

KEYSTONE RURAL HEALTH CENTER

AUDITED FINANCIAL REPORT

DECEMBER 31, 2012

CONTENTS

	Page
LIST OF REPORT DISTRIBUTION	1
INDEPENDENT AUDITOR'S REPORT	2-3
FINANCIAL STATEMENTS	
Balance sheets	4
Statements of operations	5
Statements of changes in net assets	6
Statements of cash flows	7 - 8
Notes to financial statements	9 - 20
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS	21
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	22 - 23
REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE AS REQUIRED BY OMB CIRCULAR A-133	24 - 25
SCHEDULE OF FINDINGS AND QUESTIONED COSTS	26 - 27
STATUS OF PRIOR AUDIT FINDINGS	28

KEYSTONE RURAL HEALTH CENTER

LIST OF REPORT DISTRIBUTION

DECEMBER 31, 2012

Employer Identification Number: 25-1546810

- 1 Report - Federal Audit Clearinghouse
Bureau of Census
1201 E. 10th Street
Jeffersonville, Indiana 47132
(Filed Electronically)

- 1 Report - Commonwealth of Pennsylvania
Office of the Budget/Bureau of Audits
Division of Subrecipient Audit Review
Verizon Tower - 6th Floor
303 Walnut Street
Harrisburg, Pennsylvania 17101-1830
(Filed Electronically)

- 1 Report - Rural Economic and Community Development
R.D. #3, Box 301
Mifflintown, Pennsylvania 17059
Attention: Leonard Queitzsch

- 1 Report - Family Health Council of Central Pennsylvania
Mr. Michael Dress
Suite 200
3461 Market Street
Camp Hill, Pennsylvania 17011-4441

- 1 Report - AIDSNET
2200 Avenue A, Suite 102
Bethlehem, Pennsylvania 18017



INDEPENDENT AUDITOR'S REPORT

Board of Directors
Keystone Rural Health Center
Chambersburg, Pennsylvania

Report on the Financial Statements

We have audited the accompanying financial statements of Keystone Rural Health Center (the Center), which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of operations, changes in net assets, 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 Center'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 Center'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.

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 Keystone Rural Health Center as of December 31, 2012 and 2011, and the results of its operations, changes in its net assets, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Directors
Keystone Rural Health Center

Emphasis-of-matter

As discussed in Note 2 to the consolidated financial statements, the Center adopted Financial Accounting Standards Board, Accounting Standards Update No. 2011-07, "Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities" (ASU # 2011-07). Our opinion is not modified with respect to that matter.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by *Office of Management and Budget Circular A-133, Audit of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 21, 2013 on our consideration of the Center'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 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 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 Center's internal control over financial reporting and compliance.

Smith Elliott Keorns & Company, LLC

Chambersburg, Pennsylvania
March 21, 2013

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Balance Sheets

December 31,	2012	2011
Assets		
Current assets		
Cash and cash equivalents	\$ 5,603,455	\$ 5,521,538
Accounts receivable - Patients (net of allowance for doubtful accounts of \$ 389,397 and \$ 463,258)	1,479,008	1,404,441
Grants receivable	76,750	567,323
Pharmacy accounts receivable	311,131	691,200
Accounts receivable - Affiliate	-	19,756
Estimated receivable under third-party agreements	647,847	-
Other receivables	442,040	137,252
Inventory	179,131	179,131
Prepaid expenses	92,520	183,360
	8,831,882	8,704,001
Assets limited as to use		
Cash	194,534	193,562
Investments	261,559	232,697
	456,093	426,259
Property and equipment, net	14,371,817	14,366,735
Other assets		
Investments - Other	49,309	49,309
Deferred financing costs (net of amortization of \$ 14,537 and \$ 13,499, respectively)	15,702	16,740
	65,011	66,049
Total assets	\$ 23,724,803	\$ 23,563,044

