THE BAXLEY AND APPLING COUNTY
HOSPITAL AUTHORITY
D/B/A APPLING HEALTHCARE SYSTEM
(A Component Unit of Appling County, Georgia)

FINANCIAL STATEMENTS

for the years ended August 31, 2019 and 2018

C O N T E N T S

Draffin Tucker

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
The Baxley and Appling County Hospital Authority
D/B/A Appling Healthcare System
Baxley, Georgia

Report on the Financial Statements

We have audited the accompanying financial statements of The Baxley and Appling County Hospital Authority, D/B/A Appling Healthcare System (System), which comprise the balance sheets as of August 31, 2019 and 2018, the related statements of revenues, expenses and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the System's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Continued

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Baxley and Appling County Hospital Authority, D/B/A Appling Healthcare System as of August 31, 2019 and 2018, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 24, 2020, on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of the System's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

Draffin + Tucker LLP

Albany, Georgia
January 24, 2020

THE BAXLEY AND APPLING COUNTY
HOSPITAL AUTHORITY
D/B/A APPLING HEALTHCARE SYSTEM
(A Component Unit of Appling County, Georgia)

BALANCE SHEETS
August 31, 2019 and 2018

	2019	2018
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES		
Current assets:		
Cash	$ 633,845	$ 2,643,638
Patient accounts receivable, net of estimated uncollectibles of $4,886,656 in 2019 and $5,250,271 in 2018	2,694,366	2,366,276
Supplies	539,796	569,267
Estimated third-party payor settlements	289,991	126,357
Other current assets	923,955	1,455,046
Total current assets	5,081,953	7,160,584
Capital assets:		
Non-depreciable capital assets	601,451	620,709
Depreciable capital assets, net of accumulated depreciation	15,686,007	15,348,544
Total capital assets, net of accumulated depreciation	16,287,458	15,969,253
Other assets:		
Other receivables	31,805	19,999
Restricted cash for debt service	157,496	157,260
Total other assets	189,301	177,259
Total assets	21,558,712	23,307,096
Deferred outflows of resources:		
Goodwill, net of accumulated amortization	207,424	228,698
Total assets and deferred outflows of resources	$ 21,766,136	$ 23,535,794

	2019	2018
LIABILITIES AND NET POSITION		
Current liabilities:		
Current maturities of long-term debt	$ 853,354	$ 638,763
Accounts payable	1,034,657	1,433,104
Accrued expenses	1,427,250	1,295,132
Estimated third-party payor settlements	32,396	163,355
Total current liabilities	3,347,657	3,530,354
Long-term debt, net of current maturities	6,698,583	7,173,801
Total liabilities	10,046,240	10,704,155
Net position:		
Net investment in capital assets	9,057,144	8,156,689
Restricted	156,384	156,384
Unrestricted	2,506,368	4,518,566
Total net position	11,719,896	12,831,639
Total liabilities and net position	$ 21,766,136	$ 23,535,794

The accompanying notes are an integral
part of these financial statements.

THE BAXLEY AND APPLING COUNTY
HOSPITAL AUTHORITY
D/B/A APPLING HEALTHCARE SYSTEM
(A Component Unit of Appling County, Georgia)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
for the years ended August 31, 2019 and 2018

	2019	2018
Operating revenues:		
Net patient service revenue (net of provision for bad debts of $4,468,703 in 2019 and $3,057,155 in 2018)	$ 28,565,229	$ 28,108,967
Other revenue	331,419	306,670
Total operating revenues	28,896,648	28,415,637
Operating expenses:		
Salaries and wages	12,373,536	11,812,734
Employee benefits	2,390,317	2,486,067
Supplies and other	7,830,123	7,352,499
Purchased services	6,468,098	6,613,750
Depreciation and amortization	1,681,229	1,785,290
Total operating expenses	30,743,303	30,050,340
Operating loss	(1,846,655)	(1,634,703)
Nonoperating revenues (expenses):		
Interest expense	(473,537)	(421,083)
Noncapital grants and contributions	600,000	600,000
Gain (loss) on sale or disposal of assets	(13,640)	107,416
Rural hospital tax credit contributions	122,089	647,270
Total nonoperating revenues	234,912	933,603
Excess expenses before capital grants and contributions	(1,611,743)	(701,100)
Capital grants and contributions	500,000	581,489
Decrease in net position	(1,111,743)	(119,611)
Net position, beginning of year	12,831,639	12,951,250
Net position, end of year	$ 11,719,896	$ 12,831,639

The accompanying notes are an integral
part of these financial statements.

