

WINDOM AREA HOSPITAL
Windom, Minnesota

COMBINED FINANCIAL STATEMENTS

YEARS ENDED APRIL 30, 2012 AND 2011

WINDOM AREA HOSPITAL
Windom, Minnesota
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CliftonLarsonAllen LLP
www.cliftonlarsonallen.com

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, 2012 and 2011, 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.

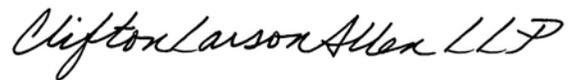
We conducted our audits in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain 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, 2012 and 2011 and the results of its operations, changes in its 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, 2012 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 audits.

Board of Directors
Windom Area Hospital and Affiliate

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such 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. We have applied certain limited procedures to the required supplementary information in accordance with U.S. generally accepted auditing standards, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.



CliftonLarsonAllen LLP

Minneapolis, Minnesota
July 10, 2012

WINDOM AREA HOSPITAL
Windom, Minnesota
MANAGEMENT'S DISCUSSION AND ANALYSIS
APRIL 30, 2012 AND 2011

Introduction

The Windom Area Hospital (Hospital) offers readers of our combined financial statements this narrative overview and analysis of the financial activities of Windom Area Hospital for the fiscal years ended April 30, 2012 and 2011. 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 combined balance sheet, combined statement of revenues, expenses and changes in net assets, and the combined 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 net assets were \$183,091 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 sheets include 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 sheets also provide 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 statements 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 statements 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 \$1,505,047 to \$19,187,085 in FY 2012 and decreased by \$921,808 to \$17,682,038 in FY 2011. Net property, plant and equipment decreased by \$377,367 in FY 2012 and by \$426,069 in FY 2011. Total liabilities increased by \$198,965 in FY 2012 and decreased by \$1,990,825 in FY 2011. The large decrease in liabilities in FY 2011 is due to the 2003 gross revenue bonds being paid off in full during the year. The total margin was 8.8%, 7.8% and 6.4% for the years ended April 30, 2012, 2011 and 2010, respectively.

WINDOM AREA HOSPITAL
Windom, Minnesota
MANAGEMENT'S DISCUSSION AND ANALYSIS
APRIL 30, 2012 AND 2011

Financial Analysis of the Hospital

The combined balance sheets and the combined statements 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 combined balance sheets at April 30, 2012, 2011 and 2010 is presented below:

Table 1
Condensed Combined Balance Sheets (in Thousands)

	April 30,		
	2012	2011	2010
Current Assets	\$ 6,737	\$ 5,516	\$ 4,855
Assets Limited as to Use	6,485	5,823	6,934
Capital Assets	5,965	6,343	6,769
Other Assets	-	-	46
Total Assets	\$ 19,187	\$ 17,682	\$ 18,604
Current Liabilities	\$ 1,046	\$ 847	\$ 947
Long-Term Debt Outstanding	-	-	1,891
Total Liabilities	1,046	847	2,838
Invested in Capital Assets, Net of Related Debt	5,965	6,343	4,773
Restricted	125	106	324
Unrestricted	12,050	10,386	10,670
Total Net Assets	18,141	16,835	15,766
Total Liabilities and Net Assets	\$ 19,187	\$ 17,682	\$ 18,604

As can be seen by Table 1, net assets increased by approximately \$1,306,000 to \$18.1 million in fiscal year 2012. In fiscal year 2011, net assets increased by approximately \$1,069,000 to \$16.8 million. The change in net assets results primarily from operating income.

WINDOM AREA HOSPITAL
Windom, Minnesota
MANAGEMENT'S DISCUSSION AND ANALYSIS
APRIL 30, 2012 AND 2011

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, 2012, 2011 and 2010.

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

	Year Ended April 30,		
	2012	2011	2010
Operating Revenues	\$ 14,905	\$ 13,880	\$ 13,477
Operating Expenses	13,680	12,886	12,778
Operating Income	1,226	994	699
Non-Operating Income	87	85	166
Excess of Revenues over Expenses	1,313	1,079	866
Capital Grants, Contributions, Other	(7)	(10)	15
Changes in Net Assets	1,306	1,069	881
Total Net Assets, Beginning of Year	16,835	15,766	14,885
Total Net Assets, End of Year	<u>\$ 18,141</u>	<u>\$ 16,835</u>	<u>\$ 15,766</u>