December 31,	2012	2011
Liabilities and net assets		
Current liabilities		
Current maturities of long-term debt	\$ 87,471	\$ 94,706
Accounts payable - Trade	288,477	557,251
Accounts payable - Construction	-	445,526
Accrued payroll	890,835	931,645
Payroll withholdings and taxes	20,990	100,533
Deferred compensation	304,937	525,939
Other liabilities	236,981	10,239
	1,829,691	2,665,839
Long-term liabilities		
Long-term debt	1,835,838	1,923,284
	1,835,838	1,923,284
Total liabilities	3,665,529	4,589,123
Net assets		
Unrestricted:		
Board designated	261,559	232,697
Undesignated	19,789,422	18,733,678
Temporarily restricted	8,293	7,546
Total net assets	20,059,274	18,973,921
Total liabilities and net assets	\$ 23,724,803	\$ 23,563,044

The Notes to the Financial Statements are an integral part of these financial statements.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Statements of Operations

Years Ended December 31,	2012	2011
Revenue, gains, and other support		
Net patient service revenue	\$ 18,972,649	\$ 19,893,968
Provision for bad debts	(398,607)	(631,983)
Net patient service revenue less provision for bad debts	18,574,042	19,261,985
Premium revenue	507,817	321,209
Other service revenue	4,444,946	4,581,299
Other revenue:		
Federal grants and support	2,889,705	2,840,099
State grants and support	114,523	132,282
Local grants and support	34,807	31,202
Other grant revenue	27,960	34,498
Grant funds released from restrictions	12,984	10,149
Total revenue, gains, and other support	26,606,784	27,212,723
Expenses		
Salaries and wages	16,305,780	18,526,622
Fringe benefits	2,938,858	2,932,371
Contracted services	1,072,249	711,374
Medical - Other	59,961	65,350
Pharmaceuticals	3,592,400	3,263,815
Materials, supplies, other	2,194,736	2,163,969
Rent - Facilities	313,405	534,171
Utilities	400,293	489,523
Insurance	43,683	154,624
Interest expense	91,354	98,953
Depreciation and amortization	1,179,199	926,072
Total expenses	28,191,918	29,866,844
Operating loss	(1,585,134)	(2,654,121)
Other income		
Contributions	264,096	266,479
Other revenue	118,659	363,319
Investment income	24,782	30,437
Community Benefit Grant - Affiliate	937,500	1,500,000
Electronic Health Records' Incentive	416,500	977,500
Gain (loss) on sale of assets	17,800	(26,249)
Total other income	1,779,337	3,111,486
Excess of revenues over expenses	194,203	457,365
Unrealized gain (loss) on investments	11,867	(9,470)
Federal grants - Capital projects	878,536	8,833,102
Increase in unrestricted net assets	\$ 1,084,606	\$ 9,280,997

The Notes to the Financial Statements are an integral part of these financial statements.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Statements of Changes in Net Assets

Year Ended December 31,	2012	2011
Unrestricted net assets		
Excess of revenues over expenses	\$ 194,203	\$ 457,365
Unrealized gain (loss) on investments	11,867	(9,470)
Federal grants - Capital projects	878,536	8,833,102
Increase in unrestricted net assets	1,084,606	9,280,997
Temporarily restricted net assets		
Partner Violence Prevention Grant	4,139	3,361
HIV/Outreach	9,592	-
Grant funds released from restrictions	(12,984)	(10,149)
Increase (decrease) in temporarily restricted net assets	747	(6,788)
Increase in net assets	1,085,353	9,274,209
Net assets, beginning	18,973,921	9,699,712
Net assets, ending	\$ 20,059,274	\$ 18,973,921

The Notes to the Financial Statements are an integral part of these financial statements.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Statements of Cash Flows

Years Ended December 31,	2012	2011
Cash flows from operating activities		
Change in net assets	\$ 1,085,353	\$ 9,274,209
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,179,199	926,072
Provision for bad debts	398,607	631,983
(Gain) loss on disposal of assets	(17,800)	26,249
Unrealized (gain) loss on investments	(11,867)	9,470
(Increase) decrease in:		
Patient accounts receivable	(473,174)	(585,565)
Grants receivable	490,573	(224,355)
340b receivable	380,069	(104,312)
Estimated receivable - Third-party agreements	(647,847)	-
Other receivable	(304,788)	27,459
A/R Affiliate	19,756	68,626
Inventory	-	(179,131)
Prepaid expenses	90,840	(28,300)
Increase (decrease) in:		
Accounts payable	(268,774)	334,202
Accrued expenses and withholdings	(120,353)	52,049
Other liabilities	226,742	6,239
A/P Affiliate	-	(60,222)
Estimated payments - Third-party agreements	-	(107,236)
Deferred compensation	(221,002)	370,659
Grants restricted to capital projects	(878,536)	(8,833,102)
Net cash provided by operating activities	926,998	1,604,994
Cash flows from investing activities		
Deposits to restricted cash reserve accounts	(972)	(1,669)
Purchase of investments	(158,185)	(48,790)
Proceeds from sale of investments	141,190	29,849
Purchase of property and equipment	(1,294,243)	(9,101,228)
Proceeds from disposal of fixed assets	128,800	-
Net cash used by investing activities	(1,183,410)	(9,121,838)

