

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
Accountants' Reports and Consolidated Financial Statements  
June 30, 2011 and 2010





**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**June 30, 2011 and 2010**

**Contents**

|   |               |           |
|---|---------------|-----------|
| <b>Independent Accountants' Report on Financial Statements and Supplementary Information .....</b>  | <b>1</b>      |           |
| <br><b>Consolidated Financial Statements</b>  |               |           |
| Balance Sheets .....  | 3             |           |
| Statements of Revenues, Expenses and Changes in Net Assets .....  | 4             |           |
| Statements of Cash Flows .....  | 5             |           |
| Notes to Financial Statements .....   | 6             |           |
| <br><b>Supplementary Information</b>  |               |           |
| Combining Schedules – Balance Sheet Information .....   | 24            |           |
| Combining Schedules – Statement of Revenues, Expenses and Changes in Net Assets Information .....   | 26            |           |
| <br><b>Independent Accountants' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with <i>Government Auditing Standards</i> .....</b> |               | <b>28</b> |
| <br><b>Schedule of Findings and Responses .....</b>   | <br><b>30</b> |           |

## Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Trustees  
McAlester Regional Health Center Authority  
McAlester, Oklahoma

We have audited the accompanying consolidated balance sheets of McAlester Regional Health Center Authority (the Authority), a component unit of the city of McAlester, Oklahoma, as of June 30, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of McAlester Regional Health Center Authority as of June 30, 2011 and 2010, and its changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 15, 2011, on our consideration of the Authority'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.

Our audits were conducted for the purpose of forming an opinion on the Authority's basic financial statements. The accompanying supplementary combining information, as listed in the table of contents, is presented for purposes of additional analysis of the basic financial statements rather than to present the financial position, changes in financial position and cash flows of the individual entities, and is not a required part of the basic financial statements. The combining information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Board of Trustees  
McAlester Regional Health Center Authority  
Page 2

The Authority has not presented a management's discussion and analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

*BKD, LLP*

December 15, 2011

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Consolidated Balance Sheets**  
**June 30, 2011 and 2010**

**Assets**

|  | <u>2011</u>                 | <u>2010</u>                 |
|--|-----------------------------|-----------------------------|
| <b>Current Assets</b>  |                             |                             |
| Cash and cash equivalents  | \$ 7,135,813                | \$ 6,936,862                |
| Short-term investments   | 1,021,764                   | 1,178,211                   |
| Restricted cash  | 129,849                     | 433,786                     |
| Restricted by lender for capital acquisitions  | 131,285                     | -                           |
| Restricted certificates of deposit for workers' compensation                               | 495,000                     | -                           |
| Note receivable – current  | 25,926                      | -                           |
| Patient accounts receivable, net of allowance;<br>2011 – \$10,128,000, 2010 – \$12,056,000 | 9,794,172                   | 11,486,932                  |
| Estimated amounts due from third-party payers  | 1,000,000                   | 585,000                     |
| Supplies   | 2,246,245                   | 2,026,377                   |
| Prepaid expenses and other   | <u>1,189,955</u>            | <u>1,264,244</u>            |
| Total current assets   | 23,170,009                  | 23,911,412                  |
| <b>Long-term Investments</b>   | 2,997,200                   | 2,478,653                   |
| <b>Capital Assets, Net</b>   | 26,482,125                  | 29,537,472                  |
| <b>Investments in Joint Ventures</b>   | 3,588,906                   | 3,692,944                   |
| <b>Note Receivable – Long-term</b>   | <u>268,282</u>              | <u>-</u>                    |
| Total assets   | <u><u>\$ 56,506,522</u></u> | <u><u>\$ 59,620,481</u></u> |

## Liabilities and Net Assets

|   | <u>2011</u>          | <u>2010</u>          |
|---|----------------------|----------------------|
| <b>Current Liabilities</b>                      |                      |                      |
| Current maturities of long-term debt            | \$ 2,053,057         | \$ 2,613,323         |
| Accounts payable                                | 1,337,427            | 1,726,000            |
| Accrued expenses                                | 4,989,067            | 3,396,229            |
|   | <u>8,379,551</u>     | <u>7,735,552</u>     |
| <b>Long-term Debt</b>                           | <u>2,574,874</u>     | <u>3,867,631</u>     |
|   | <u>10,954,425</u>    | <u>11,603,183</u>    |
| <b>Net Assets</b>                               |                      |                      |
| Invested in capital assets, net of related debt | 22,995,526           | 22,997,808           |
| Restricted – expendable for                     |                      |                      |
| Capital acquisitions and debt service           | 129,849              | 433,786              |
| Workers' compensation claims                    | 495,000              | -                    |
| Specific operating activities                   | 25,000               | 25,000               |
| Unrestricted                                    | 21,906,722           | 24,560,704           |
|   | <u>45,552,097</u>    | <u>48,017,298</u>    |
|   | <u>\$ 56,506,522</u> | <u>\$ 59,620,481</u> |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Consolidated Statements of Revenues, Expenses and Changes in Net Assets**  
**Years Ended June 30, 2011 and 2010**

|  | <b>2011</b>   | <b>2010</b>   |
|--|---------------|---------------|
| <b>Operating Revenues</b>  |               |               |
| Net patient service revenue, net of provision for uncollectible accounts; 2011 – \$12,866,178, 2010 – \$12,847,775 | \$ 73,389,139 | \$ 68,431,063 |
| Other  | 3,521,378     | 3,599,982     |
| Total operating revenues   | 76,910,517    | 72,031,045    |
| <b>Operating Expenses</b>  |               |               |
| Salaries and wages   | 31,749,849    | 33,086,094    |
| Employee benefits  | 6,340,892     | 7,225,200     |
| Purchased services and professional fees   | 12,239,273    | 12,597,780    |
| Supplies and other expenses  | 25,413,129    | 23,215,081    |
| Depreciation and amortization  | 4,369,383     | 4,546,063     |
| Loss on sale of capital assets   | 148,068       | 216,139       |
| Total operating expenses   | 80,260,594    | 80,886,357    |
| <b>Operating Loss</b>  | (3,350,077)   | (8,855,312)   |
| <b>Nonoperating Revenues (Expenses)</b>  |               |               |
| Gain on investments in joint ventures  | 959,306       | 987,542       |
| Investment income  | 246,481       | 267,022       |
| Interest expense   | (334,564)     | (374,377)     |
| Total nonoperating revenues (expenses)   | 871,223       | 880,187       |
| <b>Deficiency of Revenues over Expenses Before Capital Gifts</b>   | (2,478,854)   | (7,975,125)   |
| <b>Gifts to Purchase Capital Assets and Other Capital Gifts</b>  | 13,653        | -             |
| <b>Change in Net Assets</b>  | (2,465,201)   | (7,975,125)   |
| <b>Net Assets, Beginning of Year</b>   | 48,017,298    | 55,992,423    |
| <b>Net Assets, End of Year</b>   | \$ 45,552,097 | \$ 48,017,298 |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Consolidated Statements of Cash Flows**  
**Years Ended June 30, 2011 and 2010**

