

HAMILTON COUNTY HOSPITAL DISTRICT
Hamilton, Texas

***REPORT ON INTERNAL CONTROL,
COMMUNICATIONS WITH THE
BOARD OF DIRECTORS,
AND SUPPLEMENTAL INFORMATION***

***For the Year Ended
September 30, 2010***

PARRISH • MOODY & FIKES, p.c.
Certified Public Accountants
Waco, Texas



HAMILTON COUNTY HOSPITAL DISTRICT
REPORT ON INTERNAL CONTROL,
COMMUNICATIONS WITH THE BOARD OF DIRECTORS,
AND SUPPLEMENTAL INFORMATION

SEPTEMBER 30, 2010

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Section A

PARRISH • MOODY & FIKES, p.c.

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Board of Directors
Hamilton County Hospital District
Hamilton, Texas

In planning and performing our audit of the financial statements of Hamilton County Hospital District (the "*District*") as of and for the year ended September 30, 2010, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control over financial reporting (internal control) 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 District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all such deficiencies have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

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 combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. These significant deficiencies are summarized following this letter, along with our comments regarding other matters pertaining to the audit.

This communication is intended solely for the information and use of the Board, management, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

PARRISH MOODY & FIKES, p.c.

Waco, Texas
March 8, 2011

We would like to emphasize the nature and scope of this letter and our financial audit. As discussed in the report on the preceding page, it is not designed to provide assurance on the operation of the District's accounting system. It is designed to share things that we encounter in the course of the audit and to provide comments based on our experience with the District and other similar entities.

- *An operational audit is concerned with operational efficiency, i.e., what is the best way to process transactions to achieve desired results. It is often concerned with adequate staffing, etc. An operational audit is often designed to help evaluate the sufficiency of information for making management decisions.*
- *A financial audit is focused on measurement and testing. It is not really concerned with operational efficiency other than that captured in the District's overall bottom line. It is possible to perform a financial audit with a good deal less information than may be necessary to evaluate the departmental performance of the District or to make strategic decisions about its course of business.*

SIGNIFICANT DEFICIENCIES

Bank Reconciliations —

During the audit, we noted that bank statements for the District's accounts were not reconciled to the general ledger on a monthly basis. Most of the problems encountered within the area of cash could be avoided if a proper system of checks and balances is incorporated into the District's procedures. While we did not have significant audit adjustments as a result of the lack of reconciliations, the District's cash position was not accurately reported on a monthly basis. We recommend that all of the bank accounts be reconciled monthly to the general ledger and that all suspicious reconciling items be promptly reported to the Board and investigated.

Accounts Receivable —

Timely Billing - As part of our audit procedures, we selected a sample of accounts receivable patient balances for testing. We noted 10 of 52 accounts were not billed within 30 days of discharge. Because this is a sample, it is reasonable to believe other accounts may also experience a delay in billing. This might result in unnecessary losses.

OTHER MATTERS

Information Technology —

Information technology is an ever evolving discipline which affects the system's integrity and security. We suggest that the District review their policies and procedures to ensure that it addresses the HIPPA recommended password security as follows:

- At least eight characters in length.
- Contain three of the following:
 - Capital
 - Lowercase
 - Number
 - Special Symbol
- Require password rotation every 90 days.
- The last 24 passwords cannot be re-used.
- System password is locked out for at least 30 minutes after four failed attempts.

Compliance Plan —

Compliance is an evolving discipline, and each year the Office of Inspector General (OIG) outlines its areas of concerns. We commend the District for their adoption of a compliance plan; however to be effective, the plan must be followed actively and in accordance with the written policy. Annual training sessions should be conducted to educate employees on compliance. The plan should also be updated periodically to consider new regulations and initiatives and to include all the suggested elements as outlined by the OIG.

Increasing Importance of Charity and Indigent Reporting —

The publishing of the final “meaningful use” regulations for Electronic Health Records (EHR) has placed even greater emphasis on the accuracy of charity and indigent reporting. The EHR incentive payments are based, in some part, on the charity and indigent care provided by a facility.

In order to capture this data, CMS has turned to the updated S-10 Worksheet which will be used in next year's cost report. In order to consider the accuracy of the amounts reported in the S-10 Worksheet, the data, which includes charity care amounts and criteria, can be obtained by the fiscal intermediaries as part of cost report audits.

These audits will be similar to those performed on Medicare bad debts. The focus of these audits will likely be documentation regarding the determination of charity care status based on asset or income tests in accordance with the District policies.

We recommend that the District perform a review of current charity care procedures and documentation to ensure that they are in compliance with both the hospital's policy and related stark and federal regulations. If the data is audited and significant errors are noted, EHR incentive payments could be reduced.

Section B

HAMILTON COUNTY HOSPITAL DISTRICT

COMMUNICATIONS WITH THE BOARD OF DIRECTORS

The following summarizes our communications to the Board of Directors required by professional standards to assist the Board in fulfilling their obligation to oversee the financial reporting and disclosure process for which management is responsible.

<u>Communication Area</u>	<u>Response for the 2010 Audit</u>
Auditor's Responsibilities under Auditing Standards Generally Accepted in the United States of America	<ul style="list-style-type: none">• Financial statements are the responsibility of management. Our audit is designed to enable us to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement. We were not engaged to perform an audit of the internal control over financial reporting.
Significant Accounting Policies	<ul style="list-style-type: none">• Significant accounting policies are described in Note 1 of the financial statements. We have a responsibility to report on appropriateness of initial selection and changes in significant accounting policies as well as application of new accounting and reporting standards. We do not disagree with management's selection of accounting policies.
Auditor's Judgments About the Quality of the Accounting Principles	<ul style="list-style-type: none">• Accounting principles have been consistently applied and adequately disclosed.
Management Judgments and Accounting Estimates	<ul style="list-style-type: none">• We have a responsibility to evaluate the adequacy of the significant estimates. Management judgment is required in formulating estimates. Significant estimates include, among others, allowance for contractual adjustments, collectability of receivables, payroll and other accruals, and other impairment issues.
Significant Audit Adjustments	<ul style="list-style-type: none">• None
Unadjusted Audit Differences	<ul style="list-style-type: none">• None
Other Information in Documents Containing the Audited Financial Statements	<ul style="list-style-type: none">• We considered Management's Discussion and Analysis for consistency with the audited financial statements.
Consultation with Other Accountants	<ul style="list-style-type: none">• None
Disagreements with Management on Financial Accounting and Reporting Matters	<ul style="list-style-type: none">• We are not aware of any matters that require communication.
Major Issues Discussed with Management Prior to Retention	<ul style="list-style-type: none">• We are not aware of any matters that require communication.

