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# HOMER MEMORIAL HOSPITAL

TOWN OF HOMER, STATE OF LOUISIANA

HOSPITAL ENTERPRISE FUND

BASIC FINANCIAL STATEMENTS

WITH

MANAGEMENT'S DISCUSSION AND ANALYSIS

AND

INDEPENDENT AUDITORS' REPORT

YEARS ENDED

JUNE 30, 2004, 2003 AND 2002

HOMER MEMORIAL HOSPITAL
TOWN OF HOMER, STATE OF LOUISIANA
HOSPITAL ENTERPRISE FUND
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

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HOMER MEMORIAL HOSPITAL

Management's Discussion and Analysis

This section of Homer Memorial Hospital's (the Hospital) annual financial report presents background information and management's analysis of the Hospital's financial performance during the fiscal year that ended on June 30, 2004. Please read it in conjunction with the financial statements in this report.

## Financial Highlights

- The Hospital's total assets increased by $413,000 or approximately 4%.

- During the fiscal year, the Hospital made significant cash investments in improvements in its physical plant, new equipment, and future expansion plans. Table 2 details these investment activities.

- The Hospital's fiscal 2004 total operating revenue increased by $1,197,000 or 8.15% over fiscal 2003. Total expenses increased $468,000 or 3.16% over the same period. Overall activity at the Hospital, as measured by patient days increased by approximately 2% to 10,941 as compared to 10,745 in the previous year. Average daily census increased 2% to 29.89 as compared to 29.44 in the previous year.

- The Hospital received $672,000 in Medicaid disproportionate share payments during fiscal 2004.

## Required Financial Statements

The basic financial statements of the Hospital report information about the Hospital using Governmental Accounting Standards Board (GASB) accounting principles. These statements offer short-term and long-term financial information about its activities. The Balance Sheets include all of the Hospital's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to Hospital creditors (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of the Hospital and assessing the liquidity and financial flexibility of the Hospital. All of the current year's revenues and expenses are accounted for in the Statements of Revenue, Expenses, and Changes in Net Assets. This statement measures improvements in the Hospital's operations over the past two years and can be used to determine whether the Hospital has been able to recover all of its costs through its patient service revenue and other revenue sources. The final required financial statement is the Statement of Cash Flows. The primary purpose of this statement is to provide information about the Hospital's cash from operations, investing and financing activities, and to provide answers to such questions as where did cash come from, what was cash used for, and what was the change in cash balance during the reporting period.

## Financial Analysis of the Hospital

The Balance Sheet and the Statement of Revenue, Expenses, and Changes in Net Assets report information about the Hospital's activities These two statements report the net assets of the Hospital and changes in them Increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in the health care industry, changes in Medicare and Medicaid regulations, and changes in managed care contracting should also be considered.

Table 1

Condensed Balance Sheets

| | 2004 | 2003 | Dollar Change | Percent Change |
|---|---|---|---|---|
| Total current assets | $ 5,881,412 | $ 5,884,212 | $ (2,800) | -.05% |
| Assets limited as to use (non current) | 1,783,636 | 1,102,058 | 681,578 | 61.85% |
| Property, plant and equipment | 3,072,349 | 3,337,855 | (265,506) | -7.95% |
| Total assets | $10,737,397 | $10,324,125 | $ 413,272 | 4.00% |
| Total current liabilities | $ 934,827 | $ 1,023,665 | $ (88,838) | -8.68% |
| Long-term debt, net of current portion | 2,543,468 | 2,784,378 | (240,910) | -8.65% |
| Total liabilities | 3,478,295 | 3,808,043 | (329,748) | -8.66% |
| Net assets: | | | | |
| Invested in capital assets net of related debt | 2,818,127 | 2,969,500 | (151,373) | -5.10% |
| Restricted net assets | 842,267 | 550,060 | 292,207 | 53.12% |
| Unrestricted net assets | 3,598,708 | 2,996,522 | 602,186 | 20.10% |
| Total net assets | 7,259,102 | 6,516,082 | 743,020 | 11.40% |
| Total liabilities and fund balance | $10,737,397 | $10,324,125 | $ 413,272 | 4.00% |

As can be seen in Table 1, total assets increased by $413,000 to $10,737,000 in fiscal year 2004, up from $10,324,000 in fiscal year 2003. The change in total net assets results primarily from disproportionate share payments received by the Hospital

The Hospital paid cash for all of the acquisitions listed in the table below.

Table 2

| Capital Investments | 2004 Cost |
|---|---|
| New Equipment | |
| Air Conditioning System 4 Air Handlers and 2 Condensers | $ 6,311 |
| Mammography System | 69,600 |
| Steam Sterilizer | 32,850 |
| Computers and Printers | 19,171 |
| Gastroscope, Colonoscope, and Video Processor | 59,050 |
| Insulated Dietary Dishes, Carts and Racks | 9,289 |
| Lab Information System | 38,540 |
| TOTAL NEW EQUIPMENT | 234,811 |
| | |
| Construction / Maintenance | |
| Final Installments on New Roof | 59,122 |
| Drainpipe across Street and Parking Lot | 9,000 |
| TOTAL CONSTRUCTION / MAINTENANCE | 68,122 |
| | |
| Master Planning | |
| Final Payment on Hospital Plans | 9,750 |
| | |
| TOTAL ACQUISITIONS | $312,683 |

## Sources of Revenue

### Operating Revenue

During fiscal year 2004, the Hospital derived the majority of its total revenue from patient service revenue. Patient service revenue includes revenue from the Medicare and Medicaid programs or other third-party payors and patients who receive care in the Hospital's facilities. Reimbursement for the Medicare and Medicaid programs and other third-party payors is based upon established contracts, and the difference between the full charge and payment is recognized as a contractual adjustment. Other revenue includes interest income, cafeteria sales, and other miscellaneous services.

Table 3 represents the relative percentages of volume for patients served by payor for the fiscal years ended June 2004 and 2003. Inpatient (acute and psychiatric), outpatient and home health patients are included in the statistics below.

Table 3

Patients by Financial Class

| | June 2004 | June 2003 |
|---|---|---|
| Medicare | 23.93% | 31.32% |
| Medicaid | 37.10% | 19.53% |
| Insurance | 29.02% | 38.53% |
| Uninsured | 9.95% | 10.62% |
| Total | 100.00% | 100.00% |

**Non-Operating Income**

The Hospital holds designated and restricted funds in its Balance Sheet that are invested primarily in money market funds held at First Guaranty Bank in Public Fund Service Accounts (PFSA). Total investment income earned in the fiscal year ended June 30, 2004 was $55,509.

**Accounts Receivable**

Total Accounts Receivable has increased and the Hospital is taking steps to reduce Accounts Receivable. The Hospital has experienced turnover in the medical records department, but feels that the situation has stabilized.

Table 4

| | June 2004 | June 2003 |
|---|---|---|
| Current Accounts | $ 2,483,082 | $ 1,757,494 |
| 30-day Accounts | 1,097,133 | 941,345 |
| 60-day Accounts | 613,332 | 506,426 |
| 90-day and over Accts | 2,696,848 | 2,085,447 |
| Total | $ 6,890,395 | $ 5,290,712 |

HOMER MEMORIAL HOSPITAL

Management's Discussion and Analysis (continued)

## Income Statement

The following table presents a summary of the Hospital's historical revenues and expenses for each of the fiscal years ended June 30, 2004 and June 30, 2003.

