,277)	-	(31,277)
Increase (Decrease) in:			
Accounts Payable	(103,246)	-	(103,246)
Due to Third-Party Payors	225,000	-	225,000
Accrued Expenses	5,526	-	5,526
Net Cash Provided by Operating Activities	<u>\$ 1,973,909</u>	<u>\$ 7,713</u>	<u>\$ 1,981,622</u>

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Organization**

Windom Area Hospital (Hospital), an enterprise fund of the City of Windom, Minnesota, is managed by a board of directors appointed by the City Council, and is licensed to provide hospital services. The Hospital is exempt from Federal and State income taxes.

For financial reporting purposes, the Hospital is divided into the "Primary Enterprise" and "Component Unit." The Primary Enterprise consists of the Hospital.

The Windom Area Hospital Foundation, Inc. (Foundation) is a 501(c)(3) Organization whose sole purpose is to support the Windom Area Hospital. The Foundation conducts fundraising campaigns on behalf of the Windom Area Hospital. The Foundation's operations have been discretely presented as a component unit of the Hospital.

The memorandum-only totals aggregate the Primary Enterprise and its Component Unit. In accordance with governmental accounting standards, no consolidating or other eliminations were made in arriving at the totals; thus, they do not represent consolidated information.

**Method of Accounting**

The Hospital reports in accordance with the *Audit and Accounting Guide for Health Care Organizations* published by the American Institute of Certified Public Accountants which prescribes accounting and reporting policies, some of which are unique to providers of health care services.

**Proprietary Fund Accounting**

The Hospital utilizes the proprietary fund method of accounting whereby revenue and expenses are recognized on the accrual basis. Substantially all revenue and expenses are subject to accrual.

**Accounting Standards**

Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, Windom Area Hospital has elected not to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989.

**Use of Estimates**

The preparation of combined financial statements in conformity with U.S. generally accepted accounting principles 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 combined financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

NOTE 1 **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Grants and Contributions**

From time to time, the Hospital receives grants and contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses.

**Cash and Cash Equivalents**

For purposes of the statements of cash flows, cash and cash equivalents are considered to be highly liquid investments with an original maturity of ninety days or less, and exclude assets limited as to use.

**Accounts Receivable and Allowance for Uncollectible Accounts**

The Hospital provides an allowance for uncollectible self-pay and miscellaneous commercial insurance accounts. Patients are not required to provide collateral for services rendered. Payment for services is required upon receipt of an invoice, after payment by insurance, if any. Self-pay accounts are analyzed for collectibility based on the months past due and payment history. An allowance is estimated for these accounts based on the historical experience of the Hospital. Accounts that are determined to be uncollectible are sent to a collection agency and written off at that time. At April 30, 2007 and 2006, the allowance for uncollectible accounts was approximately \$413,000 and \$246,000, respectively.

**Supplies**

Supplies are stated at cost (principally on the first-in, first-out basis) not in excess of market value. Market value is determined by comparison with recent purchases or realizable value.

**Assets Limited as to Use**

Assets limited as to use include assets set aside for debt service, for construction payments, and by the Board of Directors for future capital improvements, over which the Board retains control and may, at its discretion, subsequently use for other purposes.

**Investments**

Investments are recorded at cost, if purchased, or at fair market value on the date received, if by gift or bequest. All investments are carried at market value.

**Investment in Partnership**

The Hospital reports its investment in partnership under the equity method of accounting. The equity method of accounting is generally required when ownership is 50 percent or less. The equity method does not include all the accounts of the entity in the financial statements; rather the investment is carried at cost, adjusted for the partner's share of the earnings, losses and distributions.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

NOTE 1    **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Deferred Debt Acquisition Costs**

Deferred debt acquisition costs are being amortized on the straight-line method over the life of the related debt.

**Capital Assets**

Capital assets are stated at cost, if purchased, or at fair market value on the date received, if donated, less accumulated depreciation. Depreciation is provided on a straight-line basis over the estimated useful lives of the property.

**Policy for Care of the Underserved**

The Hospital provides care to patients who meet certain criteria under their charity care policy without charge or at amounts less than their established rates. The Hospital believes the underserved are those persons who are unable through private resources, employer support, or public aid to provide payment for health care services or those unable to gain access to health related care because of limited resources, inadequate education, or discrimination. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

**Net Patient Service Revenue**

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

**Operating Revenues and Expenses**

The Hospital's statement of revenues, expenses and changes in net assets distinguishes between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services - the Hospital's principal activity. Non-exchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as non-operating revenues. Operating expenses are all expenses incurred to provide health care services.