HAMILTON COUNTY HOSPITAL DISTRICT

COMMUNICATIONS WITH THE BOARD OF DIRECTORS

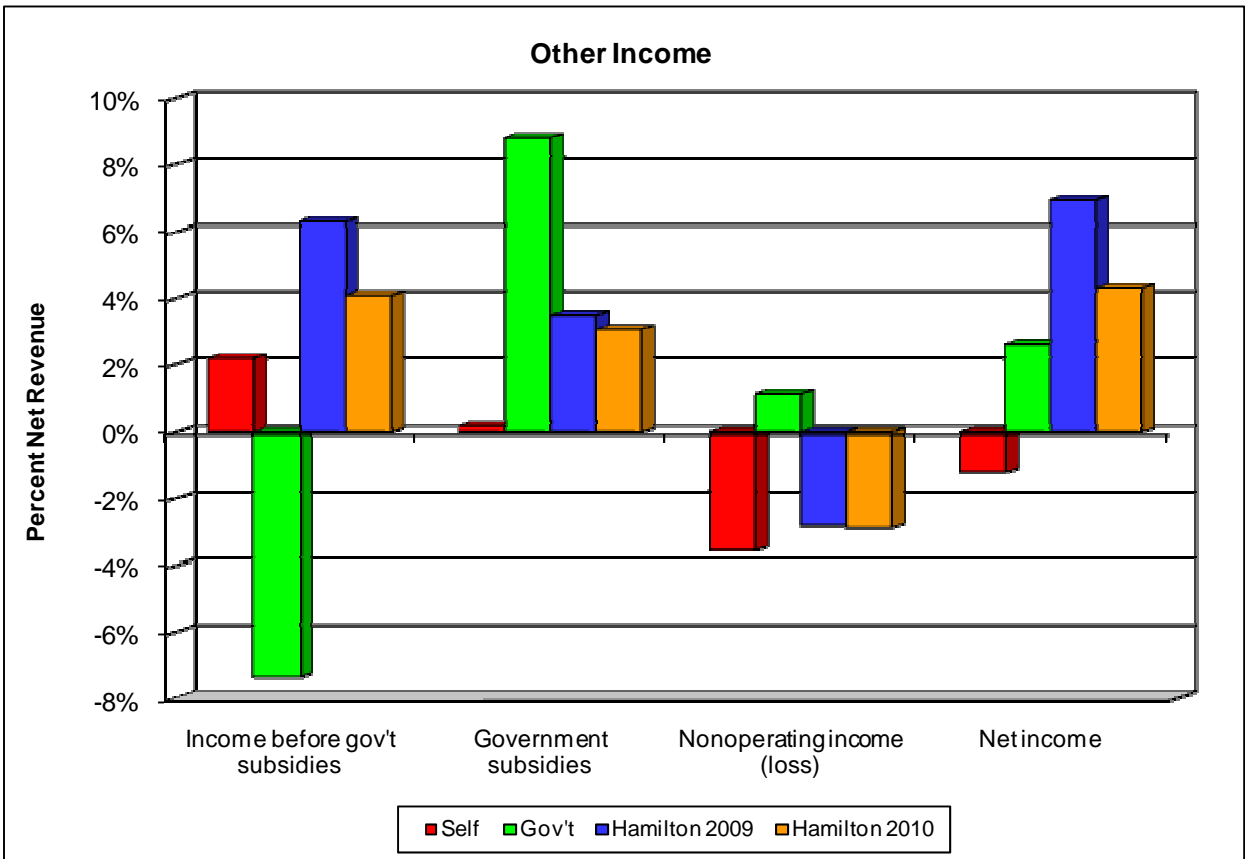
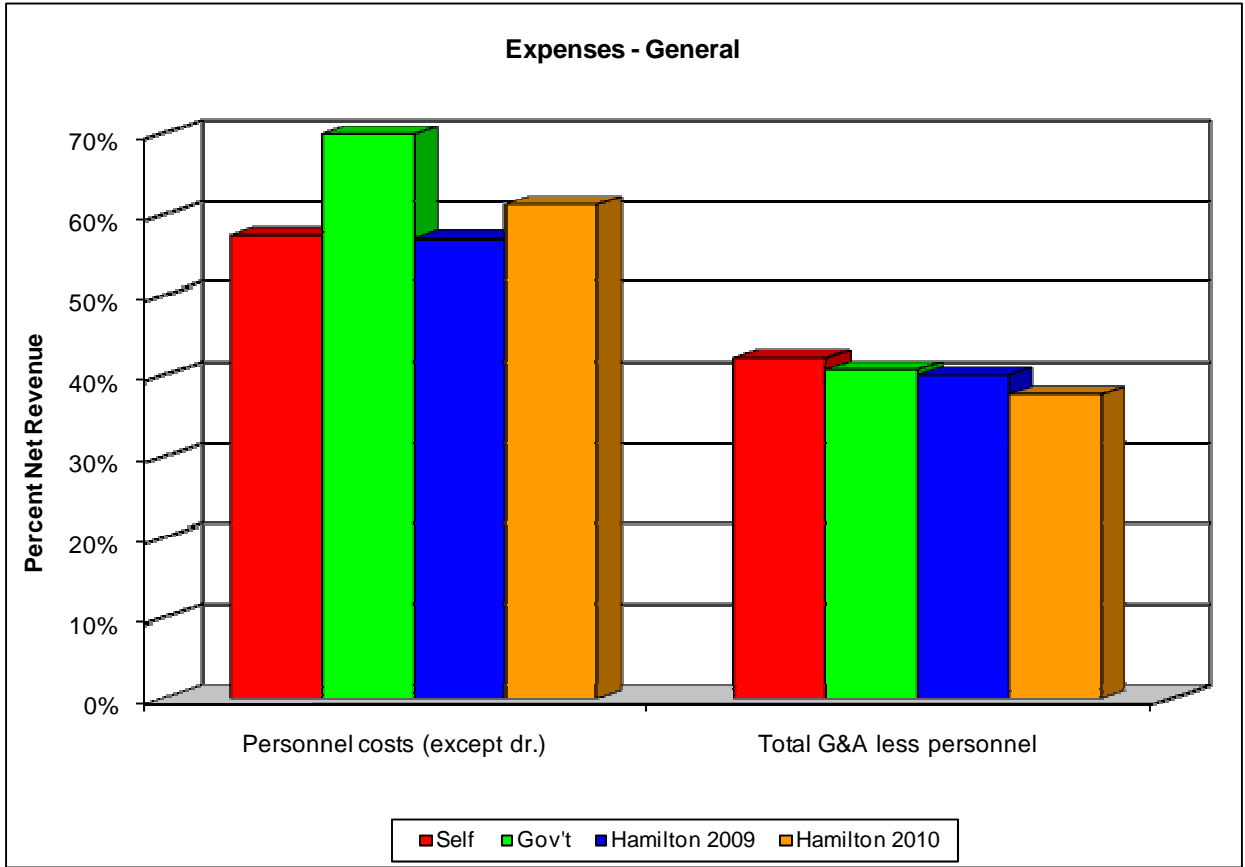
<u>Communication Area</u>	<u>Response for the 2010 Audit</u>
Methods of Accounting for Significant Unusual Transactions, Controversial or Emerging Issues	<ul style="list-style-type: none">• We are not aware of any matters that require communication.
Significant Issues Discussed with Management	<ul style="list-style-type: none">• We are not aware of any matters that require communication.
Serious Difficulties Encountered in Performing the Audit	<ul style="list-style-type: none">• None
Fraud and Illegal Acts	<ul style="list-style-type: none">• We are not aware of any matters that require communication.
Significant Deficiencies and Material Weaknesses in Internal Control	<ul style="list-style-type: none">• We are not aware of any matters which would require communication to the Board other than as included with this report.
Independence	<ul style="list-style-type: none">• We are not aware of any relationships or other matters that, in our professional judgment, may reasonably be thought to bear on our independence. We also confirm that we are independent within the meaning of the applicable published rules and pronouncements, and its interpretations and rulings.