THE BAXLEY AND APPLING COUNTY
HOSPITAL AUTHORITY
D/B/A APPLING HEALTHCARE SYSTEM
(A Component Unit of Appling County, Georgia)

STATEMENTS OF CASH FLOWS
for the years ended August 31, 2019 and 2018

	2019	2018
Cash flows from operating activities:		
Receipts from and on behalf of patients	$ 28,273,965	$ 29,405,860
Payments to suppliers and contractors	(14,127,811)	(14,707,629)
Payments to employees	(14,651,835)	(14,784,381)
Net cash used by operating activities	(505,681)	(86,150)
Cash flows from noncapital financing activities:		
Noncapital grants and contributions	600,000	600,000
Rural hospital tax credit contributions	122,089	647,270
Net cash provided by noncapital financing activities	722,089	1,247,270
Cash flows from capital and related financing activities:		
Capital grants and contributions	500,000	485,593
Proceeds from issuance of long-term debt	1,100,000	-
Principal paid on long-term debt	(1,360,627)	(567,619)
Interest paid on long-term debt	(473,537)	(423,673)
Purchase of capital assets	(1,991,801)	(2,141,678)
Proceeds from sale of capital assets	-	475,000
Net cash used by capital and related financing activities	(2,225,965)	(2,172,377)
Net decrease in cash	(2,009,557)	(1,011,257)
Cash, beginning of year	2,800,898	3,812,155
Cash, end of year	$ 791,341	$ 2,800,898
Reconciliation of cash to the balance sheets:		
Cash	$ 633,845	$ 2,643,638
Restricted cash for debt service	157,496	157,260
Total cash	$ 791,341	$ 2,800,898

Continued

THE BAXLEY AND APPLING COUNTY
HOSPITAL AUTHORITY
D/B/A APPLING HEALTHCARE SYSTEM
(A Component Unit of Appling County, Georgia)

STATEMENTS OF CASH FLOWS, Continued
for the years ended August 31, 2019 and 2018

	2019	2018
Reconciliation of operating loss to net cash flows used by operating activities:		
Operating loss	$ (1,846,655)	$ (1,634,703)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation and amortization	1,681,229	1,785,290
Provision for bad debts	4,468,703	3,057,155
Changes in:		
Patient accounts receivable	(4,818,347)	(2,021,497)
Supplies	29,471	(7,850)
Other current and noncurrent assets	519,286	(681,151)
Accounts payable	(398,447)	(44,930)
Accrued expenses	132,118	(493,029)
Estimated third-party payor settlements	(232,594)	(45,435)
Net cash used by operating activities	$ (465,236)	$ (86,150)

Supplemental disclosures of cash flow information:
The System received a capital asset donation of a building with an acquisition value of $95,896 during 2018.

The accompanying notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies

Reporting Entity

The Baxley and Appling County Hospital Authority, D/B/A Appling Healthcare System (System) is a public corporation. It was created by the Board of Commissioners of Appling County, Georgia to operate, control, and manage the operations of Appling General Hospital (Hospital), a 34-bed acute care hospital and a 30-bed inpatient psychiatric facility; and the Pavillion, a 101-bed skilled nursing facility. The County Commissioners nominate members for the Board of Trustees of the System. For this reason, the System is considered to be a component unit of Appling County, Georgia.

Use of Estimates

The preparation of financial statements in accordance 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. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Enterprise Fund Accounting

The System uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

The System prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB).

Restricted Cash for Debt Service

Restricted cash for debt service includes cash restricted by lenders related to the USDA loan as discussed in Note 8.

Allowance for Estimated Uncollectible Accounts

The System provides an allowance for estimated uncollectible accounts based on an evaluation of the overall collectability of the accounts receivable. As accounts are known to be uncollectible, the accounts are charged against the allowance.

Continued

1. Summary of Significant Accounting Policies, Continued

Supplies

Supplies are stated at the lower of cost or market value, using the first-in, first-out method.

Capital Assets

The System's capital assets are reported at historical cost. Contributed capital assets are reported at their acquisition value at the time of their donation. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method. The estimated useful life is assigned using AHA Useful Lives Guidelines listed below. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Land improvements	15 to 20 years
Buildings and building improvements	20 to 40 years
Equipment	3 to 7 years

Financing Costs

Costs related to the issuance of long-term debt are expensed in the period in which the debt was incurred.

Compensated Absences

The System's employees earn paid time off (PTO) at varying rates depending on years of service. PTO accumulates to a maximum of 400 hours. Employees are paid for accumulated PTO if they leave before retirement and are not terminated. The estimated amount of PTO payable is reported as a current liability in both 2019 and 2018.

Restricted Resources

When the System has both restricted and unrestricted resources available to finance a particular program, it is the System's policy to use restricted resources before unrestricted resources.

Continued

1. Summary of Significant Accounting Policies, Continued

Net Position

Net position of the System is classified into three components. *Net investment in capital assets* consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted net* position are noncapital assets reduced by liabilities and deferred inflows of resources related to those assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the System, including amounts deposited as required by lenders, as discussed in Note 8. *Unrestricted net position* are remaining net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that do not meet the definition of *net investment in capital assets* or *restricted net position*.

Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity Care

The System provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Operating Revenues and Expenses

The System's statement of revenues, expenses and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the System's principle activity. Nonexchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Continued

1. Summary of Significant Accounting Policies, Continued

Grants and Contributions

From time to time, the System receives grants from Appling County as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. The System received $600,000 in grants from Appling County for the years ended 2019 and 2018. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

Risk Management

The System 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. Settled claims have not exceeded this commercial coverage in any of the three preceding years. The System is self-insured for employee health insurance (see Note 11). See Note 10 for additional information related to the System's general and professional coverage.

Income Taxes

The System is a governmental entity and is exempt from income taxes. Accordingly, no provision for income taxes has been considered in the accompanying financial statements.

Estimated Malpractice and Other Self-Insurance Costs

The provisions for estimated medical malpractice claims and other claims under self-insurance plans include estimates of the ultimate costs for both reported claims and claims incurred but not reported.

Impairment of Long-Lived Assets

The System evaluates on an ongoing basis the recoverability of its assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The impairment loss to be recognized is the amount by which the carrying value of the long-lived asset exceeds the asset's fair value. In most instances, the fair value is determined by discounted estimated future cash flows using an appropriate interest rate. The System has not recorded any impairment charges in the accompanying statements of revenues, expenses and changes in net position for the years ended 2019 and 2018.

Continued

1. Summary of Significant Accounting Policies, Continued

Deferred Outflows of Resources

Deferred outflows of resources consist of goodwill, net of accumulated amortization, as of August 31, 2019 and 2018. See Note 12 for additional information.

Recently Adopted Accounting Pronouncements

In 2019, the System adopted GASB Statement No. 83, *Certain Asset Retirement Obligations* (GASB 83). GASB 83 addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability and a corresponding deferred outflow of resources based on the guidance in this Statement. The adoption of GASB 83 had no material impact on the financial statements of the System.

In March 2018, the GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements* (GASB 88). GASB 88 clarifies which liabilities should be included when disclosing information related to debt, requires additional essential information related to debt be disclosed, and requires that existing and additional information be provided for direct borrowings and direct placements of debt separately from other debt. GASB 88 is effective for fiscal years beginning after June 15, 2018. The System has adopted the provisions for all periods presented.

Accounting Pronouncement Not Yet Adopted

In January 2017, the GASB issued Statement No. 84, *Fiduciary Activities* (GASB 84). GASB 84 establishes criteria for identifying fiduciary activities of all state and local governments. An activity meeting the criteria should be reported in a fiduciary fund in the financial statements. Governments with activities meeting the criteria should present a statement of fiduciary net position and a statement of changes in fiduciary net position. GASB 84 is effective for fiscal years beginning after December 15, 2018. The System is currently evaluating the impact GASB 84 will have on its financial statements.

2. Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. The System does not believe that there are any significant credit risks associated with receivables due from third-party payors.

Continued

2. Net Patient Service Revenue, Continued

Net revenue from the Medicare and Medicaid programs accounted for approximately 36% and 33%, respectively, of the System's net patient service revenue for the year ended August 31, 2019, and 38% and 33% respectively, of the System's net patient service revenue for the year ended August 31, 2018. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The 2019 net patient service revenue increased approximately $179,000 due to prior-year retroactive adjustments in addition to amounts previously estimated.

The System believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. However, there has been an increase in regulatory initiatives at the state and federal levels including the initiation of the Recovery Audit Contractor (RAC) program and Medicaid Integrity Contractor (MIC) program. These programs were created to review Medicare and Medicaid claims for medical necessity and coding appropriateness. The RAC's have authority to pursue improper payments with a three year look back from the date the claim was paid. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties and exclusion from the Medicare and Medicaid programs.

A summary of the payment arrangements with major third-party payors follows:

- Medicare

  Inpatient acute care and 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 psychiatric services rendered to Medicare program beneficiaries are paid at prospectively determined per diems.

  Nursing Home services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system called Resource Utilization Groups (RUGs). Effective October 1, 2019, the services rendered to Medicare program beneficiaries will be paid based on a patient-driven payment methodology.

Continued

2. Net Patient Service Revenue, Continued

- Medicare, Continued

  The System is reimbursed for certain reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare Administrative Contractor (MAC). The System's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with the System. The System's Medicare cost reports have been audited by the MAC through August 31, 2015.

- Medicaid

  Inpatient acute care services rendered to Medicaid 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. Certain outpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement methodology.

  The System is reimbursed at a tentative rate with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicaid fiscal intermediary. The System's Medicaid cost reports have been audited by the Medicaid fiscal intermediary through August 31, 2016.

  The System has also entered into contracts with certain managed care organizations to receive reimbursement for providing services to selected enrolled Medicaid beneficiaries. Payment arrangements with these managed care organizations consist primarily of prospectively determined rates per discharge, discounts from established charges, or prospectively determined per diems.