**Net Assets**

Net assets of the Hospital are classified in three components. *Net assets invested in capital assets net of related debt* consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted expendable net assets are non-capital net assets* that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital. *Unrestricted net assets* are remaining net assets that do not meet the definition of *invested in capital assets net of related debt or restricted*.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**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, and natural disasters. Commercial insurance coverage is purchased for claims arising from such matters.

**Reclassifications**

Certain items in the prior year financial statements have been reclassified to conform to the current year presentation. These reclassifications had no effect on the overall net assets of the Hospital.

**NOTE 2 NET PATIENT SERVICE REVENUE**

The Hospital has agreements with third-party payors which provide for payments to the organization at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows.

**Medicare**

The Hospital has elected the Critical Access Hospital (CAH) designation. As a CAH, the Hospital is reimbursed for inpatient, outpatient and swing beds services for Medicare patients on a reasonable cost basis. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary.

**Medicaid**

Inpatient services rendered to Medicaid program beneficiaries are reimbursed under a reimbursement methodology similar to inpatient Medicare. Outpatient Medicaid services are reimbursed on reasonable cost.

Revenue from the Medicare program accounted for approximately 39 percent and 44 percent for the years ended 2007 and 2006 and revenue from the Medicaid program accounted for approximately 3 percent and 2 percent of the Hospital's net patient revenue for the years ended 2007 and 2006, respectively. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

**Other**

The Hospital has also entered into payment agreements with certain commercial insurance carriers. 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.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

**NOTE 2 NET PATIENT SERVICE REVENUE (CONTINUED)**

The following is a reconciliation of gross patient service revenue to net patient service revenue:

	<u>2007</u>	<u>2006</u>
Gross Patient Service Revenue	\$ 17,429,512	\$ 15,943,960
Adjustments and Discounts:		
Medicare	(3,226,389)	(2,890,415)
Medicaid	(239,820)	(314,749)
Other	(1,728,127)	(1,225,073)
Provision for Bad Debt	(351,348)	(84,690)
Total Adjustments and Discounts	<u>(5,545,684)</u>	<u>(4,514,927)</u>
Net Patient Service Revenue	<u>\$ 11,883,828</u>	<u>\$ 11,429,033</u>

**NOTE 3 ACCOUNTS RECEIVABLE**

Patient accounts receivable reported as current assets by Windom Area Hospital at April 30, 2007 and 2006 consist of these amounts:

	<u>2007</u>	<u>2006</u>
Receivable from Patients and Their Insurance Carriers	\$ 1,615,741	\$ 1,428,863
Receivable from Medicare	562,189	535,831
Receivable from Medicaid	165,560	41,505
Total Patient Accounts Receivable	<u>2,343,490</u>	<u>2,006,199</u>
Less: Allowance for Uncollectible Amounts	(413,000)	(246,000)
Net Patient Accounts Receivable	<u>\$ 1,930,490</u>	<u>\$ 1,760,199</u>

**NOTE 4 DEPOSITS AND INVESTMENTS**

**Deposits**

Minnesota Statutes require that all City Hospitals' deposits be protected by insurance, surety bonds, or collateral. The market value of collateral pledged must equal 110 percent of the deposits not covered by insurance or bonds (140 percent in the case of mortgage notes pledged). Minnesota Statutes also require that securities pledged as collateral be held in safekeeping by the Hospital or in a financial institution other than that furnishing the collateral.

The Hospital's deposits at year-end were fully covered by federal depository insurance or by collateral held by the Hospital's custodial bank in the Hospital's name, with the exception of one bank, which was under collateralized by approximately \$30,000 at April 30, 2007.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

NOTE 4 DEPOSITS AND INVESTMENTS (CONTINUED)

**Investments**

Credit Risk - Minnesota Statutes authorize City Hospitals to invest in obligations of the U.S. Government and its agencies and of the State of Minnesota and its agencies, bankers acceptances, commercial paper, and certain other types of securities.

Interest Rate Risk - The Hospital does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates.

Concentration of Credit Risk - The Hospital places no limit on the amount it may invest in any one issuer or institution.