Section C

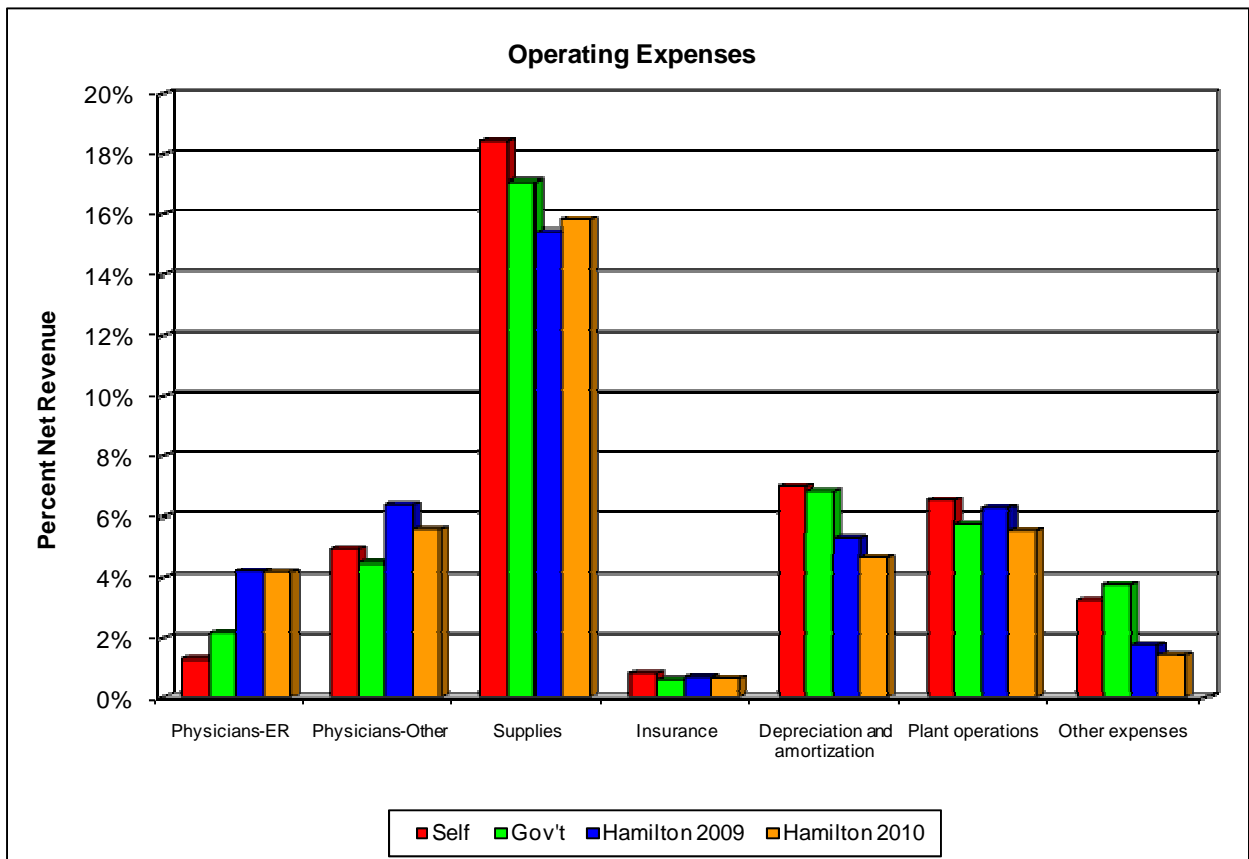
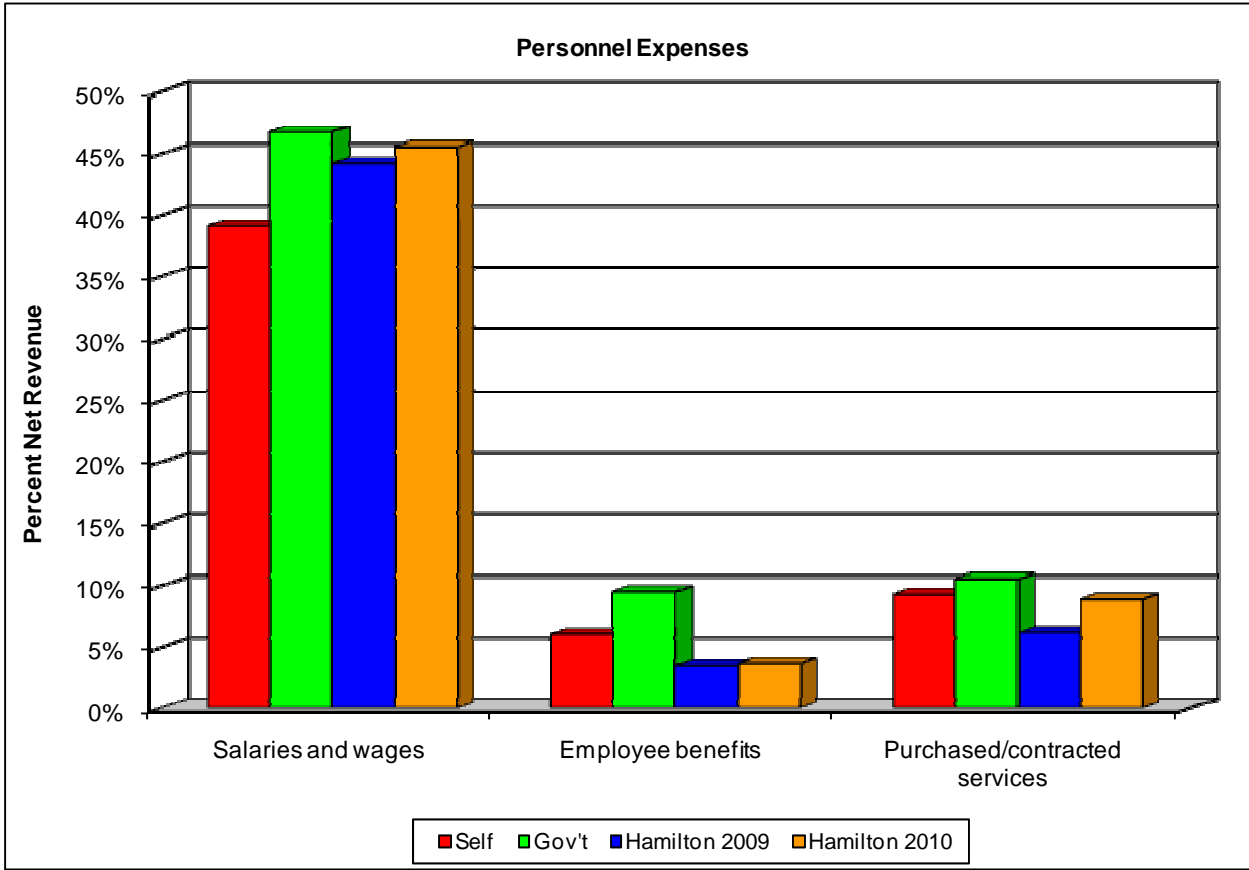
**Hamilton County Hospital District
Supplemental Information
Peer Comparison
For the Years Ended September 30,**