Operating and Financial Performance

Volume: Inpatient admissions (excluding newborns) for fiscal year 2012 were 400 compared to 436 in fiscal year 2011 and 508 in fiscal year 2010. This is a decrease of 36 or 8% between 2012 and 2011 and a decrease of 72 or 14% between 2011 and 2010. Patient days (excluding newborns) for fiscal year 2012 were 1,134 compared to 1,161 in fiscal year 2011 and 1,454 in fiscal year 2010. This is a decrease of 27 or 2% from 2011 and a decrease of 293 or 20% between 2011 and 2010. The length of stay decreased from 2.9 days in 2010 to 2.7 days in 2011 and increased to 2.8 days in 2012. Emergency department visits increased to 3,677 in fiscal year 2012 from 3,544 in fiscal year 2011. This is an increase of 133 visits or 4%. They increased from 3,238 in 2010, which is an increase of 306 visits or 9% between 2010 and 2011. All other outpatient visits for 2012 were 17,343 compared to 16,529 in 2011 and 17,289 in 2010. This is an increase of 814 visits from 2011 to 2012 and a decrease of 760 visits from 2010 to 2011. Total surgeries decreased to 1,137 in fiscal year 2012 from 1,161 in fiscal year 2011. This is a decrease of 34 surgeries or 2%. In fiscal year 2011, surgeries decreased from 1,316 which is a decrease of 155 surgeries or 12% compared to fiscal year 2010.

Net Patient Service Revenue: As a result of the rate increases during the year, net patient service revenue increased \$976,872 or approximately 7% compared to fiscal year 2011. Revenue deductions, the amount of patient service revenue uncollectible due to contractual agreements, government reimbursement policies, and bad debts increased to \$6,177,645 from \$5,822,964, an approximately 6% increase.

Other Operating Revenue: Other operating revenue increased \$47,907 and \$99,732 in fiscal years 2012 and 2011, respectively, from the previous year. The increases in fiscal years 2012 and 2011 are due to a smaller share in losses in Southwest MN Radiation Center.

WINDOM AREA HOSPITAL
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MANAGEMENT'S DISCUSSION AND ANALYSIS
APRIL 30, 2012 AND 2011

Nursing Services: Nursing service expenses increased \$350,839 and decreased \$92,696 in fiscal years 2012 and 2011, respectively, from the previous year. The increase in 2012 is a result of training expenses related to a major computer conversion.

Other Professional Services: Other professional services increased \$210,219 and \$246,667 in fiscal years 2012 and 2011, respectively, from the previous year. The large increase in the current year is due to staff training expenses and increased pharmacy drug expenses related to higher utilization and drug shortages.

General Services: General services increased \$110,048 and decreased \$50,375 in fiscal years 2012 and 2011, respectively, when compared to the previous year. Increases in these expenses in 2012 are related to increased maintenance and supply costs.

Administrative and Fiscal Services: Expenses in this category increased by \$169,705 and \$138,278 in fiscal years 2012 and 2011, respectively, when compared to the previous year. Salaries and related employee benefit costs, primarily health insurance continue to rise.

Interest and Amortization: Interest and amortization decreased \$60,005 and \$47,994 in fiscal years 2012 and 2011, respectively, when compared to the previous year. The large decreases are due to the 2003 gross revenue bonds being paid off in full during 2011.

Depreciation: Depreciation increased \$12,478 and decreased \$85,243 in fiscal years 2012 and 2011, respectively, when compared to the previous year. The increase in the current year is a result of current year equipment additions.

Non-Operating Revenue and Expenses: The total in this category increased \$2,523 and decreased \$81,360 in fiscal years 2012 and 2011, respectively, when compared to the previous year. The increase is due to more grants and contributions received at the foundation in 2012.

Capital Assets

At the end of fiscal years 2012, 2011 and 2010, the Hospital had invested \$5,965,455, \$6,342,822 and \$6,768,891, respectively, in net capital assets. The \$377,367 decrease in capital assets in fiscal year 2012 is primarily a result of the annual depreciation offset by minimal additions.

Capital Grants and Contributions

For the years ended 2012, 2011 and 2010, the Hospital had a total of \$12,983, \$9,000 and \$14,982, respectively, in capital grants and contributions. Due to economic conditions in the past three years contributions and grants have significantly decreased.