Table 5

Condensed Statements of Revenue, Expenses, and Changes in Net Assets

| | 2004 | 2003 | Dollar Change | Percent Change |
|---|---|---|---|---|
| Revenue | | | | |
| Net patient service revenue | $ 15,885,755 | $ 14,688,559 | $ 1,197,196 | 8.15% |
| Other revenue | 66,103 | 159,414 | (93,311) | -58.53% |
| Total revenue | 15,951,858 | 14,847,973 | 1,103,885 | 7.43% |
| Expenses | | | | |
| Salaries | 5,532,133 | 5,404,381 | 127,752 | 2.36% |
| Benefits and payroll taxes | 1,137,593 | 1,029,158 | 108,435 | 10.54% |
| Supplies and drugs | 3,070,536 | 3,011,461 | 59,075 | 1.96% |
| Professional fees | 1,226,515 | 1,108,275 | 118,240 | 10.67% |
| Other expenses | 1,120,546 | 921,490 | 199,056 | 21.60% |
| Insurance | 328,866 | 403,457 | (74,591) | -18.49% |
| Interest expense | 189,475 | 195,777 | (6,302) | -3.22% |
| Depreciation and amortization | 547,843 | 527,665 | 20,178 | 3.82% |
| Provision for bad debts | 2,110,840 | 2,194,587 | (83,747) | -3.82% |
| Total expenses | 15,264,347 | 14,796,251 | 468,096 | 3.16% |
| Operating income (loss) | 687,511 | 51,722 | 635,789 | 1229.24% |
| Other Income | | | | |
| Investment income | 55,509 | 65,638 | (10,129) | -15.43% |
| Excess (deficit) of revenue over expenses | $ 743,020 | $ 117,360 | $ 625,660 | 533.11% |

## Operating and Financial Performance

The following summarizes the Hospital's Statements of Revenue, Expenses, and Changes in Net Assets between 2004 and 2003:

- Overall activity at the Hospital, as measured by patient days, increased by approximately 2% to 10,941 as compared to 10,745 in the previous year. Average daily census increased 2%, i.e. 29.89 as compared to 29.44 in the previous year.
- Salaries increased by $128,000 or approximately 2.37% over the previous year. Employee benefit expense increased by $108,000 or approximately 10.54%. The increase can be attributed to an increase in the Hospital's employer contribution rate to the retirement system from 8% to 11% of employee wages. The rising cost of skilled labor continues to be a concern for the Hospital The Hospital incurs frequent overtime in an effort to maintain quality care.
- Investment income was $56,000, which is down approximately 15% from the previous year. While the Hospital had more funds deposited, the decline in interest rates negatively impacted investment income.
- Professional fees increased by $118,000 or 10.67%. The Hospital outsourced the management of its Pharmacy department which led to an increase in professional fees. The Hospital's goal is for the management company to reduce overall costs in the pharmacy department.
- Supply and drug cost increased approximately 2% during the year. The management has created an internal staff committee to analyze supply utilization. The Hospital has also acquired an automated pharmaceutical dispensing system which should lead to cost savings in the pharmacy department.

## Contacting the Hospital's Financial Manager

This financial report is designed to provide our citizens, customers, and creditors with a general overview of the Hospital's finances and to demonstrate the Hospital's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact Hospital Administration.

Bobby G. Lester, CPA
John S. Wells, CPA
Robert G. Miller, CPA
Paul A. Delaney, CPA
Mary L. Carroll, CPA

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## Independent Auditors' Report

Board of Commissioners
Homer Memorial Hospital
Homer, Louisiana

We have audited the accompanying basic financial statements of Homer Memorial Hospital (the Hospital), as of and for the years ended June 30, 2004, 2003 and 2002 as listed in the table of contents. These basic financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these basic 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 audits to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Homer Memorial Hospital, as of June 30, 2004, 2003 and 2002 and the results of its operations 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 September 17, 2004, on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such 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 Commissioners
Homer Memorial Hospital
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Management's discussion and analysis on pages "i" through "vi" is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Lester, Miller & Wells

Certified Public Accountants
September 17, 2004

HOMER MEMORIAL HOSPITAL
BALANCE SHEETS
JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| **ASSETS** | | | |
| Current: | | | |
| Cash and cash equivalents (Notes 2 & 3) | $ 87,732 | $ 975,263 | $ 267,491 |
| Short-term investments | 2,035,709 | 1,910,382 | 1,014,011 |
| Receivables, net (Note 5) | 2,098,446 | 1,573,052 | 2,975,358 |
| Assets limited as to use - current (Note 4) | 874,094 | 581,682 | 562,081 |
| Inventories | 444,451 | 450,939 | 473,364 |
| Prepaid expenses | 178,271 | 84,076 | 124,720 |
| Other current assets (Note 6) | 162,709 | 308,818 | 342,473 |
| Total current assets | 5,881,412 | 5,884,212 | 5,759,498 |
| Assets limited as to use - non current (Note 4) | 1,783,636 | 1,102,058 | 1,242,286 |
| Property, plant and equipment, net (Note 7) | 3,072,349 | 3,337,855 | 3,133,028 |
| Total assets | $ 10,737,397 | $ 10,324,125 | $ 10,134,812 |
| **LIABILITIES AND NET ASSETS** | | | |
| Current: | | | |
| Accounts payable | $ 305,406 | $ 286,045 | $ 262,422 |
| Accrued expenses | 392,383 | 503,575 | 519,754 |
| Current portion of long-term debt (Note 8) | 237,038 | 234,045 | 201,751 |
| Total current liabilities | 934,827 | 1,023,665 | 983,927 |
| Long-term debt, net of current portion (Note 8) | 2,543,468 | 2,784,378 | 2,752,163 |
| Total liabilities | 3,478,295 | 3,808,043 | 3,736,090 |
| Net Assets: | | | |
| Invested in capital assets, net of related debt | 2,818,127 | 2,969,500 | 2,945,072 |
| Restricted net assets | 842,267 | 550,060 | 530,662 |
| Unrestricted net assets | 3,598,708 | 2,996,522 | 2,922,988 |
| Total net assets | 7,259,102 | 6,516,082 | 6,398,722 |
| Total liabilities and net assets | $ 10,737,397 | $ 10,324,125 | $ 10,134,812 |

See accompanying notes to financial statements.

HOMER MEMORIAL HOSPITAL
STATEMENTS OF REVENUE, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Revenue: | | | |
| Net patient service revenue (Note 10) | $ 15,885,755 | $ 14,688,559 | $ 13,227,149 |
| Other revenue | 66,103 | 159,414 | 358,298 |
| Total revenue | 15,951,858 | 14,847,973 | 13,585,447 |
| Expenses: | | | |
| Salaries | 5,532,133 | 5,404,381 | 5,011,381 |
| Benefits and payroll taxes | 1,137,593 | 1,029,158 | 897,732 |
| Supplies and drugs | 3,070,536 | 3,011,461 | 2,550,346 |
| Professional fees | 1,226,515 | 1,108,275 | 832,920 |
| Other expenses | 1,120,546 | 921,490 | 850,481 |
| Insurance | 328,866 | 403,457 | 323,524 |
| Interest expense | 189,475 | 195,777 | 185,556 |
| Depreciation and amortization | 547,843 | 527,665 | 499,384 |
| Provision for bad debts | 2,110,840 | 2,194,587 | 3,092,739 |
| Total expenses | 15,264,347 | 14,796,251 | 14,244,063 |
| Operating income (loss) | 687,511 | 51,722 | (658,616) |
| Other income: | | | |
| Investment income | 55,509 | 65,638 | 79,177 |
| Excess (deficit) of revenue over expenses | 743,020 | 117,360 | (579,439) |
| Net assets at beginning of year | 6,516,082 | 6,398,722 | 6,978,161 |
| Net assets at end of year | $ 7,259,102 | $ 6,516,082 | $ 6,398,722 |

See accompanying notes to financial statements.