|  | <b>2011</b>   | <b>2010</b>   |
|--|---------------|---------------|
| <b>Operating Activities</b>  |               |               |
| Receipts from and on behalf of patients                                  | \$ 74,647,785 | \$ 75,590,936 |
| Payments to suppliers and contractors                                    | (34,637,494)  | (36,983,474)  |
| Payments to employees  | (38,494,866)  | (39,998,609)  |
| Other receipts and payments, net   | 3,521,378     | 4,055,031     |
| Net cash provided by operating activities                                | 5,036,803     | 2,663,884     |
| <b>Capital and Related Financing Activities</b>                          |               |               |
| Capital grants and gifts   | 13,653        | -             |
| Proceeds from issuance of long-term debt                                 | -             | 654,187       |
| Principal paid on long-term debt   | (2,745,225)   | (2,462,033)   |
| Interest paid on long-term debt  | (334,564)     | (374,377)     |
| Purchase of capital assets   | (2,139,964)   | (4,686,112)   |
| Proceeds from disposal of capital assets                                 | 37,079        | -             |
| Net cash used in capital and related financing activities                | (5,169,021)   | (6,868,335)   |
| <b>Investing Activities</b>  |               |               |
| Change in restricted assets  | (495,000)     | 1,084,972     |
| Change in note receivable  | (294,208)     | -             |
| Purchase of investments  | (1,842,468)   | (3,583,471)   |
| Proceeds from disposition of investments                                 | 1,585,870     | 3,453,866     |
| Dividends received from investments in joint ventures                    | 1,063,344     | 650,000       |
| Investment income received   | 140,979       | 200,175       |
| Net cash provided by investing activities                                | 158,517       | 1,805,542     |
| <b>Increase (Decrease) in Cash and Cash Equivalents</b>                  | 26,299        | (2,398,909)   |
| <b>Cash and Cash Equivalents, Beginning of Year</b>                      | 7,370,648     | 9,769,557     |
| <b>Cash and Cash Equivalents, End of Year</b>                            | \$ 7,396,947  | \$ 7,370,648  |
| <b>Reconciliation of Cash and Cash Equivalents to the Balance Sheets</b> |               |               |
| Cash and cash equivalents  | \$ 7,135,813  | \$ 6,936,862  |
| Restricted cash  | 129,849       | 433,786       |
| Restricted by lender for capital acquisitions                            | 131,285       | -             |
| Total cash and cash equivalents  | \$ 7,396,947  | \$ 7,370,648  |

See Notes to Consolidated Financial Statements

|  | <u>2011</u>         | <u>2010</u>         |
|--|---------------------|---------------------|
| <b>Reconciliation of Net Operating Expenses to Net Cash Provided by Operating Activities</b> |                     |                     |
| Operating loss   | \$ (3,350,077)      | \$ (8,855,312)      |
| Depreciation and amortization  | 4,369,383           | 4,546,063           |
| Impairment of capital assets   | 1,499,231           | -                   |
| Loss on sale of capital assets   | 148,068             | 216,139             |
| Changes in operating assets and liabilities  |                     |                     |
| Patient and other accounts receivable, net   | 1,673,646           | 8,688,442           |
| Supplies and prepaid expenses  | (5,070)             | 111,557             |
| Estimated amounts due from third-party payers  | (415,000)           | (1,033,687)         |
| Accounts payable and accrued expenses  | 1,116,622           | (1,009,318)         |
|  | <u>1,116,622</u>    | <u>(1,009,318)</u>  |
| Net cash provided by operating activities  | <u>\$ 5,036,803</u> | <u>\$ 2,663,884</u> |
| <b>Supplemental Cash Flows Information</b>   |                     |                     |
| Capital asset purchases in accounts payable  | \$ 24,958           | \$ 58,710           |
| Prepaid expenses in accounts payable   | \$ 192,619          | \$ 71,224           |
| Capital lease obligations incurred for capital assets  | \$ 892,202          | \$ 903,769          |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Consolidated Financial Statements**  
**June 30, 2011 and 2010**

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

***Nature of Operations and Reporting Entity***

The McAlester Regional Health Center Authority (the Authority) was created by a trust indenture dated August 11, 1969, as a public trust and an agency of the state of Oklahoma for the benefit of the City of McAlester, Oklahoma, and the surrounding area. The Authority operates, as its sole activity, McAlester Regional Health Center. Substantially all property and equipment used by the Authority are subject to a 50-year lease agreement with the City of McAlester commencing December 19, 1973. The Authority will have the option to renew the lease for another 50 years upon expiration of the lease in December 2023.

The Authority primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in McAlester, Oklahoma, and surrounding communities. The Authority also operates a rehabilitation unit, skilled nursing unit and provides home health services in the same geographic area.

***Blended Component Units***

The McAlester Regional Health Center Foundation (the Foundation) is a legally separate, tax-exempt component unit of the Authority. The Foundation's primary purpose is to raise and hold funds to support the Authority and its programs. Although the Authority does not control the timing or amount of receipts from the Foundation, the majority of the Foundation's resources and related income are to be used for the benefit of the Authority. The Authority appoints the Board of Directors of the Foundation and, accordingly, is included as a component unit in the Authority's financial statements using the blended method. All significant intercompany accounts and transactions between the Authority and the Foundation have been eliminated in the accompanying consolidated financial statements.

The Auxiliary Volunteer Services of McAlester Regional Health Center (the Auxiliary) is a legally separate component unit of the Authority. The Auxiliary's primary function is to raise and hold funds to support the Authority and its programs. The board of the Auxiliary is self-perpetuating, but the director of the Auxiliary is appointed by the chief executive officer of the Authority. Because the Board of Directors has final approval for the use of all assets of the Auxiliary, the Auxiliary is included as a component unit in the Authority's financial statements using the blended method. All significant intercompany accounts and transactions between the Authority and the Auxiliary have been eliminated in the accompanying consolidated financial statements.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

***Basis of Accounting and Presentation***

The accompanying consolidated financial statements of the Authority have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally, federal and state grants) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Authority first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

The Authority prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, the Authority has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

***Use of Estimates***

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

***Cash Equivalents***

The Authority considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2011 and 2010, cash equivalents consisted primarily of money market accounts with brokers.

***Risk Management***

The Authority is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than those related to workers' compensation and employee health claims. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

The Authority is self-insured for a portion of its exposure to the risk of loss from workers' compensation and employee health claims. Annual estimated provisions are accrued for the self-insured portion of these claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

***Investments and Investment Income***

Investments in U.S. Treasury, agency and instrumentality obligations with a remaining maturity of one year or less at time of acquisition and in nonnegotiable certificates of deposit are carried at amortized cost. The investments in joint ventures are reported on the equity method of accounting. All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income, realized gains and losses on investments sold and the net change for the year in the fair values of investments carried at fair value.

***Patient Accounts Receivable***

The Authority reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Authority provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

***Supplies***

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

***Capital Assets***

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

|                                      |             |
|--------------------------------------|-------------|
| Land improvements                    | 15–20 years |
| Buildings and leasehold improvements | 10–40 years |
| Equipment                            | 3–20 years  |

***Compensated Absences***

Authority policies permit most employees to accumulate paid time off benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Sick leave benefits expected to be realized as paid time off are recognized as expense when the time off occurs and no liability is accrued for such benefits employees have earned but not yet realized. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments, such as Social Security and Medicare taxes, computed using rates in effect at that date.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

***Restricted Cash***

The Authority receives appropriations related to excise taxes levied by two city ordinances to provide revenues for the purpose of financing and construction of a cancer treatment facility, total funds not to exceed \$1,750,000, and a wellness facility, total funds not to exceed \$6,000,000, in the City of McAlester, Oklahoma. The Authority reached the maximum funding levels from each excise tax during 2010. At June 30, 2011 and 2010, approximately \$131,000 and \$434,000, respectively, of the funds under the excise taxes remain unspent and are reflected on the accompanying consolidated balance sheets as restricted cash.

***Restricted Certificates of Deposit***

On August 5, 2010, the Oklahoma Workers' Compensation Court required the Authority to post collateral for self-insured claims of \$495,000 in the event the Authority was unable to pay its claims. As of June 30, 2011, no amounts have been drawn on this collateral. After year-end, the required collateral deposit was increased to \$570,000. At June 30, 2011, the pledged funds are reflected on the accompanying balance sheet as restricted certificates of deposit for workers' compensation.

***Net Assets***

Net assets of the Authority 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 outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital assets that must be used for a particular purpose as specified by creditors, grantors or donors external to the Authority. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the above definitions.

***Net Patient Service Revenue***

The Authority has agreements with third-party payers that provide for payments to the Authority at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

***Charity Care***

The Authority provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Authority does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

***Income Taxes***

As an essential government function of the City, the Authority is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code (the Code) and a similar provision of state law. The Authority's blended component units are generally exempt from income taxes under Section 501 of the Code and under a similar provision of Oklahoma state statutes. However, the Authority and its blended component units are subject to federal income tax on any unrelated business taxable income.