WINDOM AREA HOSPITAL
Windom, Minnesota
MANAGEMENT'S DISCUSSION AND ANALYSIS
APRIL 30, 2012 AND 2011

Economic and Other Factors and Next Year's Budget

The Windom Area Hospital's Board of Directors and management considered many factors when setting the fiscal year 2013 budget. Of primary importance in setting the 2013 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
- Recovery Audit Contractors
- Government pressure to computerize health records
- Increased expectations for quality at a lower price
- Workforce shortages
- Cost of supplies
- Increasing drug costs and drug shortages
- Aging equipment

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, 2012

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
ASSETS			
CURRENT ASSETS			
Cash and Cash Equivalents	\$ 3,631,318	\$ 103,819	\$ 3,735,137
Patient Accounts Receivable, Net	2,713,716	-	2,713,716
Accrued Interest Receivable	9,511	-	9,511
Supplies	187,762	-	187,762
Prepaid Expenses	90,790	-	90,790
Total Current Assets	<u>6,633,097</u>	<u>103,819</u>	<u>6,736,916</u>
ASSETS LIMITED AS TO USE			
Board Designated for Capital Improvements	6,359,216	-	6,359,216
Restricted by Donor	46,226	79,272	125,498
Total Assets Limited as to Use	<u>6,405,442</u>	<u>79,272</u>	<u>6,484,714</u>
CAPITAL ASSETS			
Capital Assets	14,372,386	-	14,372,386
Less: Accumulated Depreciation	(8,406,931)	-	(8,406,931)
Net Capital Assets	<u>5,965,455</u>	<u>-</u>	<u>5,965,455</u>
Total Assets	<u>\$ 19,003,994</u>	<u>\$ 183,091</u>	<u>\$ 19,187,085</u>

See accompanying Notes to Combined Financial Statements.

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
LIABILITIES AND NET ASSETS			
CURRENT LIABILITIES			
Due to Third-Party Payors	\$ 152,000	\$ -	\$ 152,000
Accounts Payable	187,904	-	187,904
Accrued Expenses	706,237	-	706,237
Total Current Liabilities	<u>1,046,141</u>	<u>-</u>	<u>1,046,141</u>
 Total Liabilities	 1,046,141	 -	 1,046,141
COMMITMENTS AND CONTINGENCIES			
NET ASSETS			
Invested in Capital Assets Net of Related Debt	5,965,455	-	5,965,455
Restricted:			
Expendable for Specific Donor Restrictions	46,226	79,272	125,498
Unrestricted	11,946,172	103,819	12,049,991
Total Net Assets	<u>17,957,853</u>	<u>183,091</u>	<u>18,140,944</u>
 Total Liabilities and Net Assets	 <u>\$ 19,003,994</u>	 <u>\$ 183,091</u>	 <u>\$ 19,187,085</u>

WINDOM AREA HOSPITAL
Windom, Minnesota
COMBINED BALANCE SHEET
APRIL 30, 2011

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
ASSETS			
CURRENT ASSETS			
Cash and Cash Equivalents	\$ 2,986,207	\$ 87,194	\$ 3,073,401
Patient Accounts Receivable, Net	1,991,405	-	1,991,405
Accrued Interest Receivable	10,705	-	10,705
Supplies	281,697	-	281,697
Prepaid Expenses	98,848	-	98,848
Due from Third-Party Payors	60,000	-	60,000
Total Current Assets	5,428,862	87,194	5,516,056
ASSETS LIMITED AS TO USE			
Board Designated for Capital Improvements	5,716,933	-	5,716,933
Restricted by Donor	60,226	46,001	106,227
Total Assets Limited as to Use	5,777,159	46,001	5,823,160
CAPITAL ASSETS			
Capital Assets	14,125,181	-	14,125,181
Less: Accumulated Depreciation	(7,782,359)	-	(7,782,359)
Net Capital Assets	6,342,822	-	6,342,822
Total Assets	\$ 17,548,843	\$ 133,195	\$ 17,682,038

See accompanying Notes to Combined Financial Statements.