The Notes to the Financial Statements are an integral part of these financial statements.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Statements of Cash Flows (Continued)

Years Ended December 31,	2012	2011
Cash flows from financing activities		
Grants restricted for capital projects	\$ 878,536	\$ 8,833,102
Payments of construction payables	(445,526)	(208,480)
Payments on capital lease obligations	-	(3,037)
Payments on long-term debt	(94,681)	(159,146)
Net cash provided by financing activities	338,329	8,462,439
Net increase in cash and cash equivalents	81,917	945,595
Cash and cash equivalents, beginning	5,521,538	4,575,943
Cash and cash equivalents, ending	\$ 5,603,455	\$ 5,521,538
Supplemental disclosure of cash flow information		
Cash paid for interest	\$ 91,354	\$ 98,953

The Notes to the Financial Statements are an integral part of these financial statements.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

1. Summary of Significant Accounting Policies

Nature of Operations: Keystone Rural Health Center (the "Center") is a community health center formed for the purpose of providing, coordinating, and delivering health and human care services to individuals presenting themselves to the Center. The Center provides a broad range of services, which includes primary care, dental, obstetrics and gynecology, pediatrics, cardiology, and mental health. The Center also provides medical services to the local migrant farm worker population. The service area encompasses South-Central Pennsylvania. The Center grants credit without collateral to patients not covered by Medicare, Medical Assistance, or other commercial payors.

In 2003, Keystone Physician Services (a nonprofit corporation) was organized for the purpose of developing and operating a cardiology practice. The sole member of this organization, controlling the appointment and removal of the Board of Directors and approval of annual operating and capital budgets, is Keystone Rural Health Center. On January 1, 2011, all of the assets, liabilities, and operations of Keystone Physician Services were transferred to its parent company, Keystone Rural Health Center. Keystone Physician Services continues to exist as an inactive entity.

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to estimates of the allowance for doubtful accounts and amounts receivable or payable under the third party contractual agreements, which are based on historical collection rates and analysis of specific third party receivables and prior cost report settlement information. Consequently, these estimates may change in the near term. The amount of the change that is reasonably possible cannot be determined.

Donor Restrictions: The Center reports gifts of cash and other assets as restricted support if they received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statements of operations as net assets released from restrictions. When long-lived assets are placed in service, thus satisfying purpose restrictions, the amount is included as a change in net assets, restricted, and unrestricted. Donor-restricted contributions whose restrictions are met within the same year as received are reflected as unrestricted contributions in the accompanying financial statements.

The Center reports gifts of equipment (or other long-lived assets) as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Center reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

1. Summary of Significant Accounting Policies (Continued)

Accounts Receivable: Accounts receivable – Patients, are written off when management determines, based upon prior experience, collection history, or contractual agreements, that an account is no longer collectible. Accounts that are over 30 days old are typically considered past due. Management does provide an allowance for doubtful accounts, which is based upon historical collection rates and analysis of specific third-party receivables.

Investments: Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair value in the balance sheet. Unrealized gains and losses are included in the change in net assets. Investments – Other are accounted for using the cost method. (See Note 4)

Property and Equipment: Property and equipment is stated at cost. The Center capitalizes fixed assets in excess of \$ 2,500. Depreciation is provided on straight-line basis based upon the estimated useful lives of the assets as follows:

Buildings	10 - 40 years
Leasehold improvements	5 - 20 years
Medical and dental equipment	3 - 20 years
Furniture and fixtures	3 - 20 years

Deferred Financing Costs: Deferred financing costs are being amortized over the life of the U.S. Department of Agriculture (USDA) loans of 30 years. The amortization expense was \$ 1,038 for 2012 and 2011, respectively.