***Subsequent Events***

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

***Reclassifications***

Certain reclassifications have been made to the 2010 financial statements to conform to the 2011 financial statement presentation. The reclassifications had no effect on the change in financial position.

**Note 2: Net Patient Service Revenue**

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

**Medicare** – Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient rehabilitation, skilled nursing and home health services are paid at prospectively determined rates that are based on the patients' acuity. The Authority is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare administrative contractor. The Medicare administrative contractor has audited the Authority's cost reports through June 30, 2009.

**Medicaid** – The Authority has also been reimbursed for services rendered to patients covered by the state Medicaid program at prospectively determined rates per discharge and fee schedules with no retroactive adjustment. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Approximately 66% and 65% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended June 30, 2011 and 2010, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

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

The 2010 net patient service revenue decreased approximately \$8,322,000 due to changes in the methodology for estimating contractual allowances and allowances for doubtful accounts.

**Note 3: Deposits, Investments and Investment Income**

***Deposits***

Custodial credit risk is the risk that, in the event of a bank failure, the Authority's deposits may not be returned to it. The Authority's deposit policy for custodial credit risk requires compliance with the provisions of state law, which requires collateralization of all deposits with federal depository insurance or other acceptable collateral in specific amounts.

At June 30, 2011 and 2010, approximately \$7,767,000 and \$2,361,000, respectively, of the Authority's bank balances of \$9,290,418 and \$8,720,552 were exposed to custodial credit risk as follows:

|   | <b>2011</b>         | <b>2010</b>         |
|---|---------------------|---------------------|
| Uninsured and uncollateralized                                  | \$ 615,000          | \$ -                |
| Uninsured and collateral held by pledging financial institution | 7,152,000           | 2,361,000           |
|   | <b>\$ 7,767,000</b> | <b>\$ 2,361,000</b> |

Effective July 21, 2010, the FDIC insurance limits were permanently increased to \$250,000. Pursuant to legislation enacted in 2010, the FDIC will fully insure all noninterest-bearing transaction accounts beginning December 31, 2010 through December 31, 2012, at all FDIC-insured institutions.

***Investments***

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

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

At June 30, 2011 and 2010, the Authority had the following investments and maturities:

| Type                      | June 30, 2011       |                     |                     |                   |              |
|---------------------------|---------------------|---------------------|---------------------|-------------------|--------------|
|                           | Fair Value          | Maturities in Years |                     |                   |              |
|                           |                     | Less than 1         | 1-5                 | 6-10              | More than 10 |
| Corporate bonds           | \$ 987,204          | \$ 101,318          | \$ 582,715          | \$ 303,171        | \$ -         |
| U.S. Treasury obligations | 943,232             | -                   | 637,526             | 305,706           | -            |
| U.S. agencies obligations | 165,324             | -                   | 165,324             | -                 | -            |
| Money market mutual funds | 163,785             | 163,785             | -                   | -                 | -            |
|                           | <u>2,259,545</u>    | <u>\$ 265,103</u>   | <u>\$ 1,385,565</u> | <u>\$ 608,877</u> | <u>\$ -</u>  |
| Corporate stocks          | 462,562             |                     |                     |                   |              |
| Accrued investment income | <u>17,161</u>       |                     |                     |                   |              |
|                           | <u>\$ 2,739,268</u> |                     |                     |                   |              |

| Type                      | June 30, 2010       |                     |                     |                   |              |
|---------------------------|---------------------|---------------------|---------------------|-------------------|--------------|
|                           | Fair Value          | Maturities in Years |                     |                   |              |
|                           |                     | Less than 1         | 1-5                 | 6-10              | More than 10 |
| Corporate bonds           | \$ 1,109,705        | \$ -                | \$ 685,306          | \$ 424,399        | \$ -         |
| U.S. Treasury obligations | 825,781             | -                   | 760,274             | 65,507            | -            |
| U.S. agencies obligations | 163,575             | -                   | 163,575             | -                 | -            |
| Money market mutual funds | 88,584              | 88,584              | -                   | -                 | -            |
|                           | <u>2,187,645</u>    | <u>\$ 88,584</u>    | <u>\$ 1,609,155</u> | <u>\$ 489,906</u> | <u>\$ -</u>  |
| Corporate stocks          | 356,004             |                     |                     |                   |              |
| Accrued investment income | <u>17,538</u>       |                     |                     |                   |              |
|                           | <u>\$ 2,561,187</u> |                     |                     |                   |              |

**Interest Rate Risk** – The Authority’s investment policy does not specifically limit the maturity of investments as a means of limiting its exposure to fair value losses arising from rising interest rates. The money market mutual funds are presented as an investment with a maturity of less than one year because they are redeemable in full immediately.

# McAlester Regional Health Center Authority

A Component Unit of the City of McAlester, Oklahoma

## Notes to Financial Statements

June 30, 2011 and 2010

**Credit Risk** – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The Authority’s investment policy does not specifically address management of credit risk. At June 30, 2011 and 2010, the Authority’s investments not directly guaranteed by the U.S. government were rated as follows:

| Investments               | June 30, 2011 |           |
|---------------------------|---------------|-----------|
|                           | Moody’s       | S & P     |
| Corporate bonds           | A3–Aaa        | A – AA+   |
| U.S. agencies obligations | Aaa           | AA+       |
| Money market mutual funds | Not Rated     | Not Rated |

  

| Investments               | June 30, 2010 |           |
|---------------------------|---------------|-----------|
|                           | Moody’s       | S & P     |
| U.S. agencies obligations | Aaa           | Not Rated |
| Corporate bonds           | Baa–Aaa       | B–AAA     |
| Money market mutual funds | Not Rated     | Not Rated |

**Custodial Credit Risk** – For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Authority’s investment policy does not address custodial credit risk.

**Concentration of Credit Risk** – The Authority limits exposure of the portfolio to any one issuer, other than the U.S. government or its agencies, to 25% of the market value of the fund in one industry and 10% in any one company. At June 30, 2011 and 2010, the following investments not explicitly guaranteed by the U.S. government exceeded 5% of the total fair value of all investments:

| Investment                             | 2011       |                     | 2010       |                     |
|--|------------|---------------------|------------|---------------------|
|  | Fair Value | Percentage of Total | Fair Value | Percentage of Total |
| Federal Home Loan Mortgage Corporation | \$ 165,324 | 6.04%               | \$ 163,575 | 6.39%               |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

**Summary of Carrying Values**

The carrying values of deposits and investments shown above are included in the accompanying consolidated balance sheets as follows:

|  | <u>2011</u>          | <u>2010</u>          |
|--|----------------------|----------------------|
| Carrying value   |                      |                      |
| Deposits   | \$ 9,171,643         | \$ 8,466,325         |
| Investments  | <u>2,739,268</u>     | <u>2,561,187</u>     |
|  | <u>\$ 11,910,911</u> | <u>\$ 11,027,512</u> |
| Included in the following balance sheet captions             |                      |                      |
| Cash and cash equivalents                                    | \$ 7,135,813         | \$ 6,936,862         |
| Short-term investments                                       | 1,021,764            | 1,178,211            |
| Restricted cash  | 129,849              | 433,786              |
| Restricted by lender for capital acquisitions                | 131,285              | -                    |
| Restricted certificates of deposit for workers' compensation | 495,000              | -                    |
| Long-term investments  | <u>2,997,200</u>     | <u>2,478,653</u>     |
|  | <u>\$ 11,910,911</u> | <u>\$ 11,027,512</u> |

**Investment Income**

Investment income for the years ended June 30 consisted of:

|   | <u>2011</u>       | <u>2010</u>       |
|---|-------------------|-------------------|
| Interest and dividend income              | \$ 136,839        | \$ 200,660        |
| Net increase in fair value of investments | <u>109,642</u>    | <u>66,362</u>     |
|   | <u>\$ 246,481</u> | <u>\$ 267,022</u> |