	<u>Primary Enterprise</u>	<u>Component Unit (Foundation)</u>	<u>Total Reporting Entity (Memorandum Only)</u>
LIABILITIES AND NET ASSETS			
CURRENT LIABILITIES			
Accounts Payable	\$ 291,491	\$ -	\$ 291,491
Accrued Expenses	555,685	-	555,685
Total Current Liabilities	<u>847,176</u>	<u>-</u>	<u>847,176</u>
Total Liabilities	847,176	-	847,176
COMMITMENTS AND CONTINGENCIES			
NET ASSETS			
Invested in Capital Assets Net of Related Debt	6,342,822	-	6,342,822
Restricted:			
Expendable for Specific Donor Restrictions	60,226	46,001	106,227
Unrestricted	10,298,619	87,194	10,385,813
Total Net Assets	<u>16,701,667</u>	<u>133,195</u>	<u>16,834,862</u>
Total Liabilities and Net Assets	<u>\$ 17,548,843</u>	<u>\$ 133,195</u>	<u>\$ 17,682,038</u>

WINDOM AREA HOSPITAL
Windom, Minnesota
COMBINED STATEMENT OF REVENUES, EXPENSES
AND CHANGES IN NET ASSETS
YEAR ENDED APRIL 30, 2012

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
REVENUE			
Net Patient Service Revenue	\$ 14,708,792	\$ -	\$ 14,708,792
Other Revenue	176,328	20,113	196,441
Total Revenue	<u>14,885,120</u>	<u>20,113</u>	<u>14,905,233</u>
EXPENSES			
Nursing Services	4,120,557	-	4,120,557
Other Professional Services	4,406,721	-	4,406,721
General Services	1,125,060	-	1,125,060
Administrative and Fiscal Services	3,278,079	1,545	3,279,624
Depreciation	747,590	-	747,590
Total Expenses	<u>13,678,007</u>	<u>1,545</u>	<u>13,679,552</u>
INCOME FROM OPERATIONS	1,207,113	18,568	1,225,681
NONOPERATING REVENUE AND EXPENSES			
Interest Income	44,437	-	44,437
Noncapital Grants and Contributions	-	51,150	51,150
Loss on Disposal of Assets	(8,347)	-	(8,347)
Total Nonoperating Revenue and Expenses	<u>36,090</u>	<u>51,150</u>	<u>87,240</u>
EXCESS OF REVENUE OVER EXPENSES	1,243,203	69,718	1,312,921
Capital Grants and Contributions	12,983	-	12,983
Expenses Paid on Behalf of Related Party	(19,822)	-	(19,822)
Related Party Transfers	19,822	(19,822)	-
INCREASE IN NET ASSETS	1,256,186	49,896	1,306,082
NET ASSETS			
Beginning of Year	<u>16,701,667</u>	<u>133,195</u>	<u>16,834,862</u>
End of Year	<u>\$ 17,957,853</u>	<u>\$ 183,091</u>	<u>\$ 18,140,944</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, 2011

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
REVENUE			
Net Patient Service Revenue	\$ 13,731,920	\$ -	\$ 13,731,920
Other Revenue	104,435	44,099	148,534
Total Revenue	<u>13,836,355</u>	<u>44,099</u>	<u>13,880,454</u>
EXPENSES			
Nursing Services	3,769,718	-	3,769,718
Other Professional Services	4,196,502	-	4,196,502
General Services	1,015,012	-	1,015,012
Administrative and Fiscal Services	3,108,353	1,566	3,109,919
Interest and Amortization	60,005	-	60,005
Depreciation	735,112	-	735,112
Total Expenses	<u>12,884,702</u>	<u>1,566</u>	<u>12,886,268</u>
INCOME FROM OPERATIONS	951,653	42,533	994,186
NONOPERATING REVENUE AND EXPENSES			
Interest Income	85,195	-	85,195
Noncapital Grants and Contributions	-	12,639	12,639
Loss on Disposal of Assets	(13,117)	-	(13,117)
Total Nonoperating Revenue and Expenses	<u>72,078</u>	<u>12,639</u>	<u>84,717</u>
EXCESS OF REVENUE OVER EXPENSES	1,023,731	55,172	1,078,903
Capital Grants and Contributions	9,000	-	9,000
Expenses Paid on Behalf of Related Party	(18,886)	-	(18,886)
Related Party Transfers	28,874	(28,874)	-
INCREASE IN NET ASSETS	1,042,719	26,298	1,069,017
NET ASSETS			
Beginning of Year	<u>15,658,948</u>	<u>106,897</u>	<u>15,765,845</u>
End of Year	<u>\$ 16,701,667</u>	<u>\$ 133,195</u>	<u>\$ 16,834,862</u>

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL
Windom, Minnesota
COMBINED STATEMENT OF CASH FLOWS
YEAR ENDED APRIL 30, 2012