HOMER MEMORIAL HOSPITAL
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Cash receipts from patients and third-party payors | $ 13,249,521 | $ 13,896,278 | $ 11,572,162 |
| Other receipts from operations | 296,727 | 239,091 | 200,967 |
| Cash payments for other operating expenses | (5,814,809) | (5,358,723) | (4,644,598) |
| Cash payments to employees and for employee-related costs | (6,780,918) | (6,449,718) | (5,784,349) |
| Net cash provided (used) by operating activities | 950,521 | 2,326,928 | 1,344,182 |
| Cash flows from investing activities: | | | |
| Investment income - restricted | -0- | 19,268 | -0- |
| Change in assets whose use is limited | (973,990) | 120,625 | (345,342) |
| Change in investments | (125,327) | (896,371) | (313,292) |
| Net cash provided (used) by investing activities | (1,099,317) | (756,478) | (658,634) |
| Cash flows from capital and related financing activities: | | | |
| Interest expense | (189,475) | (195,045) | (185,556) |
| Proceeds from issuance of long-term debt and notes payable | -0- | 307,771 | -0- |
| Principal payments on long-term debt and notes payable | (237,917) | (243,262) | (198,598) |
| Proceeds from disposal of assets | -0- | 350 | -0- |
| Purchase of property and equipment | (311,343) | (732,492) | (116,144) |
| Net cash provided (used) by capital and related financing activities: | (738,735) | (862,678) | (500,298) |
| Net increase (decrease) in cash and cash equivalents | (887,531) | 707,772 | 185,250 |
| Beginning cash and cash equivalents | 975,263 | 267,491 | 82,241 |
| Ending cash and cash equivalents | $ 87,732 | $ 975,263 | $ 267,491 |

See accompanying notes to financial statements.

HOMER MEMORIAL HOSPITAL
STATEMENTS OF CASH FLOWS (Continued)
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Supplemental disclosure of cash flow information | | | |
| Cash payments for: | | | |
| Interest (net of interest capitalized) | $ 189,475 | $ 195,777 | $ 185,556 |
| Schedule of noncash investing and financing activities | | | |
| Cost of new equipment under capital leases | $ -0- | $ 307,771 | $ -0- |
| New obligations under capital leases | $ -0- | $ 307,771 | $ -0- |
| Reconciliation of income from operations to net cash provided by operating activities: | | | |
| Operating income (loss) | $ 687,511 | $ 51,722 | $ (658,616) |
| Interest expense considered capital financing activity | 189,475 | 195,045 | 185,556 |
| Adjustments to reconcile revenue in excess of expenses to net cash provided by operating activities: | | | |
| Depreciation and amortization | 547,843 | 527,665 | 499,384 |
| (Gain) loss on disposal of asset | 29,006 | (350) | -0- |
| Interest income | 55,509 | 46,371 | 79,177 |
| (Increase) decrease in: | | | |
| Patient accounts receivable, net | (525,394) | 1,402,307 | 1,185,501 |
| Other assets | 58,402 | 96,724 | (213,628) |
| (Increase) decrease in: | | | |
| Accounts payable and accrued expenses | (91,831) | 7,444 | 266,808 |
| Net cash provided by operating activities | $ 950,521 | $ 2,326,928 | $ 1,344,182 |

See accompanying notes to financial statements.

## NOTE 1 - ORGANIZATION AND OPERATIONS

### Legal Organization

Homer Memorial Hospital (the "Hospital") is an enterprise fund of the Town of Homer, Louisiana. The Hospital is controlled by a board of directors, who are a separate and distinct body from the Selectmen of the Town of Homer. The board members consist of citizens appointed by the Mayor and Selectmen of the Town of Homer The board members serve without compensation.

### Nature of Business

The Hospital provides inpatient and outpatient and emergency hospital services, as well as skilled nursing (through "swing beds"), home health, and inpatient psychiatric services to patients from Claiborne and surrounding parishes and counties

## NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Enterprise Fund

Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises - where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

### Basis of Accounting

The Hospital uses the accrual method of accounting. Under Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Activities That Use Proprietary Fund Accounting,* the Hospital has elected not to apply Financial Accounting Standards Board pronouncements issued after November 30, 1989. Hospital accounting and reporting procedures also conform to the requirements of Louisiana Revised Statute 24:514 and to the guide set forth in the Louisiana Governmental Audit Guide, the AICPA, Audit and Accounting Guide - Health Care Organizations, published by the American Institute of Certified Public Accountants, and standards set by the Governmental Accounting Standards Board (GASB), which is the accepted standard setting body for establishing governmental accounting and financial reporting.

On July 1, 2002, the Hospital adopted the provisions of Statement No. 34 (Statement 34) of GASB, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments.* Statement 34 established standards for external financial reporting for all state and local governmental entities, which include a balance sheet, a statement of revenue, expenses, and changes in net assets; and a direct method statement of cash flows. It requires the classification of net assets into three components – invested in capital assets, net of related debt; restricted and unrestricted. These classifications are defined as follows:

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

- Restricted – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

- Unrestricted – This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

The adoption of Statement GASB 34 resulted in the previously reported unrestricted fund balance amount being classified to conform to the above net asset classifications. Additionally, the Hospital restated the 2003 and 2002 restricted and unrestricted net assets to conform to the definitions presented above.

Cash and Cash Equivalents

Cash and cash equivalents consist primarily of deposits in checking and money market accounts and certificates of deposit with original maturities of 90 days or less. Certificates of deposit with original maturities over 90 days are classified as short-term investments. Cash and cash equivalents and short-term investments are stated at cost, which approximates market value. The caption "cash and cash equivalents" does not include amounts whose use is limited or temporary cash investments.

Credit Risk

The District provides medical care primarily to residents of Claiborne and surrounding parishes (counties) and grants credit to those patients, substantially all of whom are local residents.

The Hospital's estimate of collectibility is based on evaluation of historical collections compared to gross charges and an analysis of aged accounts receivable to establish an allowance for uncollectible accounts. Actual results could differ from those estimates.

Significant Concentration of Economic Dependence

The Hospital has an economic dependence on a small number of staff physicians. These physicians admit over 90% of the Hospital's patients. The Hospital also has an economic dependence on Medicare and Medicaid as sources of payments as shown in the table in Note 5. Changes in federal or state legislation or interpretations of rules have a significant impact on the Hospital.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Third-Party Payor Revenues

Contractual agreements with governmental agencies provide for reimbursement based on a fixed price per patient stay based upon the patient's primary diagnosis for Medicare inpatient services, a fixed sixty day price per episode for home health services, and on a fixed price per patient day for Medicaid inpatient services. Medicare & Medicaid outpatient services are reimbursed based upon the lesser of reasonable cost (subject to certain limits) or charges to patients. These reimbursements are subject to audit and retroactive adjustments by each payor. Management has estimated the net revenue based upon historical reimbursement. Actual results could differ from those estimates.

Inventory

Inventories represent dietary and medical supplies on hand and are valued at the latest invoice price, which approximates the lower of cost (first-in, first-out method) or market.

Income Taxes

The Hospital is a political subdivision under the laws of the State of Louisiana, and therefore, it is exempt from federal income tax pursuant to Section 115 of the Internal Revenue Code. Additionally, pursuant to Section 6033(a)(2) it is not required to file an information return form 990.

Property, Plant and Equipment

Property, plant and equipment is recorded at cost for purchased assets or at fair market value on the date of any donation. The Hospital uses the straight-line method of calculating depreciation for financial reporting and third-party reimbursement. The following estimated useful lives are generally used.

| | |
|---|---|
| Building and Improvements | 15 to 40 years |
| Machinery and Equipment | 5 to 20 years |
| Furniture and Fixtures | 5 to 20 years |

Expenditures for additions, major renewals and betterments are capitalized and expenditures for maintenance and repairs are charged to operations as incurred. The Hospital capitalizes depreciable property and equipment valued at $5,000 or more, with a useful life greater than two years.

The cost of assets retired or otherwise disposed of and related accumulated depreciation are eliminated from the accounts in the year of disposal. Gains or losses resulting from property disposals are credited or charged to operations currently.