Temporarily Restricted Net Assets: Temporarily restricted net assets are those whose use by the Center has been limited by donors to a specific time period or purpose.

Net Patient Service Revenue: Net patient service revenue is reported at the estimated net realizable amount 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 the future periods as final settlements are determined.

Deferred Compensation: Deferred compensation represents physician incentive payments earned but not yet paid.

Premium Revenue: Keystone Rural Health Center has agreements with various Health Maintenance Organizations (HMOs) to provide medical service to subscribing participants. Under these agreements, the Center receives monthly capitation payments based on the number of each HMO's participants, regardless of service actually performed by the Center. In addition, the HMOs make fee-for-service payments to the Center for certain covered services based upon discounted fee schedules.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

1. Summary of Significant Accounting Policies (Continued)

Charity Care: The Center has a policy of providing charity care to patients who are unable to pay. The following describes the Center's calculation for estimating the annual cost of providing charity care.

- The Center calculates a cost per encounter.
- The cost per encounter over the reimbursement rate per encounter for Medicare and Medicaid are multiplied by the allocated encounters for each respective payor to determine a portion of charity care costs.
- In addition, the Center records the total cost of operating and providing care to the migrant population as a component of charity care costs.

The Center's estimated annual cost of providing charity care for the years ending December 31, 2012 and 2011 were \$ 3,119,527 and \$ 4,378,005, respectively. Contributions and grant income received to offset the cost of charity care for the years ending December 31, 2012 and 2011 were \$ 2,623,738 and \$ 2,588,949, respectively.

The amount of charges for services and supplies furnished under the community service criteria calculations as defined in the Institutions of Purely Public Charity Act aggregated approximately \$ 4,517,102 and \$ 5,891,416 in 2012 and 2011, respectively.

Tax-Exempt Status: Keystone Rural Health Center and Keystone Physician Services, (The "Organization"), are nonprofit corporations organized under the provisions of the non-profit laws of the Commonwealth of Pennsylvania. The organizations are described in Section 501(c)(3) of the Internal Revenue Code and are exempt from federal income taxes on related income pursuant to Section 509(a) of the code.

Generally accepted accounting principles require organizations to disclose significant tax positions that are subject to uncertainty about the merits of the position taken or the amount of the position that may ultimately be sustained upon examination by the taxing authorities. The effects of tax positions are recognized in the financial statements if, in the opinion of management, the tax position would more likely than not be sustained upon an examination by the taxing authorities, including the resolution of any applicable appeals or litigations. The Organization's most significant tax position is that they are exempt from payment of federal and state income taxes. Accordingly, the Organization has not reported any income tax expense in the statements of operations and changes in net assets for the years ended December 31, 2012 and 2011. The Organization has not recorded liabilities for income taxes or unrecognized income tax benefits in the balance sheets as of December 31, 2012 and 2011. The tax years subsequent to 2008 are subject to examination by federal, state, and local taxing authorities.

Malpractice Insurance: The Center has an occurrence policy, which covers malpractice claims reported to the insurance carrier during and after the policy term. This coverage is provided under the Federal Tort Claims Act.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

2. Adoption of New Accounting Standard

During 2012, the Center adopted Accounting Standards Update No. 2011-07, "Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities" (ASU # 2011-07). The objective of ASU # 2011-07 is to provide financial statement users with greater transparency about a health care entity's net patient service revenue and the related allowance for doubtful accounts. The new standard requires enhanced disclosure of patient service revenue and the changes in the allowance for uncollectible patient accounts receivable. The most significant change required by ASU # 2011-07 is the classification of the provision for bad debts associated with patient service revenue from an operating expense to a deduction from net patient service revenue. The Center has adopted the provisions of ASU # 2011-07 for the year ended December 31, 2012. The financial statements for the year ended December 31, 2011 have been restated to conform to the new requirements of ASU # 2011-07.