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from and on Behalf of Patients	\$ 14,199,675	\$ -	\$ 14,199,675
Payments to Suppliers and Contractors	(7,318,665)	(1,545)	(7,320,210)
Payments to Employees	(5,462,794)	-	(5,462,794)
Other Receipts and Payments, Net	167,981	20,113	188,094
Net Cash Provided by Operating Activities	<u>1,586,197</u>	<u>18,568</u>	<u>1,604,765</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Noncapital Grants and Contributions	-	51,150	51,150
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES			
Capital Expenditures	(370,223)	-	(370,223)
Capital Grants and Contributions	12,983	-	12,983
Net Cash Used by Capital and Related Financing Activities	<u>(357,240)</u>	<u>-</u>	<u>(357,240)</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of Investments	(1,644,055)	(51,150)	(1,695,205)
Sale of Investments	1,015,772	17,879	1,033,651
Expenses Paid on Behalf of Related Party	(19,822)	-	(19,822)
Transfer from (to) Related Party	19,822	(19,822)	-
Interest Income	44,437	-	44,437
Net Cash Used by Investing Activities	<u>(583,846)</u>	<u>(53,093)</u>	<u>(636,939)</u>
INCREASE IN CASH AND CASH EQUIVALENTS			
	645,111	16,625	661,736
Cash and Cash Equivalents - Beginning	<u>2,986,207</u>	<u>87,194</u>	<u>3,073,401</u>
CASH AND CASH EQUIVALENTS - ENDING	<u><u>\$ 3,631,318</u></u>	<u><u>\$ 103,819</u></u>	<u><u>\$ 3,735,137</u></u>

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL
Windom, Minnesota
COMBINED STATEMENT OF CASH FLOWS (CONTINUED)
YEAR ENDED APRIL 30, 2012

	<u>Primary Enterprise</u>	<u>Component Unit (Foundation)</u>	<u>Total Reporting Entity (Memorandum Only)</u>
RECONCILIATION OF INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES			
Income from Operations	\$ 1,207,113	\$ 18,568	\$ 1,225,681
Adjustments to Reconcile Income from Operations to Net Cash Provided by Operating Activities:			
Depreciation Expense	747,590	-	747,590
Loss on Disposal of Assets	(8,347)	-	(8,347)
Provision for Bad Debts	326,253	-	326,253
(Increase) Decrease in:			
Patient Accounts Receivable	(1,048,564)	-	(1,048,564)
Accrued Interest Receivable	1,194	-	1,194
Supplies and Prepaid Expenses	101,993	-	101,993
Increase (Decrease) in:			
Accounts Payable	(103,587)	-	(103,587)
Due to Third-Party Payors	212,000	-	212,000
Accrued Expenses	150,552	-	150,552
Net Cash Provided by Operating Activities	<u>\$ 1,586,197</u>	<u>\$ 18,568</u>	<u>\$ 1,604,765</u>

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL
Windom, Minnesota
COMBINED STATEMENT OF CASH FLOWS
YEAR ENDED APRIL 30, 2011

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from and on Behalf of Patients	\$ 13,652,181	\$ -	\$ 13,652,181
Payments to Suppliers and Contractors	(6,835,069)	(1,566)	(6,836,635)
Payments to Employees	(5,266,062)	-	(5,266,062)
Other Receipts and Payments, Net	145,781	44,099	189,880
Net Cash Provided by Operating Activities	<u>1,696,831</u>	<u>42,533</u>	<u>1,739,364</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Noncapital Grants and Contributions	-	12,639	12,639
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES			
Capital Expenditures	(309,043)	-	(309,043)
Capital Grants and Contributions	9,000	-	9,000
Cash Payments for Interest	(16,904)	-	(16,904)
Principal Payments on Long-Term Debt	(2,030,000)	-	(2,030,000)
Net Cash Used by Capital and Related Financing Activities	<u>(2,346,947)</u>	<u>-</u>	<u>(2,346,947)</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of Investments	(1,621,057)	(12,639)	(1,633,696)
Sale of Investments	2,860,761	33,308	2,894,069
Change in Other Assets	(680)	-	(680)
Expenses Paid on Behalf of Related Party	(18,886)	-	(18,886)
Transfer from (to) Related Party	28,874	(28,874)	-
Interest Income	85,195	-	85,195
Net Cash Provided (Used) by Investing Activities	<u>1,334,207</u>	<u>(8,205)</u>	<u>1,326,002</u>
INCREASE IN CASH AND CASH EQUIVALENTS			
	684,091	46,967	731,058
Cash and Cash Equivalents - Beginning	<u>2,302,116</u>	<u>40,227</u>	<u>2,342,343</u>
CASH AND CASH EQUIVALENTS - ENDING	<u><u>\$ 2,986,207</u></u>	<u><u>\$ 87,194</u></u>	<u><u>\$ 3,073,401</u></u>