Pledged Assets

The Hospital's property, plant and equipment is pledged as collateral on the Hospital Revenue Bonds in the original amount of $3,800,000

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue and Expenses

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are included in income or loss from operations; all peripheral transactions are reported as a component of nonoperating income.

Presentation

Certain prior year amounts may have been reclassified in order to be presented comparatively with current year classifications.

NOTE 3 - DEPOSITS AND INVESTMENTS

Included in cash and cash equivalents and assets whose use is limited are cash on hand and deposits with the depository banks for checking accounts and certificates of deposits. At June 30, 2004, 2003, and 2002, all deposits were secured. For all deposits, the market value and carrying value are the same.

Investing is performed in accordance with investment policies complying with state statutes. Funds may be invested in direct obligations of the United States Government and its agencies pledged by its full faith and credit, certificates of deposit and savings accounts which are secured by FDIC or pledge of securities, and government backed mutual or trust funds.

The Hospital's cash and investments are categorized below to give an indication of the level of risk assumed at June 30, 2004, 2003 and 2002. Category (1) includes investments that are insured, or registered in the Hospital's name, or for which the securities are held by the Hospital or its agent in the Hospital's name. Category (2) includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the Hospital's name. Category (3) includes uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent, but not in the Hospital's name. Balances at April 30 were as follows:

| | Credit Risk Category | | | Carrying |
|---|---|---|---|---|
| | (1) | (2) | (3) | Amount |
| 2004 | | | | |
| Investment type: | | | | |
| Direct obligations of or securities backed by the full faith and credit of the U.S. Government | $ -0- | $ -0- | $ -0- | $ -0- |
| Cash and cash equivalents, certificates of deposit | 4,781,171 | -0- | -0- | 4,781,171 |
| Totals | $ 4,781,171 | $ -0- | $ -0- | $ 4,781,171 |

NOTE 3 - DEPOSITS AND INVESTMENTS (Continued)

| | Credit Risk Category | | | Carrying |
|---|---|---|---|---|
| | (1) | (2) | (3) | Amount |
| 2003 | | | | |
| Investment type: | | | | |
| Direct obligations of or securities backed by the full faith and credit of the U.S. Government | $ -0- | $ -0- | $ -0- | $ -0- |
| Cash and cash equivalents, certificates of deposit | 4,569,385 | -0- | -0- | 4,569,385 |
| Totals | $ 4,569,385 | $ -0- | $ -0- | $ 4,569,385 |

| | Credit Risk Category | | | Carrying |
|---|---|---|---|---|
| | (1) | (2) | (3) | Amount |
| 2002 | | | | |
| Investment type: | | | | |
| Direct obligations of or securities backed by the full faith and credit of the U.S. Government | $ -0- | $ -0- | $ -0- | $ -0- |
| Cash and cash equivalents, certificates of deposit | 3,085,869 | -0- | -0- | 3,085,869 |
| Totals | $ 3,085,869 | $ -0- | $ -0- | $ 3,085,869 |

## NOTE 4 - ASSETS LIMITED AS TO USE

The components of assets limited as to use at June 30, is set forth in the following table. Investments are stated at fair value and are comprised primarily of certificates of deposit and money market brokerage accounts.

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Restricted by third parties | | | |
| Bond Sinking fund | $ 28,131 | $ 27,815 | $ 27,411 |
| Bond Reserve fund | 329,095 | 325,394 | 320,668 |
| Bond Contingency fund | 213,512 | 196,851 | 179,772 |
| Self-funded insurance fund | 271,529 | -0- | 2,811 |
| Total restricted by third parties | 842,267 | 550,060 | 530,662 |
| Restricted by Hospital Board | | | |
| Education fund | 89 | 89 | 89 |
| Funded depreciation | 31,738 | 31,533 | 31,330 |
| Long-term investment fund | 935,525 | 925,002 | 911,569 |
| Capital improvement | 93,804 | 177,056 | 330,717 |
| Investment fund #2 | 754,307 | -0- | -0- |
| Total restricted by Hospital Board | 1,815,463 | 1,133,680 | 1,273,705 |
| Total assets limited as to use | 2,657,730 | 1,683,740 | 1,804,367 |
| Less: Current portion | 874,094 | 581,682 | 562,081 |
| Non current assets limited as to use | $ 1,783,636 | $ 1,102,058 | $ 1,242,286 |

## NOTE 5 - ACCOUNTS RECEIVABLE

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Accounts receivable and third-party settlements | | | |
| Net patient accounts receivable | $ 5,346,432 | $ 4,340,409 | $ 4,539,189 |
| Estimated uncollectibles | (2,610,309) | (2,324,765) | (2,164,368) |
| Net accounts receivable | 2,736,123 | 2,015,644 | 2,374,821 |
| Third-party cost based settlements and other receivables | (637,677) | (442,592) | 600,537 |
| Receivables, net | $ 2,098,446 | $ 1,573,052 | $ 2,975,358 |

During the year ended June 30, 2002, management substantially changed its estimates of collectible accounts. If management had calculated the June 30, 2001, allowance using the same method as used in fiscal 2002, the allowance for uncollectibles and bad debt expense would increase by $1,176,000, while net income would decrease by the same amount, for years ending prior to July 1, 2001. Additionally, the loss for fiscal 2002 would have decreased by $1,176,000.

Concentration of credit risks in accounts receivable:

The Hospital is located in Homer, Louisiana. The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors was as follows:

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Medicare | 33% | 29% | 31% |
| Medicaid | 14% | 12% | 13% |
| Other third-party payors | 18% | 17% | 19% |
| Others | 35% | 42% | 37% |
| Total | 100% | 100% | 100% |

## NOTE 6 - OTHER CURRENT ASSETS

Other assets consist of several accounts.

| | | 2004 | | 2003 | | 2002 |
|---|---|---|---|---|---|---|
| Physician loans, net | $ | -0- | $ | 6,357 | $ | 25,000 |
| Education contracts, net | | 162,709 | | 302,461 | | 317,193 |
| Other receivables | | -0- | | -0- | | 280 |
| Total | $ | 162,709 | $ | 308,818 | $ | 342,473 |

### Physician loans

Loans to physicians are secured by notes payable from physicians, including interest charges at market rates. The following allowances are netted against the loan receivables.

| | | 2004 | | 2003 | | 2002 |
|---|---|---|---|---|---|---|
| Allowance for uncollectible loans | $ | 30,000 | $ | 193,303 | $ | 193,303 |

### Educational contracts

The Hospital provided educational assistance to selected medical students and certain employees who contractually agree to return to the Hospital's service area after graduation. Under the terms of these contracts, the Hospital advanced funds to assist the students in their educational costs. Employees agree to repay the loan through extended years of service at the Hospital. Medical students repay the loan by practicing in the Hospital service area for a period of years.