	Self Supporting	Governmental	2009	2010
% of Gross Patient Service Revenues				
Inpatient revenue	38.54 %	43.83 %	36.82 %	37.08 %
Outpatient revenue	57.92 %	51.41 %	51.44 %	47.72 %
Home health revenue	0.65 %	0.86 %	0.00 %	0.00 %
Rural health clinic revenue	2.68 %	3.42 %	11.74 %	15.20 %
Long-term care revenue	0.20 %	0.48 %	0.00 %	0.00 %
Total patient service revenues	<u>100.00 %</u>	<u>100.00 %</u>	<u>100.00 %</u>	<u>100.00 %</u>
Contractual deductions	(34.55)%	(39.31)%	(37.05)%	(35.61)%
Bad debts and uncollected accounts	(6.08)%	(9.10)%	(8.77)%	(8.77)%
Charity care	(3.41)%	(3.53)%	(2.72)%	(1.66)%
Other deductions	(15.64)%	(11.22)%	(13.32)%	(14.92)%
Disproportionate share and other credits	0.56 %	2.41 %	0.78 %	0.41 %
Total deductions from revenues	<u>(59.13)%</u>	<u>(60.74)%</u>	<u>(61.08)%</u>	<u>(60.56)%</u>
Net patient service revenues	<u>40.87 %</u>	<u>39.26 %</u>	<u>38.92 %</u>	<u>39.44 %</u>
% of Net Patient Service Revenues				
Net patient service revenue	100.00 %	100.00 %	100.00 %	100.00 %
Other operating revenue	1.75 %	3.30 %	3.30 %	3.23 %
	<u>101.75 %</u>	<u>103.30 %</u>	<u>103.30 %</u>	<u>103.23 %</u>
Salaries and wages	39.08 %	46.70 %	44.18 %	45.53 %
Employee benefits	6.08 %	9.48 %	3.42 %	3.59 %
Payroll taxes	2.91 %	3.20 %	3.15 %	3.32 %
Purchased/contracted services	9.26 %	10.53 %	6.23 %	8.88 %
Payments to physicians - ER	1.29 %	2.16 %	4.22 %	4.18 %
Payments to physicians - other	4.91 %	4.47 %	6.37 %	5.59 %
Supplies	18.43 %	17.10 %	15.43 %	15.81 %
Education and training	0.23 %	0.28 %	0.24 %	0.16 %
Travel	0.17 %	0.25 %	0.22 %	0.17 %
Telephone and utilities	2.19 %	2.66 %	3.35 %	3.04 %
Maintenance and repairs	2.58 %	2.14 %	1.88 %	1.31 %
Rental expense	1.78 %	0.97 %	1.04 %	1.19 %
Insurance	0.83 %	0.62 %	0.70 %	0.67 %
Legal and professional	0.35 %	0.53 %	0.31 %	0.31 %
Depreciation and amortization	7.02 %	6.85 %	5.30 %	4.63 %
Other expenses	2.46 %	2.71 %	0.96 %	0.77 %
Total operating expenses	<u>99.56 %</u>	<u>110.65 %</u>	<u>97.01 %</u>	<u>99.15 %</u>
Operating income (loss)	2.18 %	(7.34)%	6.29 %	4.08 %
Property taxes and local governmental subsidies	0.20 %	8.83 %	3.46 %	3.09 %
Operating income (loss) after property taxes and local governmental subsidies	<u>2.38 %</u>	<u>1.48 %</u>	<u>9.75 %</u>	<u>7.17 %</u>
Investment income	0.36 %	0.48 %	0.59 %	0.43 %
Interest expense	(3.74)%	(1.59)%	(3.76)%	(3.33)%
Other nonoperating income (loss)	(0.18)%	2.25 %	0.37 %	0.04 %
Nonoperating income (loss)	<u>(3.56)%</u>	<u>1.14 %</u>	<u>(2.80)%</u>	<u>(2.86)%</u>
Increase (decrease) in net assets	<u>(1.18)%</u>	<u>2.62 %</u>	<u>6.95 %</u>	<u>4.31 %</u>