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL
Windom, Minnesota
COMBINED STATEMENT OF CASH FLOWS (CONTINUED)
YEAR ENDED APRIL 30, 2011

	Primary Enterprise	Component Unit (Foundation)	Total Reporting Entity (Memorandum Only)
RECONCILIATION OF INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES			
Income from Operations	\$ 951,653	\$ 42,533	\$ 994,186
Adjustments to Reconcile Income from Operations to Net Cash Provided by Operating Activities:			
Depreciation Expense	735,112	-	735,112
Interest Expense Considered a Capital Financing Activity	16,904	-	16,904
Amortization	43,101	-	43,101
Loss on Disposal of Assets	(13,117)	-	(13,117)
Provision for Bad Debts	391,230	-	391,230
Equity in Earnings from Joint Ventures	37,559	-	37,559
(Increase) Decrease in:			
Patient Accounts Receivable	(514,575)	-	(514,575)
Other Accounts Receivable	10,961	-	10,961
Accrued Interest Receivable	6,645	-	6,645
Supplies and Prepaid Expenses	(181)	-	(181)
Increase (Decrease) in:			
Accounts Payable	9,857	-	9,857
Due to Third-Party Payors	26,000	-	26,000
Accrued Expenses	(4,318)	-	(4,318)
Net Cash Provided by Operating Activities	\$ 1,696,831	\$ 42,533	\$ 1,739,364

See accompanying Notes to Combined Financial Statements.

WINDOM AREA HOSPITAL
Windom, Minnesota
NOTES TO COMBINED FINANCIAL STATEMENTS
APRIL 30, 2012 AND 2011

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.

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*, as amended, 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, 2012 AND 2011

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, 2012 and 2011, the allowance for uncollectible accounts was approximately \$523,000 and \$448,000, 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 restricted by donors and assets set aside 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. Assets limited as to use are made up of cash, cash equivalents, money market accounts and certificates of deposit which are carried at amortized cost, which approximates fair 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% or less. The equity method does not include all the accounts of the entity in the combined 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, 2012 AND 2011

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Assets

Capital assets are stated at cost, if purchased, or at fair market value on the date received, if donated, less accumulated depreciation. All capital assets other than land and construction in progress are depreciated on a straight-line basis over the estimated useful lives of the property:

Land Improvements	8-20 Years
Buildings	10-40 Years
Fixed Equipment	5-20 Years
Moveable Equipment	3-20 Years

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, 2012 AND 2011

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.

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 bed 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 according to a prospective DRG payment system. Outpatient Medicaid services are reimbursed on reasonable cost.

Revenue from the Medicare program accounted for approximately 34% and 35% for the years ended 2012 and 2011, respectively, and revenue from the Medicaid program accounted for approximately 1% and 2% for the years ended 2012 and 2011, respectively, of the Hospital's net patient revenue. 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. The 2012 net patient service revenue decreased approximately \$20,000 and the 2011 net patient service revenue increased approximately \$ \$1,000 due to removal of allowance previously estimated that are no longer considered necessary as a result of changes in estimates and years that are no longer subject to audits, reviews, and investigations.

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, 2012 AND 2011

NOTE 2 NET PATIENT SERVICE REVENUE (CONTINUED)

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

	2012	2011
Gross Patient Service Revenue	\$ 20,886,437	\$ 19,554,884
Adjustments and Discounts:		
Medicare	(2,985,653)	(2,506,157)
Medicaid	(473,995)	(410,143)
Other	(2,391,744)	(2,515,434)
Provision for Bad Debt	(326,253)	(391,230)
Total Adjustments and Discounts	(6,177,645)	(5,822,964)
Net Patient Service Revenue	\$ 14,708,792	\$ 13,731,920

NOTE 3 ACCOUNTS RECEIVABLE

Patient accounts receivable reported as current assets by Windom Area Hospital at April 30, 2012 and 2011 consist of these amounts:

	2012	2011
Receivable from Patients and Their Insurance Carriers	\$ 2,376,351	\$ 1,800,910
Receivable from Medicare	642,414	494,416
Receivable from Medicaid	217,951	144,079
Total Patient Accounts Receivable	3,236,716	2,439,405
Less: Allowance for Uncollectible Amounts	(523,000)	(448,000)
Net Patient Accounts Receivable	\$ 2,713,716	\$ 1,991,405

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% of the deposits not covered by insurance or bonds (140% 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.