The loans, including interest, become immediately due and payable to the Hospital if the employee or medical student does not provide services for the Hospital for the full period of time within the contract. These loans are classified as current assets in the financial statements. The Board of Directors ended the educational program in 2000. The following is a summary of the net education contracts receivable at June 30.

| | | 2004 | | 2003 | | 2002 |
|---|---|---|---|---|---|---|
| Balance, beginning of year | $ | 302,461 | $ | 317,193 | $ | 357,938 |
| Assessment of interest on balances due | | 2,260 | | 11,807 | | 1,264 |
| Changes in allowance for doubtful collections | | -0- | | 701 | | -0- |
| Cancellation and repayments of contracts | | (140,054) | | (24,022) | | (36,770) |
| Interest paid | | (1,958) | | (3,218) | | (5,239) |
| Balance, end of year | $ | 162,709 | $ | 302,461 | $ | 317,193 |

HOMER MEMORIAL HOSPITAL
NOTES TO THE FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

## NOTE 7 - PROPERTY, PLANT AND EQUIPMENT

The following is a summary of property, plant and equipment and related accumulated depreciation for the year ended June 30, 2004.

| | June 30, 2003 | Additions | Deductions | June 30, 2004 |
|---|---|---|---|---|
| Land and improvements | $ 275,732 | $ 9,000 | $ -0- | $ 284,732 |
| Buildings and improvements | 6,546,936 | 121,573 | 31,065 | 6,637,444 |
| Leasehold improvements | 15,105 | -0- | -0- | 15,105 |
| Equipment | 4,337,476 | 235,611 | 181,164 | 4,391,923 |
| Leased assets | 14,592 | -0- | -0- | 14,592 |
| Construction in progress | 92,401 | 9,750 | 62,451 | 39,700 |
| Total | 11,282,242 | 375,934 | 274,680 | 11,383,496 |
| Accumulated depreciation | (7,944,387) | (547,843) | (181,083) | (8,311,147) |
| Net | $ 3,337,855 | $ (171,909) | $ 93,597 | $ 3,072,349 |

The following is a summary of property, plant and equipment and related accumulated depreciation for the year ended June 30, 2003

| | June 30, 2002 | Additions | Deductions | June 30, 2003 |
|---|---|---|---|---|
| Land and improvements | $ 264,028 | $ 11,704 | $ -0- | $ 275,732 |
| Buildings and improvements | 6,517,756 | 29,180 | -0- | 6,546,936 |
| Leasehold improvements | 15,105 | -0- | -0- | 15,105 |
| Equipment | 4,160,353 | 607,207 | 430,084 | 4,337,476 |
| Leased assets | 14,592 | -0- | -0- | 14,592 |
| Construction in progress | 8,000 | 84,401 | -0- | 92,401 |
| Total | 10,979,834 | 732,492 | 430,084 | 11,282,242 |
| Accumulated depreciation | (7,846,806) | (527,665) | (430,084) | (7,944,387) |
| Net | $ 3,133,028 | $ 204,827 | $ -0- | $ 3,337,855 |

## NOTE 7 - PROPERTY, PLANT AND EQUIPMENT (Continued)

The following is a summary of property, plant and equipment and related accumulated depreciation for the year ended June 30, 2002.

| | June 30, 2001 | Additions | Deductions | June 30, 2002 |
|---|---|---|---|---|
| Land and improvements | $ 234,170 | $ 29,858 | $ -0- | $ 264,028 |
| Buildings and improvements | 6,481,784 | 35,972 | -0- | 6,517,756 |
| Leasehold improvements | 15,105 | -0- | -0- | 15,105 |
| Equipment | 4,118,038 | 71,930 | 29,615 | 4,160,353 |
| Leased assets | 14,592 | -0- | -0- | 14,592 |
| Construction in progress | 1 | 7,999 | -0- | 8,000 |
| Total | 10,863,690 | 145,759 | 29,615 | 10,979,834 |
| Accumulated depreciation | (7,347,422) | (499,384) | -0- | (7,846,806) |
| Net | $ 3,516,268 | $ (353,625) | $ 29,615 | $ 3,133,028 |

## NOTE 8 - LONG-TERM DEBT

A summary of long-term debt and capital lease obligations at June 30 follows:

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| 6.125% 1988 Hospital revenue bonds, principal maturing in varying annual amounts due June 15, 2018, collateralized by a pledge of the Hospital's land, buildings, and equipment | $ 2,526,284 | $ 2,650,068 | $ 2,765,958 |
| Capital lease obligations, at varying rates of imputed interest, collateralized by leased equipment with a cost of $711,761 and book value of $378,884 at June 30, 2004 | 254,222 | 368,355 | 187,956 |
| Total debt | 2,780,506 | 3,018,423 | 2,953,914 |
| Less: Current portion | (237,038) | (234,045) | (201,751) |
| Debt less current portion | $ 2,543,468 | $ 2,784,378 | $ 2,752,163 |

NOTE 8 - LONG-TERM DEBT (Continued)

A summary of long-term debt and capital lease obligations over the next five years are as follows:

| Year Ending June 30, | Bond Debt Service | Long-Term Debt | Capital Lease Obligations |
|---|---|---|---|
| 2005 | $ 283,290 | $ 132,267 | $ 119,913 |
| 2006 | 283,290 | 140,599 | 81,656 |
| 2007 | 283,290 | 149,457 | 73,028 |
| 2008 | 283,290 | 158,873 | 6,086 |
| 2009 | 283,290 | 168,881 | -0- |
| *Thereafter* | 2,242,931 | 1,776,207 | -0- |
| Total | $ 3,659,381 | $ 2,526,284 | 280,683 |
| Less amount representing interest under capital lease obligations | | | (26,461) |
| Capital lease obligation less amount representing interest | | | $ 254,222 |

The revenue bond indenture requires the Hospital to establish and maintain certain funds for the benefit of the bondholder, Farmers Home Administration. The funding requirements are as follows:

Sinking fund requirements - The Hospital is required to make monthly deposits of $23,608. In June 1991, the Hospital began paying the debt in monthly installments in lieu of establishing a sinking fund. Accordingly, a sinking fund is not reflected in the financial statements.

Reserve fund requirements - The Hospital is required to make monthly deposits of $2,361 until the fund has accumulated $320,668. The Hospital met this requirement at June 30, 2004.

Contingency fund requirements - The Hospital is required to make monthly deposits of $1,194. The Hospital met this requirement at June 30, 2004.

NOTE 9 - OPERATING LEASES

Leases that do not meet the criteria for capitalization are classified as operating leases with related rental charged to operations as incurred. The following is a schedule by year of future minimum lease payments under operating leases as of June 30, 2004, that have initial or remaining lease terms in excess of one year.

NOTE 9 - OPERATING LEASES (Continued)

| Year Ending June 30 | | Amount |
|---|---|---|
| 2005 | $ | 79,084 |
| 2006 | | 78,384 |
| 2007 | | 78,384 |
| 2008 | | 78,384 |
| 2009 | | -0- |
| Total minimum lease payments | $ | 314,236 |

NOTE 10 - NET PATIENT SERVICE REVENUE

Inpatient acute care services rendered to Medicare beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient nonacute services, certain outpatient services, and defined capital and medical education costs related to beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost after submission of annual cost reports by the Hospital and audits thereof by the fiscal intermediary. The Hospital's classification of patients under these programs and the appropriateness of their admission are subject to an independent review organization under contract with the Hospital.

Inpatient acute care services rendered to Medicaid program recipients are paid at prospectively determined rates on a per diem basis. Costs incurred on services rendered to Medicaid inpatients, which exceed the prospectively determined payment rates, are not recoverable from the Medicaid program or its beneficiaries. Outpatient services are reimbursed under a cost reimbursement methodology. The Hospital is reimbursed at a tentative rate during the fiscal year. The fiscal intermediary may adjust these rates during the fiscal year. Final settlement is determined after submission of annual cost reports by the Hospital and audits thereof by the Medicaid fiscal intermediary.

Prior to July 1, 1998, the home health department was reimbursed the lower of cost caps or actual cost per visit by Medicare. Effective July 1, 1998, reimbursement was changed to the interim payment system (IPS) as part of a long-term plan adopted by the Centers for Medicare and Medicaid Services (CMS) to pay for these services on a prospective basis (PPS).

Effective July 1, 1999, the IPS system reimbursement caps per unit of unduplicated census was changed again. The new reimbursement amount will be based upon two-thirds of the agency specific amount, and one-third of the national median amount As of October 1, 2000, home health is paid under a PPS method.

NOTE 10 - NET PATIENT SERVICE REVENUE (Continued)

CMS moved virtually all outpatient services to a PPS method in August 2000, with a "hold harmless" provision for small rural hospitals, which provides for reimbursement of approximately 88% of the Hospital's cost of treating Medicare outpatients. The hold harmless provision currently expires December 31, 2005, and provided $58,070, $90,538 and $66,349 income in the fiscal years ended in 2004, 2003 and 2002, respectively.