**Investment Risks and Uncertainties**

The Authority invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying consolidated balance sheets.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

**Note 4: Patient Accounts Receivable**

The Authority grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at June 30 consisted of:

|   | <u>2011</u>         | <u>2010</u>          |
|---|---------------------|----------------------|
| Medicare                                  | \$ 3,916,612        | \$ 3,464,394         |
| Medicaid                                  | 1,317,944           | 1,361,080            |
| Other third-party payers                  | 7,148,702           | 10,935,393           |
| Patients                                  | <u>7,538,914</u>    | <u>7,782,065</u>     |
|   | 19,922,172          | 23,542,932           |
| Less allowance for uncollectible accounts | <u>10,128,000</u>   | <u>12,056,000</u>    |
|   | <u>\$ 9,794,172</u> | <u>\$ 11,486,932</u> |

**Note 5: Investments in Joint Ventures**

The investments in joint ventures relate to an 18% ownership in Heartland Healthcare Reciprocal Risk Retention Group (Heartland) and is accounted for using the equity method of accounting; a 50% ownership in McAlester Ambulatory Surgery Center, LLC and is accounted for using the equity method; a 50% ownership in McAlester Regional Dialysis Center, LLC and is accounted for using the equity method. Financial position and results of operations from unaudited financial statements of the joint venture entities for the fiscal years ended June 30 are summarized below:

|  |  | <u>June 30, 2011</u>  |  |
|--|--|---|--|
|  | <u>December 31,<br/>2010<br/>Heartland</u> | <u>McAlester<br/>Ambulatory<br/>Surgery<br/>Center, LLC</u> | <u>McAlester<br/>Regional<br/>Dialysis<br/>Center, LLC</u> |
| Current assets                           | \$ 14,716,074                              | \$ 2,884,254  | \$ 1,203,661   |
| Property and other long-term assets, net | <u>13,998</u>                              | <u>384,757</u>  | <u>1,015,340</u>   |
| Total assets                             | <u>\$ 14,730,072</u>                       | <u>\$ 3,269,011</u>   | <u>\$ 2,219,001</u>  |
| Total liabilities                        | \$ 5,774,564                               | \$ 201,223  | \$ 678,179   |
| Partners' equity                         | <u>8,955,508</u>                           | <u>3,067,788</u>  | <u>1,540,822</u>   |
| Total liabilities and partners' equity   | <u>\$ 14,730,072</u>                       | <u>\$ 3,269,011</u>   | <u>\$ 2,219,001</u>  |
| Revenues                                 | <u>\$ 3,382,756</u>                        | <u>\$ 3,163,396</u>   | <u>\$ 3,570,004</u>  |
| Excess of revenues over expenses         | <u>\$ 1,835,714</u>                        | <u>\$ 704,558</u>   | <u>\$ 657,367</u>  |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

|   | <b>December 31,<br/>2009<br/>Heartland</b> | <b>June 30, 2010</b>  |  |
|---|--|---|--|
|   |  | <b>McAlester<br/>Ambulatory<br/>Surgery<br/>Center, LLC</b> | <b>McAlester<br/>Regional<br/>Dialysis<br/>Center, LLC</b> |
| Current assets                                | \$ 12,812,781                              | \$ 3,247,148  | \$ 1,064,098   |
| Property and other long-term assets, net      | 20,997                                     | 329,454   | 1,246,927  |
| <b>Total assets</b>                           | <b>\$ 12,833,778</b>                       | <b>\$ 3,576,602</b>   | <b>\$ 2,311,025</b>  |
| Total liabilities                             | \$ 5,879,019                               | \$ 163,373  | \$ 877,590   |
| Partners' equity                              | 6,954,759                                  | 3,413,229   | 1,433,435  |
| <b>Total liabilities and partners' equity</b> | <b>\$ 12,833,778</b>                       | <b>\$ 3,576,602</b>   | <b>\$ 2,311,025</b>  |
| Revenues                                      | \$ 3,567,280                               | \$ 3,758,689  | \$ 3,138,083   |
| Excess of revenues over expenses              | \$ 1,208,984                               | \$ 1,148,464  | \$ 367,709   |

Complete financial statements of the joint venture entities may be obtained by contacting the Authority's management.

The Authority purchases its professional liability (medical malpractice) and general liability insurance coverage from Heartland (see *Note 7*). For the years ended June 30, 2011 and 2010, the Authority paid approximately \$372,000 and \$508,000, respectively, to Heartland for the coverage. The Authority's investment in Heartland was \$1,270,016 as of June 30, 2011 and 2010.

McAlester Ambulatory Surgery Center, LLC (the Surgery Center) is a joint venture with Warren Clinic, organized to operate an ambulatory surgery center in McAlester, Oklahoma. The Authority leases employees to the Surgery Center and provides insurance coverage and supplies on a limited basis. The Surgery Center paid the Authority approximately \$904,000 and \$1,005,000 during 2011 and 2010, respectively. At June 30, 2011 and 2010, the Surgery Center owed the Authority approximately \$71,000 and \$70,000, respectively. The Authority's investment in the Surgery Center was \$1,533,893 and \$1,706,614 as of June 30, 2011 and 2010, respectively.

McAlester Regional Dialysis Center, LLC (the Dialysis Center) is a joint venture with a physician, organized to operate a dialysis facility in McAlester, Oklahoma. The Authority leases employees to the Dialysis Center and provides insurance coverage and supplies on a limited basis. The Dialysis Center paid the Authority approximately \$1,082,000 and \$1,052,000 during 2011 and 2010, respectively. At June 30, 2011 and 2010, the Dialysis Center owed the Authority approximately \$196,000 and \$161,000, respectively. The Authority's investment in the Dialysis Center was \$784,997 and \$716,314 as of June 30, 2011 and 2010, respectively.



**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

**Note 7: Medical Malpractice Claims**

The Authority purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Authority's claims experience, an accrual of approximately \$125,000 and \$160,000 has been made as of June 30, 2011 and 2010, respectively. It is reasonably possible that this estimate could change materially in the near term.

The Authority is a subscriber (member) of Heartland Healthcare Reciprocal Risk Retention Group (Heartland), an entity approved by the state of Vermont to provide hospital professional and general liability coverage to its subscribers. Heartland was formed in order to stabilize the cost and availability of hospital professional and general liability insurance by taking advantage of the self-funding capabilities of a homogenous group of health care providers. Heartland members are provided hospital professional and general liability insurance under claims-made policies on a fixed premium basis. See *Note 5* for additional information about Heartland.

**Note 8: Self-Insured Claims**

Substantially all of the Authority's employees and their dependents are eligible to participate in the Authority's employee health insurance plan. The Authority is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of approximately \$100,000 and any amounts over \$1,000,000. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount of \$100,000 up to \$1,000,000.

The Authority is self-insured for risks related to workers' compensation claims up to \$400,000 per occurrence with an annual liability limit of \$1,000,000 in the aggregate.