At April 30, 2012 and 2011, the Hospital's deposits were fully covered by federal depository insurance or by collateral held by the Hospital's custodial bank in the Hospital's name.

WINDOM AREA HOSPITAL
Windom, Minnesota
NOTES TO COMBINED FINANCIAL STATEMENTS
APRIL 30, 2012 AND 2011

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, 2012 and 2011, the carrying amounts of deposits and investments are included in the Hospital's balance sheets as follows:

	2012	2011
Carrying Amount:		
Deposits	\$ 10,219,851	\$ 8,896,561
Included in the Following Balance Sheet Captions:		
Cash and Cash Equivalents	\$ 3,735,137	\$ 3,073,401
Board Designated for Capital Improvements	6,359,216	5,716,933
Restricted By Donor	125,498	106,227
	\$ 10,219,851	\$ 8,896,561

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, 2012 AND 2011

NOTE 5 CAPITAL ASSETS

Capital assets (in thousands) for the years ended April 30, 2012 and 2011 consist of the following:

	Balance April 30, 2011	Additions and Transfers	Retirements	Balance April 30, 2012
Land	\$ 24	\$ -	\$ -	\$ 24
Land Improvements	265	-	-	265
Buildings	7,750	30	-	7,780
Fixed Equipment	2,333	-	-	2,333
Moveable Equipment	3,704	199	(132)	3,771
Construction in Progress	49	150	-	199
Total at Historical Cost	<u>14,125</u>	<u>379</u>	<u>(132)</u>	<u>14,372</u>
Less Accumulated Depreciation for:				
Land Improvements	(251)	(4)	-	(255)
Buildings	(3,083)	(336)	-	(3,419)
Fixed Equipment	(1,758)	(66)	-	(1,824)
Moveable Equipment	(2,690)	(342)	123	(2,909)
Total Accumulated Depreciation	<u>(7,782)</u>	<u>(748)</u>	<u>123</u>	<u>(8,407)</u>
Capital Assets, Net	<u>\$ 6,343</u>	<u>\$ (369)</u>	<u>\$ (9)</u>	<u>\$ 5,965</u>

	Balance April 30, 2010	Additions and Transfers	Retirements	Balance April 30, 2011
Land	\$ 24	\$ -	\$ -	\$ 24
Land Improvements	265	-	-	265
Buildings	7,750	-	-	7,750
Fixed Equipment	2,333	-	-	2,333
Moveable Equipment	3,584	322	(202)	3,704
Construction in Progress	47	2	-	49
Total at Historical Cost	<u>14,003</u>	<u>324</u>	<u>(202)</u>	<u>14,125</u>
Less Accumulated Depreciation for:				
Land Improvements	(247)	(4)	-	(251)
Buildings	(2,746)	(337)	-	(3,083)
Fixed Equipment	(1,690)	(68)	-	(1,758)
Moveable Equipment	(2,551)	(326)	187	(2,690)
Total Accumulated Depreciation	<u>(7,234)</u>	<u>(735)</u>	<u>187</u>	<u>(7,782)</u>
Capital Assets, Net	<u>\$ 6,769</u>	<u>\$ (411)</u>	<u>\$ (15)</u>	<u>\$ 6,343</u>

WINDOM AREA HOSPITAL
Windom, Minnesota
NOTES TO COMBINED FINANCIAL STATEMENTS
APRIL 30, 2012 AND 2011

NOTE 5 CAPITAL ASSETS (CONTINUED)

Construction in progress at April 30, 2012 and 2011 consists of planning costs for a future hospital expansion and renovation project and costs related to an electronic health record and accounting system conversion which was placed in service in May 2012.

NOTE 6 INVESTMENT IN PARTNERSHIP

In April 2007, the Hospital obtained a 7% partnership interest in Southwest Minnesota Radiation Center, LLC. The Hospital's initial investment in Southwest Minnesota Radiation Center, LLC was \$100,000. In June 2008, the Hospital made an additional investment of \$100,000 to obtain a 14% partnership interest in Southwest Minnesota Radiation Center, LLC. During the year ended April 30, 2012, Southwest Minnesota Radiation Center, LLC changed its name to Sanford Cancer Center. The Hospital received no distributions during the years ended April 30, 2012 and 2011. The Hospital's portion of the equity loss was zero and \$37,559 for the years ended April 30, 2012 and 2011, respectively. The Hospital's ending investment balance was zero at April 30, 2012 and 2011.