The Hospital has also entered into agreements with certain commercial insurance carriers, health maintenance organizations, etc. The future impact of these changes is dependent upon interpretation of new regulations, patient acuity and treatment patterns and has not been fully estimated. The basis for payment to the Hospital under these various agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

The Hospital's previous reimbursements are also subject to review by federal authorities. These authorities have several initiatives in progress. No material liabilities have been identified to date under these review programs; however, the potential exists for future claims. These will be recognized in the year the amounts are determined, if any.

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy, the estimated cost of those services and supplies, and equivalent service statistics.

Additionally, the Hospital foregoes charges relating to Medicare, Medicaid and other third-party payors. Following is a schedule of patient service revenue at established rates and charges foregone for the years ended June 30:

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Gross patient service charges | $ 30,668,212 | $ 28,149,656 | $ 22,136,669 |
| Medicaid uncompensated care (UCC) | 733,214 | 675,018 | 587,205 |
| Medicare and Medicaid, without UCC | (13,235,358) | (11,842,652) | (7,896,747) |
| Other third-party payors | (2,204,257) | (2,205,769) | (1,461,389) |
| Charity care | (76,056) | (87,694) | (138,589) |
| | $ 15,885,755 | $ 14,688,559 | $ 13,227,149 |

NOTE 11 - EMPLOYEE BENEFITS

Compensated Absences - As of June 30, 2004, 2003 and 2002, the Hospital has accrued a compensated absence liability of $125,862, $142,840 and $215,834, respectively. The Hospital does pay accrued vacation absences upon termination, if proper notice and termination procedures are followed.

NOTE 12 - PENSION PLAN

All full-time Hospital employees participate in the Municipal Employees' Retirement System, State of Louisiana ("System"), a multiple employer public employee retirement system, (PERS). The payroll for Hospital employees covered by the System for the years ended June 30, 2004, 2003 and 2002, was approximately $4,204,000, $3,719,000 and $3,402,000, respectively; the Hospital's total payroll was approximately $5,532,000, $5,404,000 and $5,011,000 for the years ended June 30, 2004, 2003 and 2002, respectively.

Membership is mandatory as a condition of employment beginning on the date employed if the employee is on a permanent basis working at least thirty-five hours per week, not participating in another publicly funded retirement system, and under the age of sixty at the date of employment.

The System is comprised of two plans. "Plan A" combines the original plan and a supplemental plan, while "Plan B" involves only the original plan. Any member of Plan A can retire provided he/she is age fifty-five with twenty-five years of creditable service, is age sixty with a minimum of ten years of creditable service or at any age with thirty or more years of creditable service. A member of Plan B can retire provided he/she is age fifty-five with thirty years of creditable service or is age sixty with a minimum of ten years of creditable service.

In lieu of terminating employment and accepting a service retirement allowance, any member of Plan A or B, with thirty years of service at age fifty-five; twenty years of service at age sixty; fifteen years of service at age sixty-two; or ten years of service at age sixty-five, may elect to participate in the deferred retirement option plan (DROP) for up to two years and defer the receipt of benefits. Upon commencement of participation in the DROP plan, membership in the System terminates.

During participation in the plan, employer contributions are payable but employee contributions cease. The monthly retirement benefits that would have been payable, had the person elected to cease employment and receive a service retirement allowance are paid into the DROP fund. This fund does not earn interest. In addition, no cost of living increases are payable to participants until employment which made them eligible to become members in the System has been terminated for at least one full year.

Upon termination of employment prior to or at the end of the specified period of participation, a participant in the plan may receive, at his option, a lump sum from the account equal to the payment into the account, a true annuity based upon his actual balance in that fund, or any other method of payment if approved by the board of trustees. The monthly benefits that were being paid into the deferred retirement option plan fund will begin to be paid to the retiree. If a participant dies during the participation in the plan, a lump sum equal to his account balance in the plan fund shall be paid to his named beneficiary or, if none, to his estate. If employment is not terminated at the end of the two years, payments into the plan fund cease and the person resumes active contributing membership in the System. Additional accrued benefits are based on final average compensation used to calculate the member's original benefit unless the additional period of service is at lease thirty-six months.

NOTE 12 - PENSION PLAN (Continued)

Generally, the monthly amount of retirement allowance for any member of Plan A or Plan B shall consist of an amount equal to three percent or two percent, respectively, of the member's final compensation multiplied by his/her years of creditable service. However, under certain conditions as outlined in the statutes, the benefits are limited to specified amounts. Both plans provide for death and disability benefits. Benefits and employer/employee obligations to contribute are established by state statute.

Each participating employer of Plan A contributes an amount equal to 11% of each and every member's earnings. Each employee in Plan A contributes 9.25% of monthly earnings. Under Plan B, each participating employer contributes an amount equal to 7.5% of each and every member's earnings. Each employee in Plan B contributes 5% of monthly earnings.

The System also receives 1/4 of 1% of ad valorem taxes collected within the parishes of Louisiana, except for Orleans Parish.

Tax monies are apportioned between Plan A and Plan B in proportion to the salaries of plan participants. These additional sources of income are used as additional employer contributions. The remaining employer contributions are determined according to actuarial requirements and are set annually. The contribution requirement for the years ended June 30, 2004, 2003, and 2002, was approximately $855,000, $642,000 and $552,000, respectively, which consisted of $466,000, $298,000 and $238,000, respectively, from the Hospital and $389,000, $344,000 and $314,000, respectively, from the employees during 2004, 2003, and 2002.

The "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted to the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the System's funding status on a going concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among PERS and employees. The System does not make separate measurement of assets and pension benefits obligation for individual employers. The pension benefit obligation at June 30, 2003, (the latest actuarial report furnished to the Hospital), for the System as a whole, determined through an actuarial valuation performed as of that date (valued at market) was approximately $614 million. The System's net assets available for benefits on that date (valued at market) was approximately $529 million, with an unfunded pension benefit obligation of $75 million. The Hospital's contributions for the years ended June 30, 2004, 2003, and 2002, represented approximately 3% of total contributions paid by all participating entities respectively. Five-year historical trend information showing the System's progress in accumulating sufficient assets to pay benefits when due is presented in the System's annual financial report. No securities of the Hospital are held by the System.

## NOTE 13 - CONTINGENCIES

The Hospital evaluates contingencies based upon the best available evidence. The Hospital believes that no allowances for loss contingencies are considered necessary. To the extent that resolution of contingencies results in amounts which vary from the Hospital's estimates, future earnings will be charged or credited.

The principal contingencies are described below:

Governmental Third-Party Reimbursement Programs (Note 2) - The Hospital is contingently liable for retroactive adjustments made by the Medicare and Medicaid programs as the result of their examinations as well as retroactive changes in interpretations applying statutes, regulations and general instructions of those programs. The amount of such adjustments cannot be determined.

Further, in order to continue receiving reimbursement from the Medicare programs, the Hospital entered into an agreement with a government agent allowing the agent access to the Hospital's Medicare patient medical records for purposes of making medical necessity and appropriate level of care determination. The agent has the ability to deny reimbursement for Medicare patient claims which have already been paid to the Hospital.

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as privacy, licensure, accreditation, government healthcare program participating requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Hospital is in compliance with fraud and abuse statutes as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

Professional and General Liability Risk – Effective for claims filed after May 1, 2004, the Hospital discontinued professional and general liability insurance coverage through the Louisiana Hospital Association Trust Fund. The Hospital continues to participate in the Louisiana Patient's Compensation Fund ("PCF") established by the State of Louisiana to provide medical professional liability coverage to health care providers. The PCF provides for $400,000 in coverage for actual claims (attorney fees are not covered and must be incurred fully) per occurrence above the first $100,000 per occurrence for which the Hospital is at risk. The PCF places no limitation on the number of occurrences covered. In connection with the establishment of the Patient's Compensation Fund, the State of Louisiana enacted legislation limiting the amount of healthcare provider settlement for professional liability to $100,000 per occurrence and limited the PCF's exposure to $400,000 per occurrence.