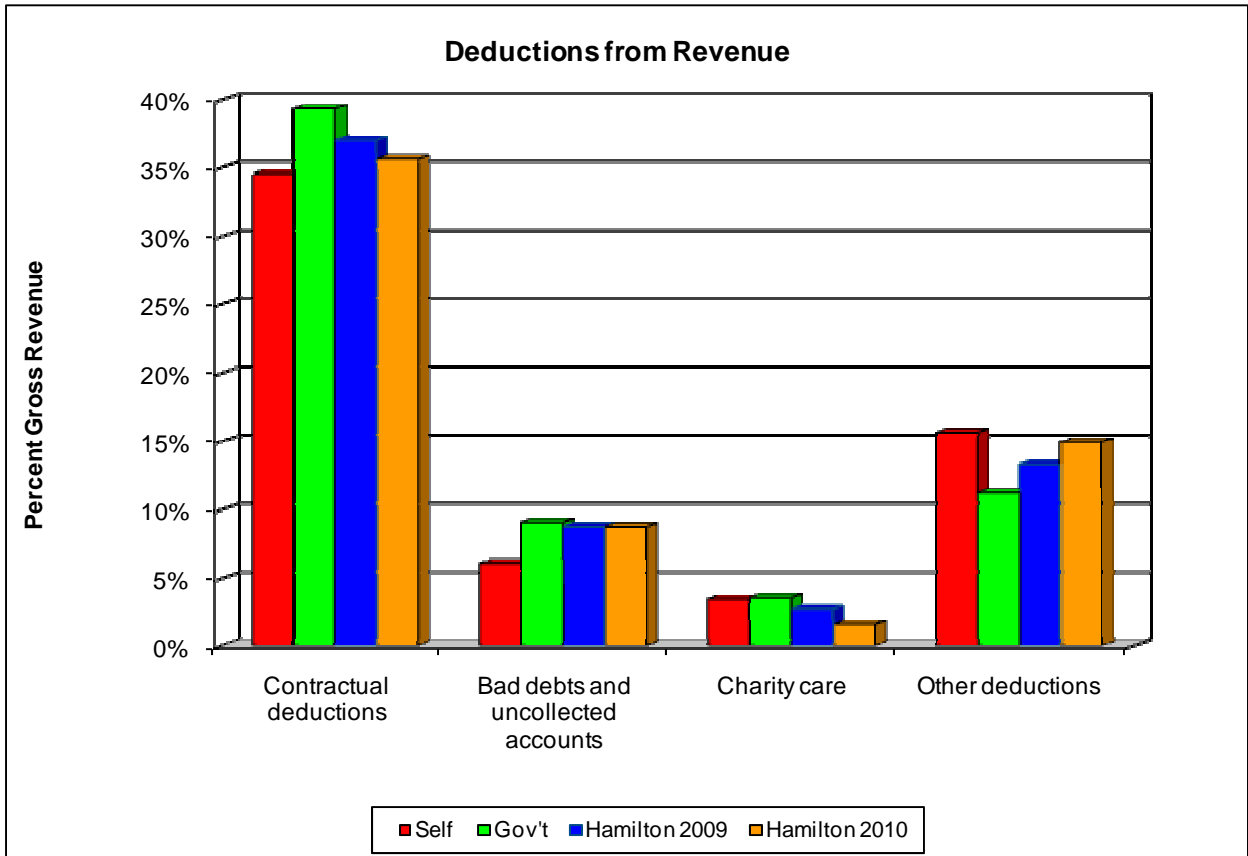
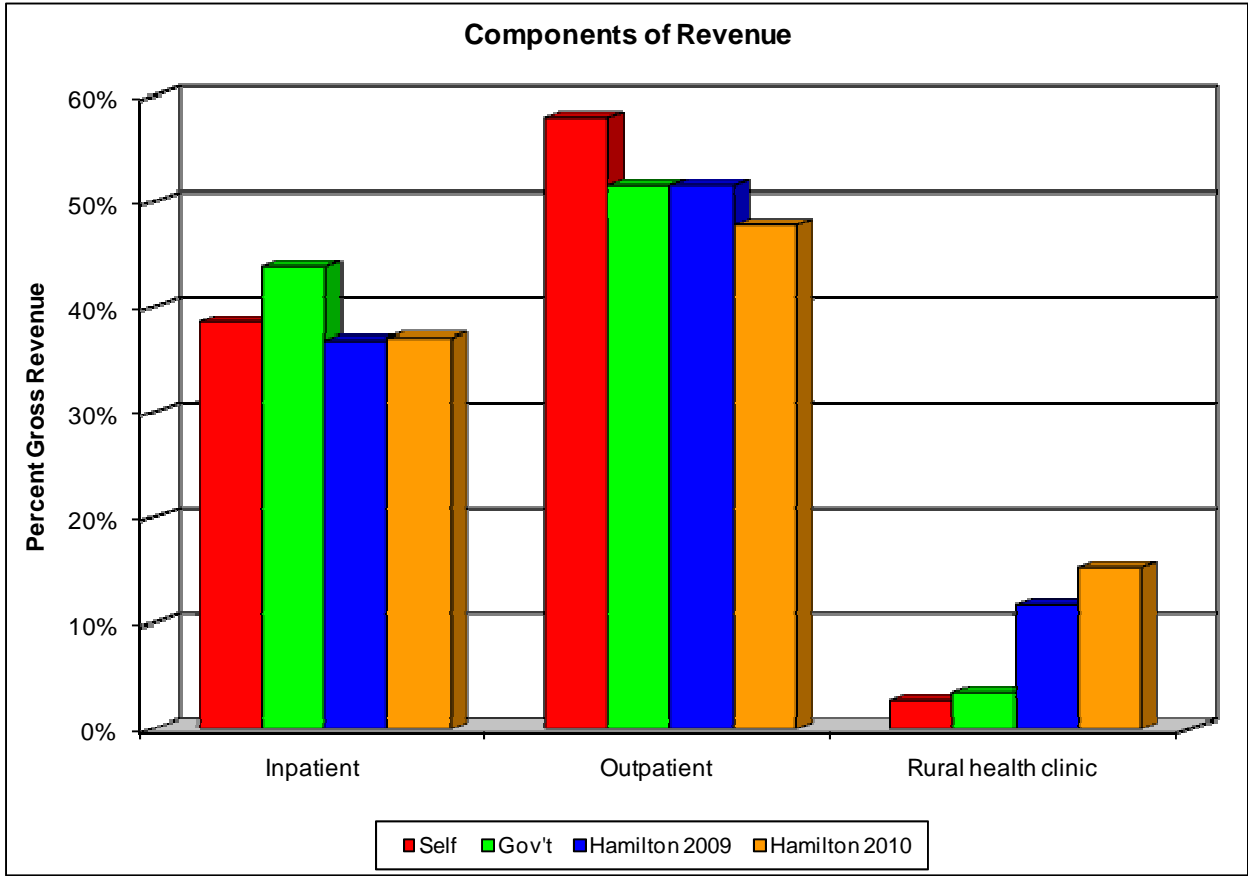
**Hamilton County Hospital District
For the Years Ended September 30,**