3. Assets Limited to Use

Assets limited to use is comprised of the following amounts and purposes at December 31, 2012 and 2011, respectively:

	2012	2011
Cash - USDA Reserve	\$ 194,534	\$ 193,562
Investments - Board Designated for future development	261,559	232,697
	\$ 456,093	\$ 426,259

4. Investments

The composition of investments in the Board designated investments (see Note 3) at December 31, 2012 and 2011 is set forth in the following schedule:

	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Cash and cash equivalents	\$ 13,138	\$ 13,138	\$ 15,052	\$ 15,052
Fixed income	87,542	92,911	85,259	89,044
Equities	125,616	155,510	106,572	128,601
	\$ 226,296	\$ 261,559	\$ 206,883	\$ 232,697

Investments – Other consist of an investment in Central Pennsylvania Physicians Risk Retention Group Inc. in order to obtain malpractice insurance coverage for Keystone Physician Services and its employed physicians, as well as an investment in Value Drug to support purchases at Keystone Pharmacy. These investments are accounted for using the cost method since market value is not readily available. The total investment at both December 31, 2012 and 2011 was \$ 49,309.

Investment income consists of interest, dividends, and realized gains and (losses) earned on investments and cash accounts.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

5. **Temporarily Restricted Net Assets** Temporary restricted net assets consist of the following at December 31, 2012 and 2011:

	2012	2011
PA Forum Emergency Preparedness	\$ 2,125	\$ 7,546
HIV/Outreach	6,168	-
	\$ 8,293	\$ 7,546

Temporarily net assets released from restrictions during each year were:

	2012	2011
PA Forum Emergency Preparedness	\$ 5,421	\$ 6,788
Partner Violence Prevention Grants	4,139	3,361
HIV/Outreach	3,424	-
	\$ 12,984	\$ 10,149

6. **Net Patient Service Revenue** The Center has agreements with third-party payors that provide for payments to the Center at amounts different from its established rates. Revenues received under cost reimbursement agreements with Medicare for medical services are based upon the Center's cost per patient encounter. Interim rates are established and paid throughout the year with a final settlement determined after the Center files its annual cost report for these services. Payment for the Commonwealth of Pennsylvania Department of Public Welfare for Medical and Dental Services are based on a perspective payment system.

The Center's patient utilization under these agreements for the years ended December 31 2012 and 2011, follows:

	Net Patient Service Revenue		Patients	
	2012	2011	2012	2011
Medicare	9.9%	18.2%	9.9%	13.1%
Medical Assistance	40.2%	35.4%	23.4%	21.7%
Commercial	41.0%	36.4%	48.0%	44.7%
Self-pay	8.9%	10.0%	18.7%	20.5%
	100.0%	100.0%	100.0%	100.0%

The Center's major payor sources consist of the Medicare, Medicaid, commercial insurance programs, private pay individuals and Medicare. Net patient service revenue, net of contractual and charity care allowances provided (but before the provision for bad debts), recognized in the statements of operations for the years ended December 31, 2012 and 2011 from these major payor sources is as follows:

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

6. Net Patient Service Revenue (Continued)

	2012				Total
	Medicaid	Medicare	Commercial	Self-Pay	
Net patient service revenue	\$ 7,627,005	\$ 1,878,292	\$ 7,778,786	\$ 1,688,566	\$ 18,972,649
	2011				Total
	Medicaid	Medicare	Commercial	Self-Pay	
Net patient service revenue	\$ 7,042,465	\$ 3,620,702	\$ 7,241,404	\$ 1,989,397	\$ 19,893,968

The change in the allowance for doubtful accounts for 2012 and 2011 is as follows:

	2012	2011
Allowance for doubtful accounts at January 1	\$ 463,258	\$ 427,404
Provision for bad debts	398,607	631,983
Write off of bad debts	(472,468)	(596,129)
Allowance for doubtful accounts at December 31	\$ 389,397	\$ 463,258

7. Grant Revenue

Grant revenue for the years ended December 31, 2012 and 2011 is comprised of the following:

	2012	2011
Federal grants and support:		
Operating grants		
Community Health Centers and Migrant Health Centers Grant Awards	\$ 2,623,738	\$ 2,588,949
Outpatient Services with Respect to HIV Disease	265,967	251,150
Subtotal - Operating grants	2,889,705	2,840,099
Capital project grants		
ARRA funds - CIP	-	494,496
ARRA funds - FIP	878,536	8,338,606
Subtotal - Capital project grants	878,536	8,833,102
	\$ 3,768,241	\$ 11,673,201
State grants and support:		
State Aids Program	\$ 114,523	\$ 132,282
	\$ 114,523	\$ 132,282
Local grants and support:		
Miscellaneous dental grants	\$ 11,250	\$ 10,000
United Way	23,557	21,202
	\$ 34,807	\$ 31,202
Other grants and support:		
AIDSNET	\$ 27,960	\$ 34,498
	\$ 27,960	\$ 34,498

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

8.	Estimated Amounts Under Third-Party Agreements	Estimated payables under third-party agreements consist of the following at December 31, 2012 and 2011:	2012	2011
		Medical Assistance estimated wrap settlements	\$ 647,847	\$ -
			\$ 647,847	\$ -

9.	Property and Equipment	The summary of property and equipment at December 31, 2012 and 2011 follows:	2012	2011
		Land	\$ 557,324	\$ 557,324
		Buildings	11,730,597	11,489,386
		Leasehold improvements	337,121	27,855
		Computer software and equipment	2,491,817	2,038,043
		Medical and dental equipment	1,859,718	1,855,718
		Furniture and fixtures	663,682	646,297
		Construction in progress	28,887	17,416
			17,669,146	16,632,039
		Less accumulated depreciation	(3,297,329)	(2,265,304)
			\$ 14,371,817	\$ 14,366,735

Depreciation expense for 2012 and 2011 was \$ 1,178,161 and \$ 925,034, respectively.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

10. Notes Payable and Long-term Debt

Notes payable balances at December 31, 2012 and 2011 follows:

	2012	2011
Note payable, U.S. Dept. of Agriculture/RECD, due June 2028, monthly payments of \$ 9,569, interest of 4.75%, secured by real estate, personal property, and revenue	\$ 1,250,607	\$ 1,304,586
Note payable, U.S. Dept. of Agriculture/RECD, due June 2013, monthly payments of \$ 1,619, interest of 4.75%, secured by personal property and revenue	7,719	26,299
Note payable, U.S. Dept. of Agriculture/RECD, due September 2029, monthly payments of \$ 1,436, interest of 4.75%, secured by real estate	181,255	189,662
Note payable, U.S. Dept. of Agriculture/RECD, due April 2034, monthly payments of \$ 2,879, interest of 4.25%, secured by real estate, personal property, and revenue	483,728	497,443
	<u>1,923,309</u>	<u>2,017,990</u>
Less current maturities	(87,471)	(94,706)
	<u>\$ 1,835,838</u>	<u>\$ 1,923,284</u>

The future payments on long-term debt for of the next five years and thereafter is as follows:

2013	\$ 87,471
2014	83,526
2015	87,503
2016	91,671
2017	96,037
Thereafter	<u>1,477,101</u>
	<u>\$ 1,923,309</u>

The loans with the U.S. Department of Agriculture contain various covenants such as maintaining adequate insurance coverage, charging enough to cover debt service, and funding various reserve accounts.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