At April 30, 2007 and 2006, the carrying amounts of deposits and investments are included in the Hospital's balance sheets as follows:

	2007	2006
Carrying Amount:		
Deposits	\$ 6,154,758	\$ 5,035,793
Included in the Following Balance Sheet Captions:		
Cash and Cash Equivalents	\$ 1,343,041	\$ 1,313,864
Debt Service Account Under Bond Indenture	2,051,984	1,183,280
Board Designated for Capital Improvements	2,677,213	2,392,973
Restricted By Donor	82,520	145,676
	\$ 6,154,758	\$ 5,035,793

Debt service funds are designated for the servicing of the General Obligation Hospital Bonds of 2003 and are required by bond indenture agreements.

The Hospital's board of directors has designated certain assets for capital improvements. The board of directors retains control and may, at its discretion, subsequently use these assets for other purposes.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

NOTE 5 CAPITAL ASSETS

Capital Assets (in thousands) for the years ended April 30, 2007 and 2006 consist of the following:

	Balance April 30, 2006	Additions and Transfers	Retirements	Balance April 30, 2007
Land	\$ 24	\$ -	\$ -	\$ 24
Land Improvements	233	32	-	265
Buildings	6,784	-	-	6,784
Fixed Equipment	2,458	-	(4)	2,454
Moveable Equipment	3,236	526	(545)	3,217
Construction in Progress	78	330	-	408
Total at Historical Cost	<u>12,813</u>	<u>888</u>	<u>(549)</u>	<u>13,152</u>
Less Accumulated Depreciation for:				
Land Improvements	(218)	(11)	-	(229)
Buildings	(1,499)	(274)	-	(1,773)
Fixed Equipment	(1,489)	(87)	3	(1,573)
Moveable Equipment	<u>(2,183)</u>	<u>(289)</u>	<u>541</u>	<u>(1,931)</u>
Total Accumulated Depreciation	<u>(5,389)</u>	<u>(661)</u>	<u>544</u>	<u>(5,506)</u>
Capital Assets, Net	<u>\$ 7,424</u>	<u>\$ 227</u>	<u>\$ (5)</u>	<u>\$ 7,646</u>
	Balance April 30, 2005	Additions and Transfers	Retirements	Balance April 30, 2006
Land	\$ 24	\$ -	\$ -	\$ 24
Land Improvements	233	-	-	233
Buildings	5,792	992	-	6,784
Fixed Equipment	1,857	604	(3)	2,458
Moveable Equipment	3,031	548	(343)	3,236
Construction in Progress	1,137	327	(1,386)	78
Total at Historical Cost	<u>12,074</u>	<u>2,471</u>	<u>(1,732)</u>	<u>12,813</u>
Less Accumulated Depreciation for:				
Land Improvements	(188)	(30)	-	(218)
Buildings	(1,270)	(229)	-	(1,499)
Fixed Equipment	(1,405)	(87)	3	(1,489)
Moveable Equipment	<u>(2,203)</u>	<u>(319)</u>	<u>339</u>	<u>(2,183)</u>
Total Accumulated Depreciation	<u>(5,066)</u>	<u>(665)</u>	<u>342</u>	<u>(5,389)</u>
Capital Assets, Net	<u>\$ 7,008</u>	<u>\$ 1,806</u>	<u>\$ (1,390)</u>	<u>\$ 7,424</u>

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

**NOTE 5 CAPITAL ASSETS (CONTINUED)**

Construction in progress at April 30, 2007 relates to an addition and renovation of the dietary department. The project is expected to be completed in fiscal 2008 with a total expected cost of approximately \$1 million. The project is being funded through internal funds therefore there was no capitalized interest.

Construction in progress at April 30, 2006 related to a computer system upgrade. The project was completed in fiscal 2007 with a total cost of approximately \$235,000. The project was funded through internal funds, therefore there was no capitalized interest.

**NOTE 6 INVESTMENT IN PARTNERSHIP**

During April 2007, the Hospital obtained a 7 percent partnership interest in Southwest Minnesota Radiation Center, LLC. The Hospital's initial investment in Southwest Minnesota Radiation Center, LLC was \$100,000 and there was no equity in earnings or distributions for the years ended April 30, 2007 and 2006.