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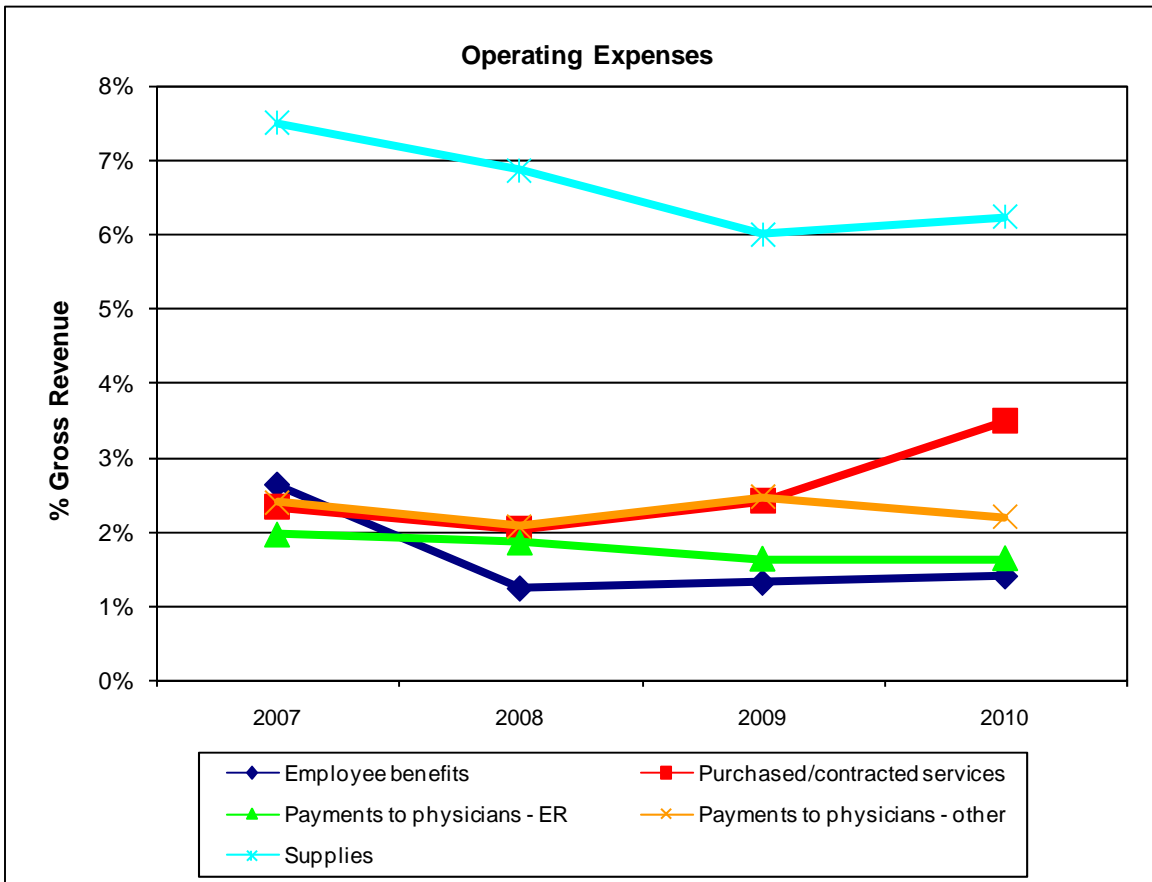
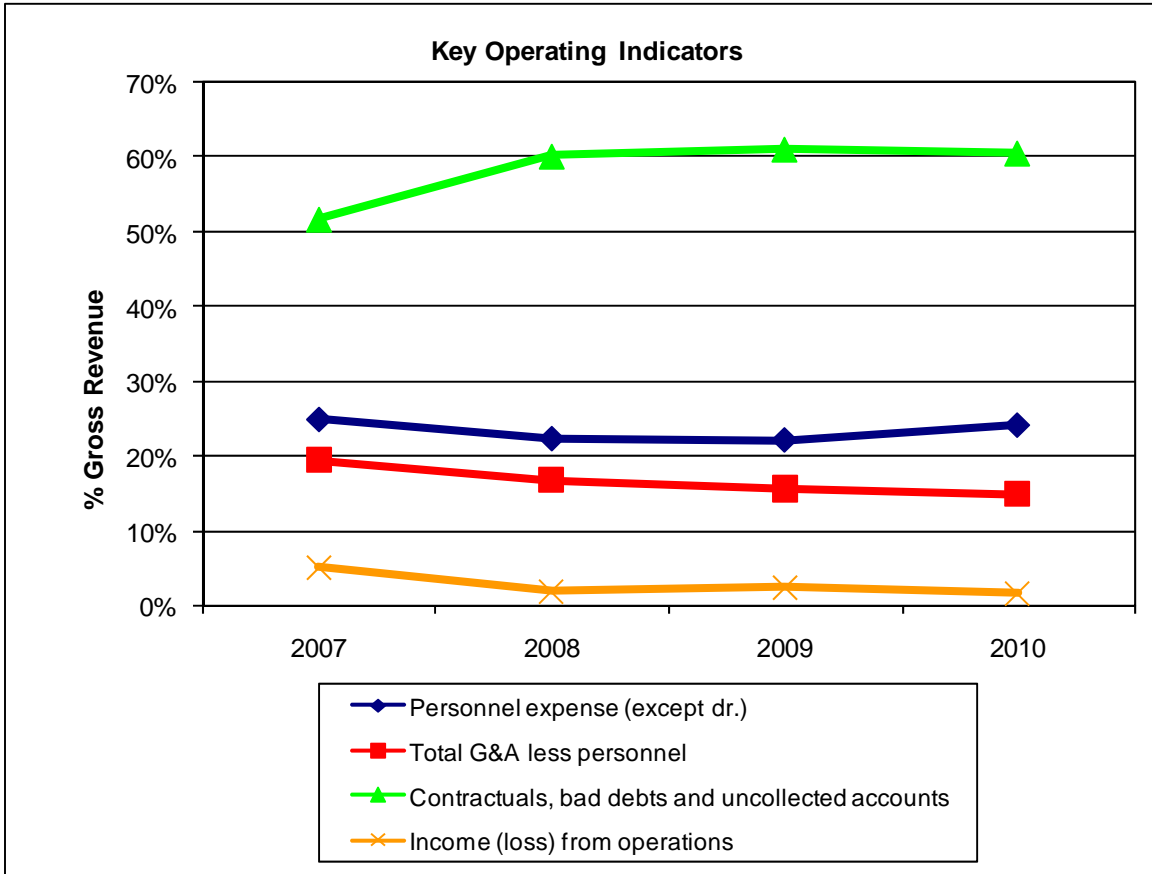