  Long-term care services are reimbursed by the Medicaid program based on a prospectively determined per diem. The per diem is determined by the facility's historical allowable operating costs adjusted for certain incentives and inflation factors.

  The System participates in the Georgia Indigent Care Trust Fund (ICTF) Program. The System receives ICTF payments for treating a disproportionate number of Medicaid and other indigent patients. ICTF payments are based on the System's estimated uncompensated cost of services to Medicaid and uninsured patients. The net amount of ICTF payments recognized in net patient service revenue was approximately $386,979 and $281,282 for the years ended 2019 and 2018, respectively.

Continued

2. Net Patient Service Revenue, Continued

- Medicaid, Continued

  The Medicare, Medicaid and SCHIP Benefits Improvement and Protection Act of 2000 (BIPA) provides for payment adjustments to certain facilities based on the Medicaid Upper Payment Limit (UPL). The UPL payment adjustments are based on a measure of the difference between Medicaid payments and the amount that could be paid based on Medicare payment principles. The net amount of the UPL payment adjustments recognized in net patient service revenue was approximately $563,495 and $763,692 for the years ended 2019 and 2018, respectively.

  The state of Georgia enacted legislation known as the Provider Payment Agreement Act (Act) whereby hospitals in the state of Georgia are assessed a “provider payment” in the amount of 1.45% of their net patient revenue. The Act became effective July 1, 2010, the beginning of state fiscal year 2011. The provider payments are due on a quarterly basis to the Department of Community Health. The payments are to be used for the sole purpose of obtaining federal financial participation for medical assistance payments to providers on behalf of Medicaid recipients. The provider payment results in a corresponding increase in hospital payments on Medicaid services of approximately 11.88%. Approximately $229,153 and $248,012 relating to the Act is included in supplies and other in the accompanying statement of revenues, expenses and changes in net position for the years ended August 31, 2019 and 2018, respectively.

- Other Arrangements

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

3. Uncompensated Services

The System was compensated for services at amounts less than its established rates. Charges for uncompensated services for 2019 and 2018 were $26,842,345 and $29,168,175, respectively.

Uncompensated care includes charity and indigent care services of $614,779 and $1,406,012 in 2019 and 2018, respectively. The cost of charity and indigent care services provided during 2019 and 2018 was approximately $341,000 and $738,000, respectively computed by applying a total cost factor to the charges forgone.

Continued

3. Uncompensated Services, Continued

The following is a summary of uncompensated services and a reconciliation of gross patient charges to net patient service revenue for 2019 and 2018.

	2019	2018
Gross patient charges	$ 55,407,574	$ 57,277,142
Uncompensated services:		
Charity and indigent care	614,779	1,406,012
Medicare	8,588,420	10,553,649
Medicaid	1,504,053	2,131,306
Other allowances	11,666,390	12,020,053
Bad debts	4,468,703	3,057,155
Total uncompensated services	26,842,345	29,168,175
Net patient service revenue	$ 28,565,229	$ 28,108,967

4. Deposits

Deposits are classified on the balance sheets as follows:

	2019	2018
Cash - demand deposit accounts	$ 633,845	$ 2,643,638
Restricted cash for debt service - demand deposit account	157,496	157,260
Total	$ 791,341	$ 2,800,898

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the System will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The System's bank deposits at 2019 and 2018 are entirely insured or collateralized with direct loans to the System held by the financial institution.

Continued

5. Accounts Receivable and Payable

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the System at August 31, 2019 and 2018 consisted of these amounts:

	2019	2018
Patient accounts receivable:		
Receivable from patients and their insurance carriers	$ 4,852,072	$ 4,964,341
Receivable from Medicare	1,867,514	1,626,895
Receivable from Medicaid	861,436	1,025,311
Total gross patient accounts receivable	7,581,022	7,616,547
Less allowance for uncollectible amounts and contractual adjustments	4,886,656	5,250,271
Patient accounts receivable, net	$ 2,694,366	$ 2,366,276
Accounts payable and accrued expenses:		
Payable to employees (including payroll taxes)	$ 1,024,320	$ 878,112
Payable to suppliers	1,034,657	1,433,104
Other	402,930	417,020
Total accounts payable and accrued expenses	$ 2,461,907	$ 2,728,236

Continued

6. Capital Assets

A summary of capital assets follows:

	2018 Balance	Increase	Transfer	Decrease	2019 Balance
Land	$ 577,091	$ -	$ -	$ -	$ 577,091
Construction in progress	43,618	199,339	(216,472)	(2,125)	24,360
Total non-depreciable capital assets	620,709	199,339	(216,472)	(2,125)	601,451
Land improvements	413,311	41,500	-	-	454,811
Buildings and improvements	17,473,270	65,295	186,102	(1,766)	17,722,901
Fixed equipment	3,832,850	1,503,893	-	-	5,336,743
Major movable equipment	14,088,527	183,898	30,370	(17,950)	14,284,845
Total depreciable capital assets	35,807,958	1,794,586	216,472	(19,716)	37,799,300
Less accumulated depreciation and amortization for:					
Land improvements	(346,245)	(11,933)	-	-	(358,178)
Buildings and improvements	(7,622,941)	(516,350)	-	919	(8,138,372)
Fixed equipment	(2,096,338)	(386,245)	-	-	(2,482,583)
Major movable equipment	(10,393,890)	(745,425)	-	5,155	(11,134,160)
Total accumulated depreciation	(20,459,414)	(1,659,953)	-	6,074	(22,113,293)
Total depreciable capital assets, net	15,348,544	134,633	216,472	(13,642)	15,686,007
Total capital assets, net	$ 15,969,253	$ 333,972	$ -	$ (15,767)	$ 16,287,458

Continued

6. Capital Assets, Continued

	2017 Balance	Increase	Transfer	Decrease	2018 Balance
Land	$ 567,907	$ -	$ 77,500	$ (68,316)	$ 577,091
Construction in progress	613,123	1,510,153	(1,827,710)	(251,948)	43,618
Total non-depreciable capital assets	1,181,030	1,510,153	(1,750,210)	(320,264)	620,709
Land improvements	452,643	-	18,396	(57,728)	413,311
Buildings and improvements	16,555,217	14,086	1,239,465	(335,498)	17,473,270
Fixed equipment	3,186,722	568,124	78,004	-	3,832,850
Major movable equipment	13,282,872	397,310	414,345	(6,000)	14,088,527
Total depreciable capital assets	33,477,454	979,520	1,750,210	(399,226)	35,807,958
Less accumulated depreciation and amortization for:					
Land improvements	(346,727)	(11,901)	-	12,383	(346,245)
Buildings and improvements	(7,229,561)	(474,803)	-	81,423	(7,622,941)
Fixed equipment	(1,884,122)	(212,216)	-	-	(2,096,338)
Major movable equipment	(9,334,796)	(1,065,094)	-	6,000	(10,393,890)
Total accumulated depreciation	(18,795,206)	(1,764,014)	-	99,806	(20,459,414)
Total depreciable capital assets, net	14,682,248	(784,494)	1,750,210	(299,420)	15,348,544
Total capital assets, net	$ 15,863,278	$ 725,659	$ -	$ (619,684)	$ 15,969,253

Continued

6. Capital Assets, Continued

The cost of assets under capital lease obligations was approximately $44,000 at 2019 and 2018. Accumulated amortization related to the equipment under capital lease obligations was approximately $29,000 and $23,000 at 2019 and 2018, respectively.

7. Other Receivables

Other receivables consist primarily of loans to physicians through recruiting incentive arrangements. In general, the loans are being forgiven over a period of time in which the physician practices medicine in the Baxley and Appling County, Georgia area. If the physician discontinues medical practice in this area, the outstanding principal and accrued interest becomes due immediately. The amounts forgiven and charged to expense during 2019 and 2018 were approximately $4,900 and $7,500, respectively.

8. Long-Term Debt and Capital Leases

A summary of long-term debt and capital leases at August 31, 2019 and 2018, follows:

	2019	2018
Long-Term Debt		
USDA Community Facility loan, due in monthly installments of $13,032, including interest at 2.875%, due June 16, 2031, secured by real estate.	$ 1,483,717	$ 1,593,332
Note payable, due in monthly installments of $7,592, including interest at the greater of the index prime rate plus 1.00% with a minimum rate of 5.5%, due April 5, 2023, secured by real estate.	302,455	373,477

Continued

8. Long-Term Debt and Capital Leases, Continued

	2019	2018
Long-Term Debt, Continued		
Note payable, due in monthly installments of $9,475, including interest at the greater of the Wall Street Journal prime rate plus 1.25% with a minimum rate of 5.25%, due July 8, 2032, secured by real estate.	$ 463,478	$ 485,330
Note payable, due in monthly installments of $48,496, including interest at the greater of the Wall Street Journal prime rate plus 1.25% with a minimum rate of 5.25%, due October 25, 2029, secured by real estate.	4,602,423	4,908,718
Note payable, due in monthly installments of $6,928, including interest of 4.25%, due August 22, 2024, secured by equipment.	373,886	437,988
Note payable, due in monthly installments of $18,276, including interest of 6%, due October 16, 2024, secured by equipment and accounts receivable.	321,623	-
Capital Lease		
Capital lease obligations, with interest rates ranging from 3.15% to 4.49%, collateralized by leased equipment.	4,355	13,719
Total long-term debt and capital lease obligations	7,551,937	7,812,564
Less: Current maturities of long-term debt	853,354	638,763
Long-term debt, net of current maturities	$ 6,698,583	$ 7,173,801

Continued

8. Long-Term Debt and Capital Leases, Continued

A schedule of changes in the System's long-term debt follows:

	2018 Balance	Additions	Reductions	2019 Balance	Due Within One Year
Direct borrowings:					
Community Facility Loan	$ 1,593,332	$ -	$ (109,615)	$ 1,483,717	$ 115,393
Notes payable	6,205,513	1,100,000	(1,241,648)	6,063,865	733,606
Capital Lease	13,719	-	(9,364)	4,355	4,355
Total long-term debt	$ 7,812,564	$ 1,100,000	$ (1,360,627)	$ 7,551,937	$ 853,354

	2017 Balance	Additions	Reductions	2018 Balance	Amounts Due Within One Year
Direct borrowings:					
Community Facility Loan	$ 1,699,844	$ -	$ (106,512)	$ 1,593,332	$ 112,126
Notes payable	6,657,994	-	(452,481)	6,205,513	517,273
Capital Lease	22,345	-	(8,626)	13,719	9,364
Total long-term debt	$ 8,380,183	$ -	$ (567,619)	$ 7,812,564	$ 638,763

USDA Loan

In June 2016, the System obtained a community facility loan from the United States Department of Agriculture (USDA) in the amount of $1.8 million, secured by real estate. The term of the loan is 15 years with an interest rate of 2.875%.

Under the terms of the USDA loan, the System is required to maintain a mortgage reserve fund sufficient to meet the current portion of the debt service requirements for the USDA loan as required by the original loan documents. The System was in compliance with this requirement at August 31, 2019. The mortgage reserve fund is presented with restricted cash for debt service and is included in restricted net position on the balance sheet.

8. Long-Term Debt and Capital Leases, Continued

Continued

USDA Loan, Continued

The USDA loan contains a provision that in an event of default, outstanding obligations may become immediately due and payable.

Notes Payable

In October 2014, the System obtained a note from Pineland Bank (formerly Peoples State Bank and Trust) in the amount of $6 million. The proceeds were used to consolidate all notes payable, capital leases, and the line-of-credit outstanding at that time. The term of the note is 15 years at a variable rate of prime plus 1.25%, with a minimum rate of 5.25%.

In April 2016, the System obtained a note from Pineland Bank (formerly Peoples State Bank and Trust) in the amount of $526,894. The proceeds were used to purchase medical equipment. The term of the note is 7 years at a variable rate of prime plus 1.00%, with a minimum rate of 5.50%.

In August 2016, the System was approved for a loan from Pineland Bank (formerly Peoples State Bank and Trust) up to $1.2 million. As of August 31, 2019, the System has drawn $510,905. The term of the loan is 15 years at a variable rate of prime plus 1.25%, with a minimum rate of 5.25%.

In August 2017, the System obtained a loan from Pineland Bank in the amount of $501,571. The proceeds were used to purchase a new CT Scanner in fiscal year 2018. The term of the loan is 7 years at a fixed interest rate of 4.25%.

In October 2018, the System obtained a note from Pineland Bank in the amount of $1.1 million. The proceeds were used to exercise a purchase option from an operating lease for an MRI machine. The term of the note is 6 years at a fixed rate of 6.00%.

All notes payable contain a provision that in an event of default, outstanding obligations may become immediately due and payable.

Continued

8. Long-Term Debt and Capital Leases, Continued

Capital Lease

In February 2015, the System entered into a capital lease, collateralized by leased equipment with an amortized cost of approximately $15,000 and $21,000 as of August 31, 2019 and 2018, respectively. The term of the lease is 5 years at a rate in the range of 3.15% to 4.49%.

Scheduled principal and interest repayments on long-term debt and capital leases are as follows:

Year Ending August 31,	Principal	Interest
2020	$ 853,354	$ 399,879
2021	787,123	359,743
2022	710,796	318,726
2023	794,636	274,242
2024	581,514	237,329
2025-2029	2,992,474	699,232
2030-2032	832,040	6,352
Total	$ 7,551,937	$ 2,295,503

9. Concentrations of Credit Risk

The System 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 at August 31, 2019 and 2018, is as follows:

	2019	2018
Medicare	25%	21%
Blue Cross and other third-party payors	45%	41%
Patients	19%	25%
Medicaid	11%	13%
	100%	100%

Continued

10. Commitments and Contingencies

Operating Leases

The System has operating leases with various vendors, primarily for equipment. Future estimated minimum operating lease payments that have initial or remaining lease terms in excess of one year are as follows:

Year Ending August 31,	Operating Lease Payments
2020	$ 101,496
2021	47,596
Total	$ 149,092

Rental expense under all operating lease agreements for the years ended August 31, 2019 and 2018 was approximately $147,000 and $317,000, respectively.

Malpractice Insurance

The System is covered by a claims-made general and professional liability insurance policy with a specified deductible per incident and excess coverage on a claims-made basis. The liability limits related to this policy are $1 million per occurrence and $5 million in aggregate in 2019 and 2018. Umbrella coverage is provided by Hudson Specialty Insurance Company for $5 million per claim and annual aggregate. The System uses a third-party administrator to review and analyze incidents that may result in a claim against the System. Management believes these claims, if asserted, would be settled within the limits of insurance coverage.