A provision is accrued for self-insured employee health claims and workers' compensation claims, including both claims reported and claims incurred but not yet reported. The accruals are estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Authority's estimates will change by a material amount in the near term.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

Activity in the Authority's accrued employee health and workers' compensation claims liability during 2011 and 2010 is summarized as follows:

|  | <b>June 30, 2011</b>   |                              |
|--|------------------------|------------------------------|
|  | <b>Employee Health</b> | <b>Workers' Compensation</b> |
| Balance, beginning of year   | \$ 621,764             | \$ 566,650                   |
| Current year claims incurred and changes in estimates for claims incurred in prior years | 3,088,754              | 240,949                      |
| Claims and expenses paid   | (3,510,518)            | (239,293)                    |
| Balance, end of year   | \$ 200,000             | \$ 568,306                   |

|  | <b>June 30, 2010</b>   |                              |
|--|------------------------|------------------------------|
|  | <b>Employee Health</b> | <b>Workers' Compensation</b> |
| Balance, beginning of year   | \$ 165,402             | \$ 736,514                   |
| Current year claims incurred and changes in estimates for claims incurred in prior years | 3,457,005              | 463,815                      |
| Claims and expenses paid   | (3,000,643)            | (633,679)                    |
| Balance, end of year   | \$ 621,764             | \$ 566,650                   |

**Note 9: Long-Term Debt**

The following is a summary of long-term debt transactions for the Authority for the years ended June 30:

|                           | <b>2011</b>              |                  |                   |                  |                       |                        |
|---------------------------|--------------------------|------------------|-------------------|------------------|-----------------------|------------------------|
|                           | <b>Beginning Balance</b> | <b>Additions</b> | <b>Deductions</b> | <b>Transfers</b> | <b>Ending Balance</b> | <b>Current Portion</b> |
| Notes payable to banks    | \$ 2,443,073             | \$ -             | \$ 939,571        | \$ -             | \$ 1,503,502          | \$ 385,508             |
| Notes payable to vendors  | -                        | -                | -                 | 976,294          | 976,294               | 653,236                |
| Capital lease obligations | 4,037,881                | 892,202          | 1,805,654         | (976,294)        | 2,148,135             | 1,014,313              |
| Total long-term debt      | \$ 6,480,954             | \$ 892,202       | \$ 2,745,225      | \$ -             | \$ 4,627,931          | \$ 2,053,057           |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

|                           | 2010                 |              |              |           |                   |                    |
|---------------------------|----------------------|--------------|--------------|-----------|-------------------|--------------------|
|                           | Beginning<br>Balance | Additions    | Deductions   | Transfers | Ending<br>Balance | Current<br>Portion |
| Notes payable to banks    | \$ 2,635,893         | \$ 654,187   | \$ 847,007   | \$ -      | \$ 2,443,073      | \$ 921,605         |
| Capital lease obligations | 4,749,138            | 903,769      | 1,615,026    | -         | 4,037,881         | 1,691,718          |
| Total long-term debt      | \$ 7,385,031         | \$ 1,557,956 | \$ 2,462,033 | \$ -      | \$ 6,480,954      | \$ 2,613,323       |

**Notes Payable to Banks**

The notes payable to banks are due between August 2011 and December 2022, payable monthly, including interest at rates of 3.25% to 5.50%. The notes are secured by real estate and certain capital assets. The debt service requirements as of June 30, 2011, are as follows:

| Year Ending June 30, | Total to be<br>Paid | Principal    | Interest   |
|----------------------|---------------------|--------------|------------|
| 2012                 | \$ 446,692          | \$ 385,508   | \$ 61,184  |
| 2013                 | 285,614             | 236,495      | 49,119     |
| 2014                 | 221,870             | 182,994      | 38,876     |
| 2015                 | 494,803             | 472,966      | 21,837     |
| 2016                 | 44,392              | 33,155       | 11,237     |
| 2017–2021            | 186,605             | 152,897      | 33,708     |
| 2022–2023            | 41,397              | 39,487       | 1,910      |
|                      | \$ 1,721,373        | \$ 1,503,502 | \$ 217,871 |

**Notes Payable to Vendor**

As discussed in *Note 14*, agreements previously recorded in obligations under capital lease were transferred to notes payable to vendor. The notes payable to vendor are due between August 2012 and November 2013, payable monthly, including interest at rates of 8.18% to 9.45%. The debt service requirements as of June 30, 2011, are as follows:

| Year Ending June 30, | Total to be<br>Paid | Principal  | Interest  |
|----------------------|---------------------|------------|-----------|
| 2012                 | \$ 713,676          | \$ 653,236 | \$ 60,440 |
| 2013                 | 266,025             | 251,766    | 14,259    |
| 2014                 | 72,772              | 71,292     | 1,480     |
|                      | \$ 1,052,473        | \$ 976,294 | \$ 76,179 |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

***Capital Lease Obligations***

The Authority is obligated under leases for equipment that are accounted for as capital leases. The following is a schedule by year of future minimum lease payments under the capital leases, including interest at rates of 3.77% to 7.00% together with the present value of the future minimum lease payments as of June 30, 2011:

| Year Ending June 30,                           |              |
|--|--------------|
| 2012   | \$ 1,094,269 |
| 2013   | 670,314      |
| 2014   | 341,962      |
| 2015   | 160,713      |
| 2016   | 19,806       |
| Total minimum lease payments                   | 2,287,064    |
| Less amount representing interest              | 138,929      |
| Present value of future minimum lease payments | \$ 2,148,135 |

**Note 10: Related-Party Transactions**

McAlester Public Health Authority (MPHA) operates a building in which it leases space to tenants. The Authority appoints some of the board members of MPHA. MPHA is not consolidated with the Authority as the Authority does not have financial accountability for MPHA. The Authority provides administrative services and maintenance to MPHA for a monthly fee. For the years ended June 30, 2011 and 2010, MPHA paid approximately \$60,000 to the Authority.

**Note 11: Charity Care and Uncompensated Care**

In support of its mission, the Authority voluntarily provides free care to patients who lack financial resources and are deemed to be medically indigent. Because the Authority does not pursue collection of amounts determined to qualify as charity care, they are not reported in net patient service revenue. In addition, the Authority provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts which are less than established charges for the services provided to the recipients and many times the payments are less than the cost of rendering the services provided.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

Uncompensated charges relating to these services are approximately as follows:

|  | <b>2011</b>   | <b>2010</b>   |
|--|---------------|---------------|
| Charity allowances                           | \$ 1,865,000  | \$ 2,049,000  |
| State Medicaid and other public aid programs | 20,100,000    | 19,437,000    |
|  | \$ 21,965,000 | \$ 21,486,000 |

In addition to uncompensated charges, the Authority also commits significant time and resources to endeavors and critical services which meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screening and assessments, prenatal education and care, community educational services and various support groups.

**Note 12: Pension Plan**

The Authority contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Authority's required contributions, determined in accordance with the terms of the plan. The plan is administered by the Authority's Board of Trustees. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Authority's governing body. Contribution rates for plan members and the Authority, expressed as a percentage of covered payroll, were 3.7% and 1.9% for 2011 and 4.0% and 1.8% for 2010, respectively. Contributions actually made by plan members and the Authority aggregated approximately \$1,057,000 and \$537,000 during 2011 and \$1,114,000 and \$535,000 during 2010, respectively.

**Note 13: Risks and Uncertainties**

***Current Economic Conditions***

The current protracted economic decline continues to present hospitals with unprecedented circumstances and challenges, which in some cases have resulted in large declines in the fair values of investments and other assets, large declines in contributions, constraints on liquidity and difficulty obtaining financing. The accompanying consolidated financial statements have been prepared using values and information currently available to the Authority.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Notes to Financial Statements**  
**June 30, 2011 and 2010**

Current economic conditions, including the rising unemployment rate, have made it difficult for certain of the Authority's patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net patient service revenue, which could have an adverse impact on the Authority's future operating results. Further, the effect of economic conditions on the state may have an adverse effect on cash flows related to the Medicaid program.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the accompanying consolidated financial statements could change rapidly, resulting in material future adjustments in investment values and allowances for accounts that could negatively impact the Authority's ability to meet debt covenants or maintain sufficient liquidity.

***Litigation***

In the normal course of business, the Authority is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Authority's self-insurance program (discussed elsewhere in these notes) or by commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Authority evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

**Note 14: Subsequent Events**

The Authority signed an agreement effective September 26, 2006 (the Agreement) with an information technology (IT) vendor to provide hardware, software and related support services to the Authority in various phases over multiple years. Each phase was funded through its own financing agreement, generally accounted for as capital leases by the Authority. A component of the Agreement outsourced the management of certain IT functions to the vendor over a 10-year term starting on November 1, 2010, at a monthly cost ranging from \$93,772 to \$188,584.

During 2011, the Authority notified the vendor of its intent to terminate the Agreement and entered into settlement discussions on damages entitled to the vendor as a result of early termination. On September 30, 2011, the parties signed a settlement agreement and mutual release at a cost of \$1,950,000 to the Authority. The liability is recorded in accrued expenses on the accompanying consolidated balance sheets.