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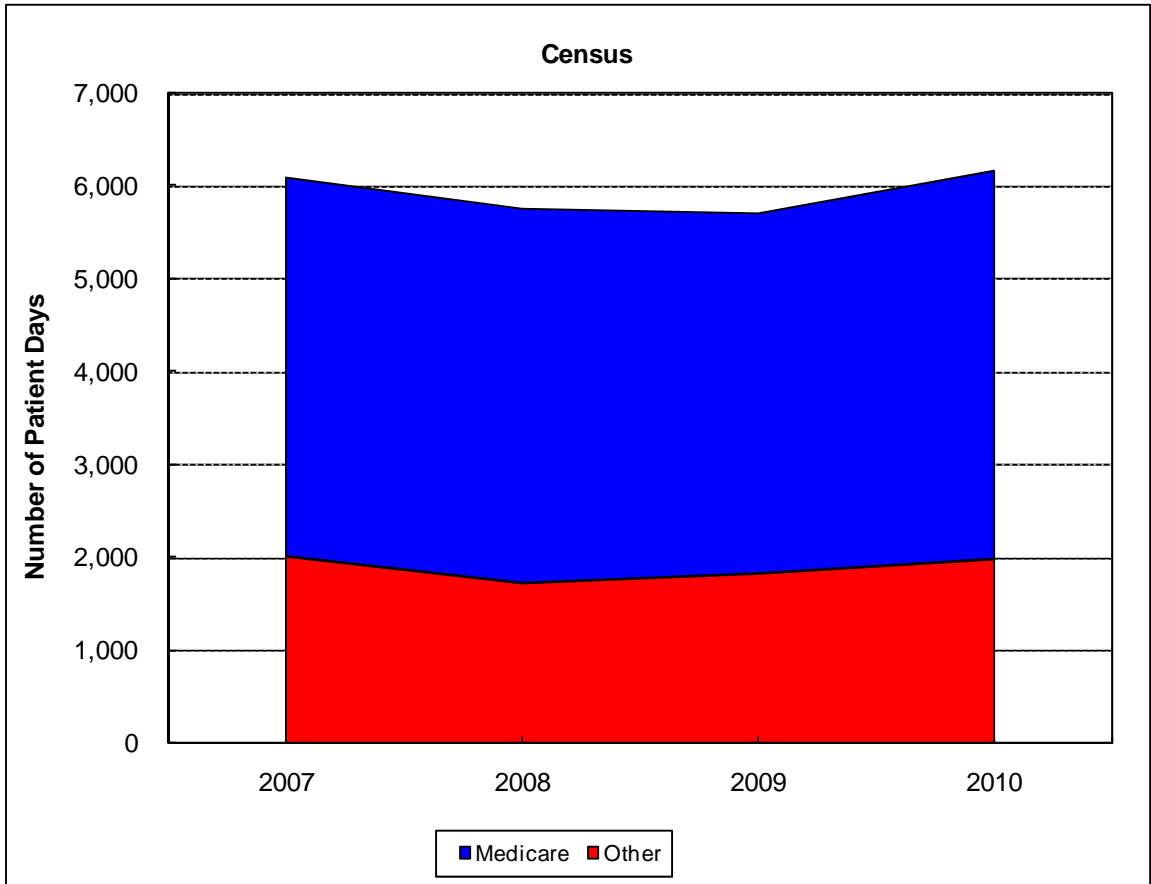
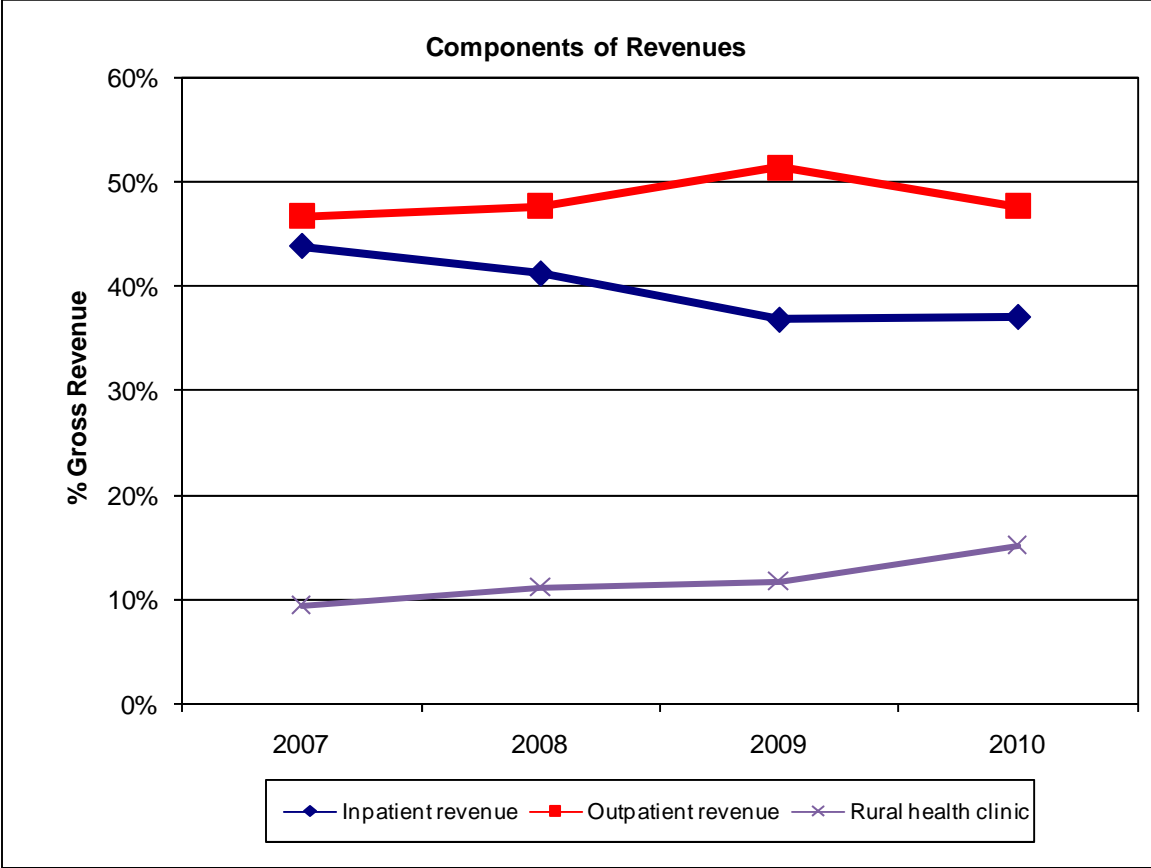


Section D

**Hamilton County Hospital District
For the Years Ended September 30,**



**Hamilton County Hospital District
For the Years Ended September 30,**



**Hamilton County Hospital District
For the Years Ended September 30,**