- 10. Notes Payable and Long-term Debt (Continued)**
- Under the balance sheet caption "assets limited as to use", cash includes reserves required by the loan agreements with the U.S. Department of Agriculture. The balance of these reserves at December 31, 2012 and 2011 amounted to \$ 194,534 and \$ 193,562 respectively.
- There are no prepayment penalties associated with any of the loans.
- Total interest costs for 2012 and 2011 were \$ 91,354 and \$ 98,953, respectively.
- 11. Affiliated Organization**
- The Center's bylaws allow for an association with Summit Health. By authority set forth in the Center's bylaws, Keystone's Board selects the majority of the directors and Summit Health may nominate a minority. All board member selections are in accordance with Section 330 of the Public Health Act and related regulations.
- During 2007, the Center and its subsidiary experienced negative cash flow and profitability. To ensure the continued operations of the Center and its programs to the medically underserved population at its various sites, the Center requested assistance from Summit Health. Summit Health awarded a Community Benefit Grant to the Center and its subsidiary in response. Operationally, the Community Benefit Grant is to support the otherwise uncompensated costs in providing services, to maintain the existing level of physician and health care services, and patient access thereto. In addition, the Community Benefit Grant should enhance the financial stability of the Center with a goal of meeting the suggested Federally Qualified Health Center guideline requirement for ninety days cash on hand and other purposes Summit Health and the Center mutually agree. The term of the original grant was for three years commencing on October 1, 2007 and ending September 30, 2010.
- On September 20, 2010, the Community Benefit Grant was renewed. The term of the new grant was for 10 years commencing January 1, 2011 and ending December 31, 2021. The financial commitment of Summit Health was \$1.5 million per grant year to cover anticipated operating deficits. The grant does have various conditions covering the availability of these funds to the Center. The funding for 2012 and 2011 was \$ 937,500 and \$1,500,000, respectively. Subsequent to year end this agreement was amended. Please refer to Note 17, Subsequent Events, for details of the amended grant agreement entered into on March 18, 2013.
- As part of the Community Benefit Grant, Summit Health, at its sole discretion and financial obligation, has made available an individual to serve as a financial consultant and liaison between the Center and Summit Health. This individual is to assure compliance with the Community Benefit agreement, assist with developing and implementing operating and capital budgets, business plans, financial statements, and assist with the management of cash flow. This contributed service is recorded in contributions and salaries of the Center, at a value of \$ 250,000 for each of the years ending December 31, 2012 and 2011. This benefit ended December 31, 2012.
- Should the Community Benefit Grant be discontinued, this could have a negative financial impact upon the Center.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

11. Affiliated Organization (Continued)

The balance sheet at December 31, 2011 contained various affiliated Organization receivables. The details of which are as follows:

Receivables:

	2012	2011
Summit Health:		
Medical Director fees	\$ -	\$ 5,000
Services at Waynesboro Hospital	-	4,525
FCIC Office Lease agreement	-	10,231
	<u>\$ -</u>	<u>\$ 19,756</u>

The statements of operations for the years ended December 31, 2012 and 2011 contain affiliated organization grant revenue. The detail is as follows:

	2012	2011
Summit Health:		
Community Benefit Grant - Cardiology	\$ 187,500	\$ -
Community Benefit Grant - Keystone operations	750,000	1,500,000
	<u>\$ 937,500</u>	<u>\$ 1,500,000</u>

Summit Physician Services, an affiliate of Summit Health, leased space, equipment and obtained certain services from the Center. In exchange for these items, the Center received \$ 25,249 in 2012 and \$ 224,503 in 2011, which is included in other revenue in the statements of operations.

12. Operating Lease Commitments

Leases that do not meet the criteria for capitalization are classified as operating leases with rent charged to operations as incurred.

The Center currently leases office space at several locations and a parking lot.

Total commitments under long-term operating leases for the next five years are as follows:

2013	\$ 156,864
2014	156,864
2015	156,864
2016	84,612
2017	-

Total rental expense for 2012 and 2011 was \$ 313,405 and \$ 534,171, respectively.

13. Concentration of Credit Risk

The Center maintains its funds at several financial institutions with a majority of these funds being maintained in repurchase agreements.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

14. Functional Expense Allocation

The allocation by total program services and general and administrative is as follows:

	2012	2011
Program services	\$ 25,054,719	\$ 26,480,207
General and administrative	3,137,199	3,386,637
	\$ 28,191,918	\$ 29,866,844

15. Fair Value Measurements

Fair Value Measurement: Generally accepted accounting principles define fair value, describe a framework for measuring fair value, and require disclosure about fair value measurements. The established framework includes a three-level hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the assets and liabilities fall within different levels of the hierarchy, the classification is based on the lowest level input that is significant to the fair value measurement of the asset or liability. Classification of assets and liabilities within the hierarchy considers the markets in which the assets are traded and the reliability and transparency of the assumptions used to determine fair value. The hierarchy requires the use of observable market data when available. The levels of the hierarchy and those investments included in each are as follows:

Level 1: Represented by quoted prices available in an active market. Level 1 securities include highly liquid government bonds, treasury securities, mortgage products, and exchange traded equities.

Level 2: Represented by assets and liabilities similar to Level 1 where quoted prices are not available, but are observable, directly or indirectly through corroboration with observable market data, such as quoted prices for similar securities and quoted prices in inactive markets and estimated using pricing models or discounted cash flows. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions, and certain corporate and asset backed securities.