As a result of terminating the Agreement, management discontinued use of the IT system and concluded the remaining assets under capital lease, including various components included in construction in progress, were impaired. The remaining capital lease obligations were transferred to notes payable to vendor during 2011 (*See Note 9*). At June 30, 2011, the Authority recorded a loss on impairment of capital assets in the amount of \$1,500,000 and a loss on settlement of \$1,950,000 recognized in supplies and other expenses on the accompanying consolidated statement of revenues, expenses and changes in net assets.

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Combining Schedule – Balance Sheet Information**  
**June 30, 2011**

|  | <b>McAlester<br/>Regional<br/>Health Center<br/>Authority</b> | <b>Blended<br/>Component<br/>Units</b> | <b>Total</b>         | <b>Eliminations</b> | <b>Combined<br/>Balance</b> |
|--|---|--|----------------------|---------------------|-----------------------------|
| <b>Assets</b>  |   |  |                      |                     |                             |
| <b>Current Assets</b>  |   |  |                      |                     |                             |
| Cash and cash equivalents                                    | \$ 6,828,505  | \$ 307,308                             | \$ 7,135,813         | \$ -                | \$ 7,135,813                |
| Short-term investments                                       | 758,427   | 263,337                                | 1,021,764            | -                   | 1,021,764                   |
| Restricted cash  | 129,849   | -                                      | 129,849              | -                   | 129,849                     |
| Restricted by lender for capital acquisitions                | 131,285   | -                                      | 131,285              | -                   | 131,285                     |
| Restricted certificates of deposit for workers' compensation | 495,000   | -                                      | 495,000              | -                   | 495,000                     |
| Note receivable – current                                    | 25,926  | -                                      | 25,926               | -                   | 25,926                      |
| Patient accounts receivable, net of allowance                | 9,794,172   | -                                      | 9,794,172            | -                   | 9,794,172                   |
| Estimated amounts due from third-party payers                | 1,000,000   | -                                      | 1,000,000            | -                   | 1,000,000                   |
| Supplies   | 2,231,774   | 14,471                                 | 2,246,245            | -                   | 2,246,245                   |
| Prepaid expenses and other                                   | 1,189,955   | -                                      | 1,189,955            | -                   | 1,189,955                   |
| Total current assets   | 22,584,893  | 585,116                                | 23,170,009           | -                   | 23,170,009                  |
| <b>Long-term Investments</b>                                 | 2,997,200   | -                                      | 2,997,200            | -                   | 2,997,200                   |
| <b>Capital Assets, Net</b>                                   | 26,482,125  | -                                      | 26,482,125           | -                   | 26,482,125                  |
| <b>Investments in Joint Ventures</b>                         | 3,588,906   | -                                      | 3,588,906            | -                   | 3,588,906                   |
| <b>Note Receivable – Long-term</b>                           | 268,282   | -                                      | 268,282              | -                   | 268,282                     |
| Total assets   | <u>\$ 55,921,406</u>  | <u>\$ 585,116</u>                      | <u>\$ 56,506,522</u> | <u>\$ -</u>         | <u>\$ 56,506,522</u>        |

|   | <b>McAlester<br/>Regional<br/>Health Center<br/>Authority</b> | <b>Blended<br/>Component<br/>Units</b> | <b>Total</b>         | <b>Eliminations</b> | <b>Combined<br/>Balance</b> |
|---|---|--|----------------------|---------------------|-----------------------------|
| <b>Liabilities and Net Assets</b>               |   |  |                      |                     |                             |
| <b>Current Liabilities</b>                      |   |  |                      |                     |                             |
| Current maturities of long-term debt            | \$ 2,053,057  | \$ -                                   | \$ 2,053,057         | \$ -                | \$ 2,053,057                |
| Accounts payable                                | 1,337,427   | -                                      | 1,337,427            | -                   | 1,337,427                   |
| Accrued expenses                                | 4,974,923   | 14,144                                 | 4,989,067            | -                   | 4,989,067                   |
|   | <u>8,365,407</u>  | <u>14,144</u>                          | <u>8,379,551</u>     | <u>-</u>            | <u>8,379,551</u>            |
| Total current liabilities                       |   |  |                      |                     |                             |
|   | <u>8,365,407</u>  | <u>14,144</u>                          | <u>8,379,551</u>     | <u>-</u>            | <u>8,379,551</u>            |
| <b>Long-term Debt</b>                           | <u>2,574,874</u>  | <u>-</u>                               | <u>2,574,874</u>     | <u>-</u>            | <u>2,574,874</u>            |
|   |   |  |                      |                     |                             |
| Total liabilities                               | <u>10,940,281</u>   | <u>14,144</u>                          | <u>10,954,425</u>    | <u>-</u>            | <u>10,954,425</u>           |
| <b>Net Assets</b>                               |   |  |                      |                     |                             |
| Invested in capital assets, net of related debt | 22,995,526  | -                                      | 22,995,526           | -                   | 22,995,526                  |
| Restricted – expendable for                     |   |  |                      |                     |                             |
| Capital acquisitions and debt service           | 129,849   | -                                      | 129,849              | -                   | 129,849                     |
| Workers’ compensation claims                    | 495,000   | -                                      | 495,000              | -                   | 495,000                     |
| Specific operating activities                   | -   | 25,000                                 | 25,000               | -                   | 25,000                      |
| Unrestricted                                    | 21,360,750  | 545,972                                | 21,906,722           | -                   | 21,906,722                  |
|   | <u>44,981,125</u>   | <u>570,972</u>                         | <u>45,552,097</u>    | <u>-</u>            | <u>45,552,097</u>           |
| Total net assets                                |   |  |                      |                     |                             |
|   | <u>44,981,125</u>   | <u>570,972</u>                         | <u>45,552,097</u>    | <u>-</u>            | <u>45,552,097</u>           |
| Total liabilities and net assets                | <u>\$ 55,921,406</u>  | <u>\$ 585,116</u>                      | <u>\$ 56,506,522</u> | <u>\$ -</u>         | <u>\$ 56,506,522</u>        |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Combining Schedule – Balance Sheet Information**  
**June 30, 2010**

|   | <b>McAlester<br/>Regional<br/>Health Center<br/>Authority</b> | <b>Blended<br/>Component<br/>Units</b> | <b>Total</b>         | <b>Eliminations</b> | <b>Combined<br/>Balance</b> |
|---|---|--|----------------------|---------------------|-----------------------------|
| <b>Assets</b>                                 |   |  |                      |                     |                             |
| <b>Current Assets</b>                         |   |  |                      |                     |                             |
| Cash and cash equivalents                     | \$ 6,543,921  | \$ 392,941                             | \$ 6,936,862         | \$ -                | \$ 6,936,862                |
| Short-term investments                        | 1,074,890   | 103,321                                | 1,178,211            | -                   | 1,178,211                   |
| Restricted cash                               | 433,786   | -                                      | 433,786              | -                   | 433,786                     |
| Patient accounts receivable, net of allowance | 11,486,932  | -                                      | 11,486,932           | -                   | 11,486,932                  |
| Estimated amounts due from third-party payers | 585,000   | -                                      | 585,000              | -                   | 585,000                     |
| Supplies                                      | 2,009,574   | 16,803                                 | 2,026,377            | -                   | 2,026,377                   |
| Prepaid expenses and other                    | 1,254,170   | 10,074                                 | 1,264,244            | -                   | 1,264,244                   |
|   | <u>23,388,273</u>   | <u>523,139</u>                         | <u>23,911,412</u>    | <u>-</u>            | <u>23,911,412</u>           |
| Total current assets                          | 23,388,273  | 523,139                                | 23,911,412           | -                   | 23,911,412                  |
| <b>Long-term Investments</b>                  | 2,478,653   | -                                      | 2,478,653            | -                   | 2,478,653                   |
| <b>Capital Assets, Net</b>                    | 29,537,472  | -                                      | 29,537,472           | -                   | 29,537,472                  |
| <b>Investments in Joint Ventures</b>          | 3,692,944   | -                                      | 3,692,944            | -                   | 3,692,944                   |
|   | <u>3,692,944</u>  | <u>-</u>                               | <u>3,692,944</u>     | <u>-</u>            | <u>3,692,944</u>            |
| Total assets                                  | <u>\$ 59,097,342</u>  | <u>\$ 523,139</u>                      | <u>\$ 59,620,481</u> | <u>\$ -</u>         | <u>\$ 59,620,481</u>        |