**NOTE 7 LONG-TERM DEBT**

A summary of long-term debt at April 30, 2007 and 2006 consists of the following:

	Balance April 30, 2006	Additions	Reductions	Balance April 30, 2007
2003 Gross Revenue Hospital Bonds	\$ 2,320,000	\$ -	\$ -	\$ 2,320,000
Less: Current Portion				(95,000)
Less: Unamortized Bond Discount				(40,974)
Total Long-Term Debt, Net of Current Maturities				<u>\$ 2,184,026</u>
	Balance April 30, 2005	Additions	Reductions	Balance April 30, 2006
2003 Gross Revenue Hospital Bonds	\$ 2,500,000	\$ -	\$ (180,000)	\$ 2,320,000
Capital Leases	21,379	-	(21,379)	-
	<u>\$ 2,521,379</u>	<u>\$ -</u>	<u>\$ (201,379)</u>	<u>2,320,000</u>
Less: Current Portion				(90,000)
Less: Unamortized Bond Discount				(43,420)
Total Long-Term Debt, Net of Current Maturities				<u>\$ 2,186,580</u>

**2003 Gross Revenue Hospital Bonds:** City of Windom, Minnesota, Gross Revenue Hospital Bonds, Series 2003, maturing in June 2023. Bonds bear interest rate from 1.75 percent to 5.50 percent with an average coupon rate of 5.09 percent. Bonds are secured by the revenues of the Hospital.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

**NOTE 7 LONG-TERM DEBT (CONTINUED)**

The aggregate maturities on long-term debt as of April 30, 2007 are as follows:

<u>Year Ending April 30,</u>	Long-Term Debt	
	Principal	Interest
2008	\$ 95,000	\$ 112,405
2009	95,000	109,317
2010	100,000	105,655
2011	105,000	101,424
2012	110,000	96,718
2013-2017	630,000	398,356
2018-2022	805,000	216,244
2023-2024	380,000	21,129
Total	<u>\$ 2,320,000</u>	<u>\$ 1,161,248</u>

The provisions of the above debt agreement contains various restrictive covenants and certain amounts to be deposited with the trustee. Such deposits are included with assets limited as to use. A capital lease with cost and accumulated amortization of \$224,087 was paid off during fiscal year 2006.

**NOTE 8 DEFINED BENEFIT PENSION PLAN - STATEWIDE**

**Plan Description**

Substantially all employees of the Hospital are required by State Law to belong to the pension plan administered by the Public Employees Retirement Association (PERA).

Disclosure relating to this plan follows:

**Plan Description**

The Hospital contributes to the Public Employees Retirement Fund (PERF), a cost-sharing multiple-employer defined benefit pension plan administered by PERA. PERF provides retirement, disability, and death benefits to plan members and beneficiaries. Benefits are established by State Statute and vest after three years of credited service. PERA issues a publicly available financial report that includes combined financial statements and required supplementary information for the plan. That report may be obtained by contacting PERA, 514 St. Peter Street #200, St. Paul, MN 55102 or by calling 651-296-7460 or 1-800-652-9026.

**Funding Policy**

Plan members are required to contribute 5.50 percent of the annual covered salary and the Hospital is required to contribute at an actuarially determined rate. The current rate is 6.00 percent of annual covered payroll. The contribution requirements of plan members and the Hospital are established and may be amended by State Statute. The Hospital's contributions, equal to the required contributions, to PERF for the years ended April 30, 2007 and 2006 was \$253,503 and \$221,809, respectively.

WINDOM AREA HOSPITAL  
Windom, Minnesota  
NOTES TO COMBINED FINANCIAL STATEMENTS  
APRIL 30, 2007 AND 2006

**NOTE 9    CONCENTRATIONS OF CREDIT RISK**

The Hospital is located in Windom, Minnesota. The Hospital grants credit, without collateral, to its patients, most of whom are local residents and are insured under third-party payor agreements. The Hospital also grants credit, without collateral, for other miscellaneous receivables.

**NOTE 10    CONTINGENCIES**

**Malpractice Claims**

The Hospital's malpractice insurance is a claims made policy. Should this policy lapse and not be replaced with equivalent coverage, claims based upon occurrence during its term, but reported subsequent thereto, will be uninsured.

**Other**

In the normal course of business, there could be various outstanding contingent liabilities such as, but not limited to, the following:

- Lawsuits alleging negligence in care
- Environmental pollution
- Violation of regulatory body's rules and regulations
- Violation of federal and/or state laws

No contingent liabilities such as, but not limited to those described above, are reflected in the accompanying combined financial statements. No such liabilities have been asserted and, therefore, no estimate of loss, if any, is determinable.

**NOTE 11    MANAGEMENT CONTRACT**

The Hospital has a management agreement with Sanford Health Services (Sanford). This agreement gives Sanford, through the Hospital's administrator full authority to implement and fulfill the policy decisions of the Hospital's board of directors. Either party may terminate this agreement with proper notice. Total management fees, including the administrator's salary and benefits, were \$178,519 and \$173,841 for the years ended April 30, 2007 and 2006, respectively.