NOTE 13 - CONTINGENCIES (Continued)

The Hospital is unaware of and included no provision for professional liability losses not covered by the Louisiana Patient's Compensation Fund. The Hospital is contingently liable for losses and related defense costs from professional liability not underwritten by the Louisiana Patient's Compensation Fund.

The Hospital is unaware of and included no provision for uninsured general liability losses. The Hospital is contingently liable for losses and related defense costs from general liability.

SUPPLEMENTARY INFORMATION

HOMER MEMORIAL HOSPITAL
SCHEDULES OF NET PATIENT SERVICE REVENUE
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Routine services: | | | |
| Adult and pediatric | $ 4,410,627 | $ 4,418,185 | $ 3,669,120 |
| Intensive care unit | 774,070 | 769,250 | 670,650 |
| Senior care | 1,403,174 | 1,229,362 | 1,322,589 |
| Nursery | 12,600 | 14,400 | 26,200 |
| Swing bed | 242,820 | 188,955 | 132,900 |
| Total routine services | 6,843,291 | 6,620,152 | 5,821,459 |
| Other professional services: | | | |
| Operating room | | | |
| Inpatient | 239,764 | 262,924 | 225,098 |
| Outpatient | 361,319 | 387,153 | 273,264 |
| Total | 601,083 | 650,077 | 498,362 |
| Anesthesia | | | |
| Inpatient | 732 | -0- | -0- |
| Outpatient | -0- | -0- | -0- |
| Total | 732 | -0- | -0- |
| Radiology | | | |
| Inpatient | 1,857,991 | 1,631,110 | 1,096,822 |
| Outpatient | 3,434,856 | 2,685,408 | 2,032,506 |
| Total | 5,292,847 | 4,316,518 | 3,129,328 |
| Laboratory | | | |
| Inpatient | 1,806,600 | 1,612,329 | 1,353,925 |
| Outpatient | 1,158,383 | 1,089,496 | 847,390 |
| Total | 2,964,983 | 2,701,825 | 2,201,315 |
| Blood | | | |
| Inpatient | 99,810 | 98,409 | 74,374 |
| Outpatient | 22,496 | 18,966 | 9,241 |
| Total | $ 122,306 | $ 117,375 | $ 83,615 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF NET PATIENT SERVICE REVENUE (Continued)
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Respiratory therapy | | | |
| Inpatient | $ 2,335,645 | $ 1,995,437 | $ 1,490,094 |
| Outpatient | 163,410 | 158,054 | 137,971 |
| Total | 2,499,055 | 2,153,491 | 1,628,065 |
| Physical therapy | | | |
| Inpatient | 32,211 | 50,879 | 33,822 |
| Outpatient | 425 | 178 | 560 |
| Total | 32,636 | 51,057 | 34,382 |
| Occupational therapy | | | |
| Inpatient | 1,140 | 1,148 | 114 |
| Outpatient | -0- | -0- | -0- |
| Total | 1,140 | 1,148 | 114 |
| Electrocardiology | | | |
| Inpatient | 196 | 67 | 242 |
| Outpatient | 15,580 | 53,775 | 40,547 |
| Total | 15,776 | 53,842 | 40,789 |
| Central supply | | | |
| Inpatient | 1,475,084 | 1,398,237 | 1,185,826 |
| Outpatient | 537,436 | 535,396 | 412,487 |
| Total | 2,012,520 | 1,933,633 | 1,598,313 |
| Pharmacy | | | |
| Inpatient | 6,165,375 | 5,764,860 | 3,974,114 |
| Outpatient | 1,171,953 | 1,064,747 | 939,196 |
| Total | $ 7,337,328 | $ 6,829,607 | $ 4,913,310 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF NET PATIENT SERVICE REVENUE (Continued)
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Emergency room | | | |
| Inpatient | $ 376,014 | $ 374,961 | $ 219,972 |
| Outpatient | 1,990,339 | 1,708,703 | 1,503,679 |
| Total | 2,366,353 | 2,083,664 | 1,723,651 |
| Neurology | | | |
| Inpatient | 5,315 | 10,556 | 2,702 |
| Outpatient | 126,347 | 156,211 | 52,564 |
| Total | 131,662 | 166,767 | 55,266 |
| Home health | | | |
| Skilled nursing visits | 278,600 | 294,500 | 270,700 |
| Physical therapy visits | 63,500 | 46,800 | 30,500 |
| Aide visits | 104,400 | 129,200 | 105,400 |
| Supplies | -0- | -0- | 2,100 |
| Total | 446,500 | 470,500 | 408,700 |
| Other professional services | | | |
| Inpatient | 14,395,877 | 13,200,917 | 9,657,105 |
| Outpatient | 8,982,544 | 7,858,087 | 6,249,405 |
| Home health | 446,500 | 470,500 | 408,700 |
| Total other professional services | 23,824,921 | 21,529,504 | 16,315,210 |
| Gross patient service charges | 30,668,212 | 28,149,656 | 22,136,669 |
| Contractual adjustments | 15,439,615 | 14,048,421 | 9,358,136 |
| Charity care | 76,056 | 87,694 | 138,589 |
| Uncompensated care reimbursement | (733,214) | (675,018) | (587,205) |
| Total patient service allowances | 14,782,457 | 13,461,097 | 8,909,520 |
| Net patient service revenue | $ 15,885,755 | $ 14,688,559 | $ 13,227,149 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF OTHER OPERATING REVENUE
YEARS ENDED JUNE 30, 2004, 2003, AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Cafeteria | $ 40,833 | $ 43,882 | $ 41,456 |
| Medical records | 2,459 | 11,443 | 2,076 |
| Vending machines | 2,615 | 1,891 | 1,869 |
| Rentals | 4,615 | 6,650 | 3,075 |
| Pharmacy sales to employees | 7,360 | 2,920 | 1,160 |
| Workers' compensation premium adjustment | -0- | -0- | 233,624 |
| Stop loss recovery | -0- | 60,000 | 62,082 |
| Miscellaneous | 8,221 | 32,628 | 12,956 |
| Total other operating revenue | $ 66,103 | $ 159,414 | $ 358,298 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF OPERATING EXPENSES – SALARIES AND BENEFITS
YEARS ENDED JUNE 30, 2004, 2003, AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Salaries: | | | |
| Administrative and general | $ 740,835 | $ 701,154 | $ 658,831 |
| Plant operations and maintenance | 86,692 | 79,335 | 66,698 |
| Housekeeping | 188,357 | 197,531 | 215,830 |
| Dietary and cafeteria | 153,401 | 155,004 | 142,422 |
| Nursing administration | 78,911 | 68,858 | 99,401 |
| Central supply | 70,750 | 65,074 | 77,360 |
| Pharmacy | 91,973 | 154,956 | 182,655 |
| Medical records | 183,006 | 189,439 | 154,317 |
| Nursing services | 1,571,148 | 1,443,861 | 1,189,577 |
| Intensive care unit | 396,245 | 364,457 | 307,679 |
| Senior care unit | 430,979 | 442,849 | 379,789 |
| Nursery | 7,912 | 16,738 | 29,326 |
| Operating room | 197,492 | 183,166 | 178,873 |
| Anesthesia | -0- | 4,855 | 4,846 |
| Radiology | 202,325 | 174,918 | 165,135 |
| Laboratory | 257,635 | 251,089 | 248,722 |
| Respiratory therapy | 244,427 | 266,271 | 229,542 |
| Emergency room | 405,884 | 394,536 | 414,898 |
| Home health | 224,161 | 250,290 | 265,480 |
| Total salaries | $ 5,532,133 | $ 5,404,381 | $ 5,011,381 |
| Benefits and payroll taxes: | | | |
| Payroll taxes | $ 158,651 | $ 149,990 | $ 145,607 |
| Health insurance | 512,841 | 552,258 | 494,010 |
| Other | 466,101 | 326,910 | 258,115 |
| Total benefits and payroll taxes | $ 1,137,593 | $ 1,029,158 | $ 897,732 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF OPERATING EXPENSES – SUPPLIES AND DRUGS
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Administration | $ 122,122 | $ 131,232 | $ 136,886 |
| Housekeeping | 104,943 | 102,425 | 94,501 |
| Maintenance | 50,396 | 50,190 | 54,500 |
| Dietary | 201,808 | 195,115 | 164,524 |
| Medical records | 81,102 | 33,962 | 27,614 |
| Adults and pediatrics | 200,087 | 185,777 | 42,018 |
| Intensive care unit | 18,952 | 24,699 | 15,348 |
| Nursery | 829 | 1,493 | 2,359 |
| Emergency room | 32,796 | 25,069 | 15,493 |
| Operating room | 143,008 | 204,880 | 121,143 |
| Anesthesiology | 1,312 | 3,744 | 2,433 |
| Radiology | 414,457 | 378,020 | 454,708 |
| Laboratory | 240,399 | 249,472 | 195,819 |
| Blood | 131,105 | 96,690 | 71,195 |
| Physical therapy | 16 | 23 | -0- |
| EKG | 11 | -0- | 52,844 |
| EEG | 42,375 | 41,400 | 19,925 |
| Central supply | 19,688 | 111,579 | 131,010 |
| Respiratory therapy | 34,882 | 46,007 | 33,230 |
| Pharmacy | 1,184,040 | 1,083,037 | 880,510 |
| Home health | 30,758 | 20,073 | 9,371 |
| Senior care | 15,450 | 26,574 | 24,915 |
| Total supplies and drugs | $ 3,070,536 | $ 3,011,461 | $ 2,550,346 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF OPERATING EXPENSES – PROFESSIONAL FEES
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Adults and pediatrics | $ 47,230 | $ 39,623 | $ 1,291 |
| Operating room | -0- | 50 | -0- |
| Emergency room | 640,113 | 628,513 | 643,097 |
| Anesthesiology | 80,845 | 84,411 | 64,996 |
| Laboratory | 66 | 3,356 | 790 |
| Physical therapy | 16,850 | 19,000 | 13,800 |
| Occupational therapy | 320 | 300 | 400 |
| Respiratory therapy | -0- | -0- | 250 |
| Pharmacy | 231,338 | 33,480 | 4,680 |
| Radiology | 122,475 | 189,396 | 9,056 |
| Home health | 43,200 | 40,175 | 28,906 |
| Senior care | 34,886 | 56,161 | 43,884 |
| Dietary | 8,692 | 6,854 | 7,770 |
| Administration | 500 | 6,956 | 14,000 |
| Total professional fees | $ 1,226,515 | $ 1,108,275 | $ 832,920 |