|   | <b>McAlester<br/>Regional<br/>Health Center<br/>Authority</b> | <b>Blended<br/>Component<br/>Units</b> | <b>Total</b>         | <b>Eliminations</b> | <b>Combined<br/>Balance</b> |
|---|---|--|----------------------|---------------------|-----------------------------|
| <b>Liabilities and Net Assets</b>               |   |  |                      |                     |                             |
| <b>Current Liabilities</b>                      |   |  |                      |                     |                             |
| Current maturities of long-term debt            | \$ 2,613,323  | \$ -                                   | \$ 2,613,323         | \$ -                | \$ 2,613,323                |
| Accounts payable                                | 1,726,000   | -                                      | 1,726,000            | -                   | 1,726,000                   |
| Accrued expenses                                | 3,382,085   | 14,144                                 | 3,396,229            | -                   | 3,396,229                   |
|   | <u>7,721,408</u>  | <u>14,144</u>                          | <u>7,735,552</u>     | <u>-</u>            | <u>7,735,552</u>            |
|   | <u>3,867,631</u>  | <u>-</u>                               | <u>3,867,631</u>     | <u>-</u>            | <u>3,867,631</u>            |
|   | <u>11,589,039</u>   | <u>14,144</u>                          | <u>11,603,183</u>    | <u>-</u>            | <u>11,603,183</u>           |
| <b>Net Assets</b>                               |   |  |                      |                     |                             |
| Invested in capital assets, net of related debt | 22,997,808  | -                                      | 22,997,808           | -                   | 22,997,808                  |
| Restricted – expendable for                     |   |  |                      |                     |                             |
| Capital acquisitions and debt service           | 433,786   | -                                      | 433,786              | -                   | 433,786                     |
| Specific operating activities                   | -   | 25,000                                 | 25,000               | -                   | 25,000                      |
| Unrestricted                                    | 24,076,709  | 483,995                                | 24,560,704           | -                   | 24,560,704                  |
|   | <u>47,508,303</u>   | <u>508,995</u>                         | <u>48,017,298</u>    | <u>-</u>            | <u>48,017,298</u>           |
|   | <u>\$ 59,097,342</u>  | <u>\$ 523,139</u>                      | <u>\$ 59,620,481</u> | <u>\$ -</u>         | <u>\$ 59,620,481</u>        |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Combining Schedule – Statement of Revenues, Expenses and Changes in Net Assets Information**  
**June 30, 2011**

|   | McAlester<br>Regional<br>Health Center<br>Authority | Blended<br>Component<br>Units | Total                | Eliminations | Combined<br>Balance  |
|---|---|-------------------------------|----------------------|--------------|----------------------|
| <b>Operating Revenues</b>   |   |                               |                      |              |                      |
| Net patient service revenue, net of provision for uncollectible accounts  | \$ 73,389,139                                       | \$ -                          | \$ 73,389,139        | \$ -         | \$ 73,389,139        |
| Other   | 3,292,586   | 228,792                       | 3,521,378            | -            | 3,521,378            |
| Total operating revenues  | <u>76,681,725</u>                                   | <u>228,792</u>                | <u>76,910,517</u>    | <u>-</u>     | <u>76,910,517</u>    |
| <b>Operating Expenses</b>   |   |                               |                      |              |                      |
| Salaries and wages  | 31,749,849  | -                             | 31,749,849           | -            | 31,749,849           |
| Employee benefits   | 6,340,892   | -                             | 6,340,892            | -            | 6,340,892            |
| Purchased services and professional fees                                  | 12,239,273  | -                             | 12,239,273           | -            | 12,239,273           |
| Supplies and other expenses   | 25,242,349  | 170,780                       | 25,413,129           | -            | 25,413,129           |
| Depreciation and amortization   | 4,369,383   | -                             | 4,369,383            | -            | 4,369,383            |
| Loss on sale of capital assets  | 148,068   | -                             | 148,068              | -            | 148,068              |
| Total operating expenses  | <u>80,089,814</u>                                   | <u>170,780</u>                | <u>80,260,594</u>    | <u>-</u>     | <u>80,260,594</u>    |
| <b>Operating Income (Loss)</b>  | <u>(3,408,089)</u>                                  | <u>58,012</u>                 | <u>(3,350,077)</u>   | <u>-</u>     | <u>(3,350,077)</u>   |
| <b>Nonoperating Revenues (Expenses)</b>                                   |   |                               |                      |              |                      |
| Gain on investments in joint ventures                                     | 959,306   | -                             | 959,306              | -            | 959,306              |
| Investment income   | 242,516   | 3,965                         | 246,481              | -            | 246,481              |
| Interest expense  | (334,564)   | -                             | (334,564)            | -            | (334,564)            |
| Total nonoperating revenues (expenses)                                    | <u>867,258</u>                                      | <u>3,965</u>                  | <u>871,223</u>       | <u>-</u>     | <u>871,223</u>       |
| <b>Excess (Deficiency) of Revenues over Expenses Before Capital Gifts</b> | (2,540,831)   | 61,977                        | (2,478,854)          | -            | (2,478,854)          |
| <b>Gifts to Purchase Capital Assets and Other Capital Gifts</b>           | <u>13,653</u>                                       | <u>-</u>                      | <u>13,653</u>        | <u>-</u>     | <u>13,653</u>        |
| <b>Change in Net Assets</b>   | (2,527,178)   | 61,977                        | (2,465,201)          | -            | (2,465,201)          |
| <b>Net Assets, Beginning of Year</b>                                      | <u>47,508,303</u>                                   | <u>508,995</u>                | <u>48,017,298</u>    | <u>-</u>     | <u>48,017,298</u>    |
| <b>Net Assets, End of Year</b>  | <u>\$ 44,981,125</u>                                | <u>\$ 570,972</u>             | <u>\$ 45,552,097</u> | <u>\$ -</u>  | <u>\$ 45,552,097</u> |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Combining Schedule – Statement of Revenues, Expenses and Changes in Net Assets Information**  
**June 30, 2010**