Various claims and assertions are made against the System during the ordinary course of providing services. In addition, other claims may be asserted arising from services provided to patients in the past. It is the opinion of management that the System has adequate liability insurance protection to indemnify any material asserted or unasserted claims as of August 31, 2019.

Continued

10. Commitments and Contingencies, Continued

Compliance Plan

The healthcare industry has been subjected to increased scrutiny from governmental agencies at both the federal and state level with respect to compliance with regulations. Areas of noncompliance identified at the national level include Medicare and Medicaid, Internal Revenue Service, and other regulations governing the healthcare industry. In addition, the Reform Legislation includes provisions aimed at reducing fraud, waste, and abuse in the healthcare industry. These provisions allocate significant additional resources to federal enforcement agencies and expand the use of private contractors to recover potentially inappropriate Medicare and Medicaid payments. The System has implemented a compliance plan focusing on such issues. There can be no assurance that the System will not be subjected to future investigations with accompanying monetary damages.

Health Care Reform

There has been increasing pressure on Congress and some state legislatures to control and reduce the cost of healthcare at the national and the state levels. Legislation has been passed that includes cost controls on healthcare providers, insurance market reforms, delivery system reforms and various individual and business mandates among other provisions. The costs of these provisions are and will be funded in part by reductions in payments by government programs, including Medicare and Medicaid. There can be no assurance that these changes will not adversely affect the System.

Litigation

The System is involved in litigation and regulatory investigations arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the System’s future financial position or results from operations. See malpractice insurance disclosures above.

11. Self-Insurance – Employee Health Plan

The System provides a self-insurance program for its employees under which a third-party administrator processes and pays claims. The System reimburses the third-party administrator monthly. The System has purchased stop-loss insurance coverage for claims in excess of $80,000 for each individual employee. Under this self-insurance program, the System paid or accrued approximately $1,415,000 and $1,379,000 during the years ended August 31, 2019 and 2018, respectively.

Continued

12. Deferred Outflows of Resources

Deferred outflows of resources consisted of the following:

	2019	2018
Goodwill, net of amortization	$ 207,424	$ 228,698

Pursuant to the implementation of GASB Statement No. 69, the System's goodwill is reported net of accumulated amortization expense and is amortized over 15 years. Amortization expense is reported in depreciation and amortization in the amount of approximately $21,000 for 2019 and 2018.

13. Employee Retirement Plan

The System has a defined contribution retirement plan pursuant to Section 403(b) of the Internal Revenue Code covering all employees that are 18 or older and work at least 20 hours a week. Under the terms of this plan, the System will contribute 50% of the employee's contributions not to exceed 6% of the employee's annual salary. The System's contributions will vest 20% for each year of service up to 100% vesting after five years of service. As of January 2012, the System suspended matching contributions indefinitely. The System may also make a discretionary contribution which is allocated to eligible employees based on the employee's compensation to total compensation of eligible employees. The System made no contributions during the years ended August 31, 2019 and 2018.

14. Special Purpose Sales Tax

The System entered into an agreement with Appling County, Georgia to secure funding for hospital renovations through a referendum held during 2017 approving a 1% sales and use tax in the County with $3,000,000 allocated to the System over six years. As of August 31, 2019, the System has recorded approximately $833,000 cumulative contributions from the referendum.

Special purpose sales tax funds are reflected in capital grants and contributions in the accompanying statements of revenues, expenses, and changes in net position.

Continued

16. Rural Hospital Tax Credit

The State of Georgia (State) passed legislation which allows individuals or corporations to receive a state tax credit for making a contribution to certain qualified rural hospital organizations. The System submitted the necessary documentation and was approved by the State to participate in the rural hospital tax credit program for program years 2019 and 2018. Contributions received under the program approximate $122,000 and $647,000 during fiscal years 2019 and 2018, respectively.

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

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

Board of Trustees
The Baxley and Appling County Hospital Authority
D/B/A Appling Healthcare System
Baxley, Georgia

We have audited, in accordance with the 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, the financial statements of The Baxley and Appling County Hospital Authority, D/B/A Appling Healthcare System (System), which comprise the balance sheet as of August 31, 2019, and the related statements of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated January 24, 2020.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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 System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System'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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Responses, we identified certain deficiencies in internal control, that we consider to be material weaknesses and 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 a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the System's financial statements will not be prevented, or detected and corrected on a timely basis. We consider deficiencies 2019-001, 2019-002, 2019-003, and 2019-004 presented in the accompanying Schedule of Findings and Responses to be material weaknesses.