HOMER MEMORIAL HOSPITAL
SCHEDULES OF OPERATING EXPENSES – OTHER EXPENSES
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Management fees | $ 186,000 | $ 233,000 | $ 240,362 |
| Legal and accounting | 189,538 | 154,000 | 144,518 |
| Repairs and maintenance | 11,092 | 15,000 | 55,105 |
| Utilities | 240,382 | 221,213 | 178,742 |
| Telephone | 60,097 | 62,503 | 53,905 |
| Travel | 16,564 | 13,825 | 9,986 |
| Rentals | 135,595 | 60,125 | 61,525 |
| Education | 12,210 | 20,251 | 6,818 |
| Public relations | 3,143 | 6,968 | 7,925 |
| Education contracts | 130,284 | -0- | 8,963 |
| Miscellaneous | 135,641 | 134,605 | 82,632 |
| Total other expenses | $ 1,120,546 | $ 921,490 | $ 850,481 |

HOMER MEMORIAL HOSPITAL
SCHEDULE OF PER DIEM AND
OTHER COMPENSATION PAID TO BOARD MEMBERS
YEARS ENDED JUNE 30, 2004, 2003 AND 2002

| | ---- TERM ---- | | |
|---|---|---|---|
| | BEGAN | ENDING | 2004 |
| Commissioners: | | | |
| Mr. Thomas "Buddy" Pixley, Chairman | Jan. 2003 | Dec. 2007 | None |
| Mayor Huey Dean | Jan. 2003 | Dec. 2006 | None |
| Mr C. C. Austin | | | |
| (Mayor's Designee) | Jan. 2003 | Dec. 2006 | None |
| Mr. Mike Hays | Jan. 2001 | Dec. 2005 | None |
| Mrs. Charles Etta Johnson | Jan. 2003 | Dec. 2007 | None |
| Mrs. Dottie Palmer, Secretary | Jan. 2001 | Dec. 2005 | None |
| Dr. Cliff Salmon | Medical Staff Representative | | None |
| Mr. George Tigner | Jan. 2002 | Dec. 2006 | None |
| Mr. Lawson Wilder | Jan 2002 | Dec. 2006 | None |
| Mrs. Gussie Young, Vice-Chairman | Jan. 2001 | Dec. 2005 | None |

Bobby G. Lester, CPA
John S. Wells, CPA
Robert G. Miller, CPA
Paul A. Delaney, CPA
Mary L. Carroll, CPA

Melanie I. Layssard, CPA
Brenda J. Lloyd, CPA

**LESTER, MILLER & WELLS**

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

Board of Commissioners
Homer Memorial Hospital
Homer, Louisiana

We have audited the basic financial statements of Homer Memorial Hospital (the Hospital) as of and for the years ended June 30, 2004, 2003 and 2002, and have issued our report thereon dated September 17, 2004. 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.

## Compliance

As part of obtaining reasonable assurance about whether the Hospital's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 that are required to be reported under Government Auditing Standards.

## Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Hospital's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the general purpose financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to the Hospital's management in the following schedule.

Board of Commissioners
Homer Memorial Hospital
Page Two

This report is intended for the information of the Board of Commissioners, Management and the Office of the Legislative Auditor of the State of Louisiana. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Lester, Miller & Wells
Certified Public Accountants
September 17, 2004

HOMER MEMORIAL HOSPITAL
MANAGEMENT RECOMMENDATIONS
YEARS ENDED JUNE 30, 2004, 2003, AND 2002

June 30, 2004
Accounts Receivable

**Finding:** Medicaid home health claims for the twelve month audit period were not processed for payment before the cost report submission deadline.

**Recommendation:** Accounts receivable for the Hospital should be more proactively monitored in order to expedite payments due. Management should review collection status on a monthly basis Responsibilities should be communicated to each member of the collections staff and aging reports for their area of accountability should be reviewed with them.

**Management's Response:** The Medicaid home health claims have been properly filed and payment is in process.

Inventory

**Finding:** A significant adjustment was necessary to accurately report inventory according to the physical count at year end. Supply costs were overstated on interim financial statements and did not properly match revenue with expenses during the year. It is essential for the financial position of the Hospital to be accurately portrayed on a monthly basis.

**Recommendation:** We suggest that management review the inventory allocation model for Hospital supply accounting. We suggest a review of inventory balances each month to ensure that unrealistic inventory account balances are detected before year end.

**Management's Response:** Management has implemented procedures to review monthly inventory account balances to ensure accurate reporting on an interim basis.

June 30, 2003
Accounts Payable

**Finding:** A large amount of expenses are not being accrued, especially expenses relating to services such as professional fees.

**Recommendation:** For large service expenses such as professional fees and legal and accounting fees, review the invoices for service dates rendered so that the accruals will be made in the proper periods.

**Management's Response:** Management has implemented procedures to review monthly invoices and vendor accounts, to ensure accurate monthly accruals of expenses.