|  | <b>McAlester<br/>Regional<br/>Health Center<br/>Authority</b> | <b>Blended<br/>Component<br/>Units</b> | <b>Total</b>         | <b>Eliminations</b> | <b>Combined<br/>Balance</b> |
|--|---|--|----------------------|---------------------|-----------------------------|
| <b>Operating Revenues</b>  |   |  |                      |                     |                             |
| Net patient service revenue, net of provision for uncollectible accounts | \$ 68,431,063   | \$ -                                   | \$ 68,431,063        | \$ -                | \$ 68,431,063               |
| Other  | 3,281,108   | 318,874                                | 3,599,982            | -                   | 3,599,982                   |
| Total operating revenues   | <u>71,712,171</u>   | <u>318,874</u>                         | <u>72,031,045</u>    | <u>-</u>            | <u>72,031,045</u>           |
| <b>Operating Expenses</b>  |   |  |                      |                     |                             |
| Salaries and wages   | 33,086,094  | -                                      | 33,086,094           | -                   | 33,086,094                  |
| Employee benefits  | 7,225,200   | -                                      | 7,225,200            | -                   | 7,225,200                   |
| Purchased services and professional fees                                 | 12,597,780  | -                                      | 12,597,780           | -                   | 12,597,780                  |
| Supplies and other expenses  | 22,974,386  | 337,020                                | 23,311,406           | (96,325)            | 23,215,081                  |
| Depreciation and amortization  | 4,546,063   | -                                      | 4,546,063            | -                   | 4,546,063                   |
| Loss on sale of capital assets   | 216,139   | -                                      | 216,139              | -                   | 216,139                     |
| Total operating expenses   | <u>80,645,662</u>   | <u>337,020</u>                         | <u>80,982,682</u>    | <u>(96,325)</u>     | <u>80,886,357</u>           |
| <b>Operating Income (Loss)</b>   | <u>(8,933,491)</u>  | <u>(18,146)</u>                        | <u>(8,951,637)</u>   | <u>96,325</u>       | <u>(8,855,312)</u>          |
| <b>Nonoperating Revenues (Expenses)</b>                                  |   |  |                      |                     |                             |
| Gain on investments in joint ventures                                    | 987,542   | -                                      | 987,542              | -                   | 987,542                     |
| Investment income  | 262,020   | 5,002                                  | 267,022              | -                   | 267,022                     |
| Interest expense   | (374,377)   | -                                      | (374,377)            | -                   | (374,377)                   |
| Total nonoperating revenues (expenses)                                   | <u>875,185</u>  | <u>5,002</u>                           | <u>880,187</u>       | <u>-</u>            | <u>880,187</u>              |
| <b>Deficiency of Revenues over Expenses Before Capital Gifts</b>         | (8,058,306)   | (13,144)                               | (8,071,450)          | 96,325              | (7,975,125)                 |
| <b>Gifts to Purchase Capital Assets and Other Capital Gifts</b>          | <u>96,325</u>   | <u>-</u>                               | <u>96,325</u>        | <u>(96,325)</u>     | <u>-</u>                    |
| <b>Change in Net Assets</b>  | (7,961,981)   | (13,144)                               | (7,975,125)          | -                   | (7,975,125)                 |
| <b>Net Assets, Beginning of Year</b>                                     | <u>55,470,284</u>   | <u>522,139</u>                         | <u>55,992,423</u>    | <u>-</u>            | <u>55,992,423</u>           |
| <b>Net Assets, End of Year</b>   | <u>\$ 47,508,303</u>  | <u>\$ 508,995</u>                      | <u>\$ 48,017,298</u> | <u>\$ -</u>         | <u>\$ 48,017,298</u>        |

**Independent Accountants' Report on Internal Control over  
Financial Reporting and on Compliance and Other Matters  
Based on an Audit of the Financial Statements Performed in  
Accordance with *Government Auditing Standards***

Board of Trustees  
McAlester Regional Health Center Authority  
McAlester, Oklahoma

We have audited the consolidated financial statements of McAlester Regional Health Center Authority (the Authority) as of and for the year ended June 30, 2011, and have issued our report thereon dated December 15, 2011, which contained an explanatory paragraph regarding omission of required supplementary information. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority'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 was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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 in the accompanying schedule of findings and responses, 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 Authority's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2011-1, 2011-2, 2011-3 and 2011-4 to be material weaknesses.

Board of Trustees  
McAlester Regional Health Center Authority

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Authority'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*.

We noted certain matters that we reported to the Authority's management in a separate letter dated December 15, 2011.

The Authority's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the Authority's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the governing body, management and others within the Authority and is not intended to be and should not be used by anyone other than these specified parties.

*BKD, LLP*

December 15, 2011

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Schedule of Findings and Responses**  
**Year Ended June 30, 2011**

| <b>Reference Number</b> | <b>Finding</b>  |
|-------------------------|---|
| 2011-1                  | <p>Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting.</p> <p>Condition – The accounts payable coordinators have incompatible duties in the purchases, cash disbursements and accounts payable transactions cycle.</p> <p>Context – These employees have the ability to generate a payment with electronic check signature, record accounts payable and checks issued and add or modify vendor setup files in the system.</p> <p>Effect – Potentially material misstatements in the financial statements or material misappropriations of assets due to error or fraud could occur and not be prevented or detected in a timely manner.</p> <p>Cause – Duties in the purchases, cash disbursements and accounts payable transactions cycle are not adequately segregated, and monitoring or other compensating controls are insufficient.</p> <p>Recommendation – Management should periodically evaluate the costs versus the benefits of further segregation of duties or addition of monitoring or other compensating controls and implement those changes it deems appropriate for which benefits are determined to exceed costs.</p> <p>Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will perform the suggested evaluation and make any changes deemed appropriate that are cost beneficial within the next year.</p> |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Schedule of Findings and Responses, continued**  
**Year Ended June 30, 2011**

| <b>Reference Number</b> | <b>Finding</b>   |
|-------------------------|--|
| 2011-2                  | <p>Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting.</p> <p>Condition – The staff accountant has incompatible duties in the payroll transactions cycle.</p> <p>Context – Employee has the ability to input payroll data, such as hours worked, authorize a payroll payment to be paid via electronic funds transfer, record payroll transactions and electronic funds transfers, change direct deposit information and perform other recording and reconciling duties.</p> <p>Effect – Potential material misstatements in the financial statements or material misappropriation of assets due to error or fraud could occur and not be prevented or detected in a timely manner.</p> <p>Cause – Duties in the payroll transactions cycle are not adequately segregated, and monitoring or other compensating controls are insufficient.</p> <p>Recommendation – Management should periodically evaluate the costs versus the benefits of further segregation of duties or addition of monitoring or other compensating controls and implement those changes it deems appropriate for which benefits are determined to exceed costs.</p> <p>Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will perform the suggested evaluation and make any changes deemed appropriate that are cost beneficial within the next year.</p> |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Schedule of Findings and Responses, continued**  
**Year Ended June 30, 2011**

| <b>Reference Number</b> | <b>Finding</b>   |
|-------------------------|--|
| 2011-3                  | <p>Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting.</p> <p>Condition – The patient financial services director has incompatible duties in the patient revenues, cash receipts and accounts receivable transactions cycle.</p> <p>Context – The patient financial services director has the ability to generate a patient bill, provide electronic fund transfer instructions to third-party payers, authorize discounts and adjustments, including bad debt write-offs, and record discounts, adjustments and bad debt write-offs.</p> <p>Effect – Potentially material misstatements in the financial statements or material misappropriations of assets due to error or fraud could occur and not be prevented or detected in a timely manner.</p> <p>Cause – Duties in the patient revenues, cash receipts and accounts receivable transactions cycle are not adequately segregated, and monitoring or other compensating controls are insufficient.</p> <p>Recommendation – Management should periodically evaluate the costs versus the benefits of further segregation of duties or addition of monitoring or other compensating controls and implement those changes it deems appropriate for which benefits are determined to exceed costs.</p> <p>Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will perform the suggested evaluation and make any changes deemed appropriate that are cost beneficial within the next year.</p> |

**McAlester Regional Health Center Authority**  
**A Component Unit of the City of McAlester, Oklahoma**  
**Schedule of Findings and Responses, continued**  
**Year Ended June 30, 2011**

| <b>Reference Number</b> | <b>Finding</b>  |
|-------------------------|---|
| 2011-4                  | <p>Criteria or Specific Requirement – Management is responsible for establishing and maintaining effective internal controls to promote accurate recording and classification of accounting transactions.</p> <p>Condition – Management’s procedures for recording and classifying transactions and procedures for preparing general ledger reconciliations did not prevent inaccurate recording of transactions.</p> <p>Context – Several material journal entries were required to correct misstatements not identified or corrected by management.</p> <p>Effect – Potential material misstatements in the financial statements or material misappropriation of assets due to error or fraud could occur and not be prevented or detected in a timely manner.</p> <p>Cause – Recording and monitoring procedures in the internal control over financial reporting process were not performed correctly.</p> <p>Recommendation – Management should ensure that controls are adequate to properly record accounting entries. Management should also ensure that monthly general ledger reconciliations are completed timely and accurately, and all reconciling items are researched and resolved on a timely basis.</p> <p>Views of Responsible Officials and Planned Corrective Actions – Management concurs with the finding and recommendation. Management will take steps to evaluate the current internal controls over the recording and classification of accounting transactions and prepare accurate monthly reconciliations, including resolving any variances.</p> |