Continued

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. We consider deficiency 2019-005 presented in the accompanying Schedule of Findings and Responses to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free from 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.*

System's Response to Findings

The System's response to findings identified in our audit is described in the accompanying Schedule of Findings and Responses. The System's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Draffin & Tucker, LLP

Albany, Georgia
January 24, 2020

Material Weakness 2019-001

Condition/Criteria:	Accrued salaries were not accrued properly for wages earned, but not yet paid, at year end.
Cause:	During fiscal year 2019, a new payroll system was implemented, which necessitated a change in the accrual procedures. While procedures were modified, an adequate review process was not implemented.
Effect:	The System's financial statements were materially misstated, resulting in an audit adjusting entry to correct the accrual.
Recommendation:	We recommend implementing a detailed review of all accruals each month by management to reduce risk of misstatement.
Views of responsible officials and planned corrective actions:	The Hospital changed payroll systems during the year in order for more timely reporting within each department and to better automate the payroll process. The implementation went well from the standpoint of department head activities, but the accounting, especially the payroll accrual process was the source of several meetings with the new system (PayCom). PayCom transitioned through several accounting managers dedicated to our account. As of December's close, the payroll accrual process is working as it should. For a while the consultant's company was accruing some payroll expense to a balance sheet account instead of the expense. There were manual adjustments made by accounting staff in order to estimate expenses each month until the payroll system's internal process was corrected.

Continued

Material Weakness 2019-002

Condition/Criteria:	The MRI equipment and related note payable were not recorded on the general ledger.
Cause:	There was no procedure in place at the time of the debt issuance to detect errors in properly recording the transaction.
Effect:	The System's financial statements were materially misstated.
Recommendation:	We recommend implementing a policy for review of all new debt agreements and equipment purchased to ensure proper recording.
Views of responsible officials and planned corrective actions:	A policy has been implemented to record debt agreements and capitalize equipment purchased to ensure depreciation is recorded.

Material Weakness 2019-003

Condition/Criteria:	The prepaid insurance balances did not accurately reflect the balance for the remaining terms of the policies in effect.
Cause:	There was no procedure in place to provide for adequate review of the prepaid insurance calculation during 2019.
Effect:	The System's financial statements were materially misstated.
Recommendation:	We recommend creating policies and procedures for prepaid insurance to ensure they adequately address the computation and review of the balances during the month-end close process.
Views of responsible officials and planned corrective actions:	This has been an adjusting entry for years in the past, and the comment is correct for 2019. One of the two additions to the accounting/finance department will be assigned to maintain a prepaid insurance schedule. Training will be conducted if necessary in order to maintain an excel spreadsheet as to balances at each month end's close.

Continued

Material Weakness 2019-004

Condition/Criteria:	The reserve for uncollectible accounts receivable were incorrectly stated at year-end.
Cause:	The System's procedure for computing regarding allowances for uncollectible accounts receivable was not followed in 2019.
Effect:	The System's financial statements were materially misstated.
Recommendation:	We recommend developing and implementing a methodology for valuation and allowances for older accounts receivable to more reflect the collectability of accounts receivable.
Views of responsible officials and planned corrective actions:	One aspect of past procedures not continued was each insurance clerk estimating at month end how much of their accounts receivable was collectible. Since this was an estimate, we discontinued this part of the process for a while in order to emphasize spending that time on billing. The accounting process of using past ratios and calculations was continued as usual. In addition, a spreadsheet was maintained throughout the year looking at the percentage of each type of account (Hospital, BHU, Pavilion, Physician Practice) which was reserved after month end. The percent reserved remained consistent, and went from 63% to 65% from February (when this spreadsheet was first set up) through August 2019. The reserve percentage has since increased to 71%. A second check we do on the recorded net revenue is to compare net patient revenue to actual cash collections from patient accounts. As presented in August on the interim financial statements, the net patient revenue as reported was $27,168,375. Per the daily cash log maintained throughout several years past and ongoing, the total patient cash received was $27,361,885 a percentage difference of 0.7%. The financial report has less than the actual patient cash received, which also excluded the DSH and UPL payments. Admittedly this year was difficult in predicting what should be reserved since we had to beef up the utilization review department and we also brought in new providers during the year, which were not all credentialed at the time the fiscal year ended.

Continued

Significant Deficiency 2019-005

Condition/Criteria:	The August 2019 financial statements were not closed in the financial reporting system until October 2019.
Cause:	There was no policy in place at year-end to ensure that the monthly financial statements were closed in a timely manner.
Effect:	The System's financial statements could be materially misstated.
Recommendation:	We recommend implementing a policy to ensure the financial statements are reviewed and closed timely each month to ensure accurate reporting of the System's financial position and operations on a monthly and annual basis.
Views of responsible officials and planned corrective actions:	We had discussed this in April-May timeframe that we needed to close month end more timely in order to have time to review statements before they were disseminated. The two finance FTEs discussed earlier will help that process. One of the additions still had some duties related to physician credentialing. There will be a policy addressed to expedite the month end closing process.