NOTE 7 DEFINED BENEFIT PENSION PLAN - STATEWIDE

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. The plan is established and administered in accordance with Minnesota State Statutes, Chapters 353 and 356.

Benefits are established by state statute and are based upon the member's highest average salary for any five successive years of allowable service, age and years of credit at termination of service. PERA issues a publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by contacting PERA, 60 Empire Drive, Suite #200, St. Paul, MN 55103 or by calling 651-296-7460 or 1-800-652-9026.

Funding Policy

Plan members are required to contribute 6% of the annual covered salary through December 31, 2010 and 6.25% effective January 1, 2011 and the Hospital is required to contribute at an actuarially determined rate. The current rate is 7.25% 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, 2012 and 2011 was \$399,037 and \$369,759, respectively. The Hospital's contributions were equal to the contractually required contributions for each year as set by state statute.

WINDOM AREA HOSPITAL
Windom, Minnesota
NOTES TO COMBINED FINANCIAL STATEMENTS
APRIL 30, 2012 AND 2011

NOTE 8 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 9 COMMITMENTS AND 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.

Compliance

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Federal government activity had increased with respect to investigations and allegations concerning possible violations by health care providers, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenues for patient services. Management believes the Hospital is in substantial compliance with current laws and regulations.

Operating Leases

The Hospital has various equipment leases and rental agreements that are accounted for as operating leases. Future minimum lease payments for the operating leases by year are as follows:

<u>Year Ending April 30,</u>	<u>Amount</u>
2013	\$ 330,732
2014	330,732
2015	330,732
2016	330,732
2017	330,732
Thereafter	415,905
Total Minimum Lease Payments	<u><u>\$ 2,069,565</u></u>

Total rent expense associated with the operating leases for the years ended April 30, 2012 and 2011 was approximately \$302,000 and \$287,000, respectively.

WINDOM AREA HOSPITAL
Windom, Minnesota
NOTES TO COMBINED FINANCIAL STATEMENTS
APRIL 30, 2012 AND 2011

NOTE 9 COMMITMENTS AND CONTINGENCIES (CONTINUED)

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 10 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 \$246,637 and \$240,351 for the years ended April 30, 2012 and 2011, respectively.



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**INDEPENDENT AUDITORS' REPORT ON
MINNESOTA 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, 2012, and have issued our report thereon dated July 10, 2012.

We conducted our audit in accordance with U.S. generally accepted auditing standards and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, 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 Political Subdivisions* covers seven main categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous county and city, and tax increment districts. Our study included all of the listed categories, except that we did not test for compliance with tax increment financing because this category is not applicable to Windom Area Hospital.

The results of our tests indicate that for the items tested, Windom Area Hospital complied with the material terms and conditions of applicable legal provisions.

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.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Minneapolis, Minnesota
July 10, 2012



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**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF COMBINED 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, 2012, and have issued our report thereon dated July 10, 2012. 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 combined 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 and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A deficiency in internal control 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 and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider deficiencies described in the accompanying Schedule of Findings to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Windom Area Hospital's combined 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 accompanying schedule of findings. 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.



CliftonLarsonAllen LLP

Minneapolis, Minnesota
July 10, 2012

**WINDOM AREA HOSPITAL
SCHEDULE OF FINDINGS
APRIL 30, 2012**

12-1 Control over the Financial Reporting Process

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

Response

Management determined 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.

12-2 Segregation of Duties -- Accounts Payable, Payroll and Accounts Receivable

The Hospital's CFO 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. The accounts payable clerk also has the ability to both enter invoices, and print checks. We recommend the ability to print checks to be limited to someone who does not have access to enter invoices, or add vendors. The Hospital does have a mitigating control in that all checks require two signatures, and one of the signatures would be from an employee other than those mentioned above.

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 Hospital does have a mitigating control where a report showing all new employees is printed and reviewed monthly by another employee.

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 write-offs 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.

**WINDOM AREA HOSPITAL
SCHEDULE OF FINDINGS (CONTINUED)
APRIL 30, 2012**

12-3 Misstatements Detected by the Audit

During the course of the audit, 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 undertake the necessary steps in order to ensure the general ledger accounts are accurately maintained throughout the year.