## INDEPENDENT AUDITORS' REPORT ON LEGAL COMPLIANCE

Board of Directors  
Windom Area Hospital  
Windom, Minnesota

We have audited the combined financial statements of Windom Area Hospital and its discretely presented component unit as of and for the year ended April 30, 2007, and have issued our report thereon dated July 10, 2007.

We conducted our audit in accordance with U.S. generally accepted auditing standards and the provisions of the *Minnesota Legal Compliance Audit Guide for Local Government*, promulgated by the State Auditor pursuant to Minnesota Statute Section 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Local Government* covers seven main categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, tax increment financing, and miscellaneous provisions. Our study included all of the listed categories, except we did not test for tax increment financing as the Hospital has no tax increment financing. The results of our tests indicate that for the items tested, the Hospital complied with the material terms and conditions of applicable legal provisions, except for improper collateralization of deposits as of April 30, 2007.

Minnesota Statute Section 118A.03 Subd. 3, requires Windom Area Hospital to have collateral of at least 110 percent of the amount on deposit in excess of FDIC coverage. Deposits of approximately \$30,000 at their financial institution were not properly collateralized as of April 30, 2007.

This report is intended solely for the information and use of the board of directors, management, and the Office of the State Auditor of Minnesota and is not intended to be and should not be used by anyone other than these specified parties.



LarsonAllen LLP

Minneapolis, Minnesota  
July 10, 2007

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND  
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE  
WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors  
Windom Area Hospital  
Windom, Minnesota

We have audited the combined financial statements of Windom Area Hospital and its discretely presented component unit as of and for the year ended April 30, 2007, and have issued our report thereon dated July 10, 2007. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered Windom Area Hospital's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the entity's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. Material weaknesses are described in the accompanying Schedule of Findings.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Windom Area Hospital's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Windom Area Hospital's responses to the findings identified in our audit are described in the body of the separate letter issued to the board of director's of the Hospital. We did not audit Windom Area Hospital's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management and the board of directors and is not intended to be and should not be used by anyone other than these specified parties.



LarsonAllen LLP

Minneapolis, Minnesota  
July 10, 2007

WINDOM AREA HOSPITAL  
SCHEDULE OF FINDINGS  
APRIL 30, 2007

**Material Weaknesses**

**06-1 Control over the Financial Reporting Process**

As part of the audit, management requested us to prepare a draft of your financial statements, including the related notes to financial statements. Management reviewed, approved, and accepted responsibility for those financial statements prior to their issuance; however, management did not perform a detailed review of the completeness of the footnote disclosures.

Response

Management feels that committing the resources necessary to perform a review of the footnote disclosures for completeness would be a duplication of expenditures, as this is part of the cost of the audit engagement. In addition, the CEO and CFO review internal financial statements on a monthly basis and present the results to the board of directors.

Conclusion

Response accepted.

**06-2 Segregation of Duties --Accounts Payable, Payroll and Accounts Receivable**

The accounts payable clerk currently has the ability to create new vendors, enter invoices, and print checks. Together these functions create an opportunity for misappropriation of the Hospital's assets. We recommend that the ability to create a new vendor be limited to an individual outside of the accounts payable process.

The Hospital's payroll clerk has the ability to set up employees for payment, enter hours, changes wage rates, and process the payroll. This creates an elevated risk of misappropriation of assets wherein one individual could create fictitious employees, modify wage rates, or hours prior to and after payroll generation and other potential acts which could go undetected. We recommend limiting the ability to create a new employee and printing checks to an individual who does not have additional access to other areas of the payroll cycle.

The business office manager at the Hospital is able to write-off patient balances from the Hospital's records, post payments, and has access to cash receipts. We suggest that the ability to post payments be limited to an individual who does not have the access to cash receipts.

Response

Management will review the cost and benefit of implementing these findings in order to strengthen internal controls.

Conclusion

Response accepted.

WINDOM AREA HOSPITAL  
SCHEDULE OF FINDINGS (CONTINUED)  
APRIL 30, 2007

**Material Weaknesses (Continued)**

**06-3 Misstatements Detected by the Audit**

During the course of the audit, several adjusting journal entries were proposed to properly state the balances of the general ledger accounts at year-end.

Response

Management feels that the proposed adjustments were necessary to properly state the balances of the general ledger accounts at year-end. In addition, management will under take the necessary steps in order to ensure the general ledger accounts are accurately maintained throughout the year.

Conclusion

Response accepted.