Level 3: Represented by financial instruments where there is limited activity or unobservable market prices and pricing models significant to determining the fair value measurement including the reporting entity's own assumptions about the market risk. Level 3 securities would include hedge funds, private equity securities, and internally developed values.

The following valuation techniques were used to measure fair value of assets in the table below on a recurring basis:

Equity and Fixed Income Securities and Mutual Funds – Fair value of equity and fixed income securities/mutual funds was based on quoted market prices.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Notes to the Financial Statements

15. **Fair Value Measurements (Continued)** Fair value assets measured on a recurring basis at December 31, 2012 and 2011 are as follows:

2012	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	\$ 13,138	\$ 13,138	\$ -	\$ -
Fixed income funds:				
Intermediate term bond fund	65,352	-	65,352	-
Short term bond fund	27,559	-	27,559	-
Mutual funds:				
Large cap fund	104,078	-	104,078	-
Mid cap fund	21,358	-	21,358	-
Small cap fund	15,445	-	15,445	-
Foreign large cap fund	14,629	-	14,629	-
	\$ 261,559	\$ 13,138	\$ 248,421	\$ -

2011	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	\$ 15,052	\$ 15,052	\$ -	\$ -
Fixed income funds:				
Intermediate term bond fund	62,728	-	62,728	-
Short term bond fund	26,315	-	26,315	-
Mutual funds:				
Large cap fund	87,222	-	87,222	-
Mid cap fund	16,416	-	16,416	-
Small cap fund	12,644	-	12,644	-
Foreign large cap fund	12,320	-	12,320	-
	\$ 232,697	\$ 15,052	\$ 217,645	\$ -

16. **340(B) Federal Drug Pricing Program** The 340(B) Federal Drug Pricing Program resulted from the Veterans Health Care Act of 1992. This program limits the cost of covered outpatient drugs to the Center's patients who have met specific eligibility requirements. As of December 31, 2012 and 2011, the Center received \$ 3,730,446 and \$ 3,701,560 in revenues, respectively, from the 340(B) Drug Pricing Program. This amount is recorded in the statements of operations under other service revenue.

17. **Subsequent Events** The Center has evaluated events and transactions subsequent to December 31, 2012 through March 21, 2013, the date these financial statements were available to be issued.

On March 18, 2013, Summit Health amended the Community Benefit Grant. Summit Health will award Keystone Rural Health Center up to \$750,000 annually, for eight consecutive years. For each grant year, the Community Benefit Funds will be distributed to the Center in four equal payments.

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Schedule of Expenditures of Federal Awards

Year Ended December 31, 2012

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditures
U.S. Department of Health and Human Services			
Community/Migrant Health Centers Program	93.224	N/A	\$ 2,623,738
ARRA - Facility Improvement Program	93.703	N/A	878,536
Ryan White HIV/AIDS: Early Intervention Services	93.918	N/A	265,967
Passed through the Family Health Council of Central Pennsylvania: HIV Care Formula Grant	93.917	SAP 4100039370	<u>70,340</u>
Subtotal - U.S. Department of Health Human Services			<u>3,838,581</u>
U.S. Department of Housing and Urban Development			
Passed through the Family Health Council of Central Pennsylvania: Housing Opportunities for Persons with AIDS	14.241	SAP 4100039370	<u>44,183</u>
Total			<u><u>\$ 3,882,764</u></u>

Notes to Schedule of Expenditures of Federal Awards

Note 1. Basis of Presentation

The schedule of expenditures of federal awards includes the federal grant activity of Keystone Rural Health Center and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic consolidated financial statements.

Note 2. Community Facilities Loan Program

The community facilities loan program is not included in this schedule as it was determined to not have any on-going compliance requirements.



Smith Elliott, Kearns & Company, LLC
Certified Public Accountants & Consultants

**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

Board of Directors
Keystone Rural Health Center
Chambersburg, Pennsylvania

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 Keystone Rural Health Center (the Center) which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of operations, change in net assets, and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated March 21, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Center'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 Center's internal control. Accordingly, we do not express an opinion on the effectiveness of the Center's internal control.

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 Center's financial statements will not be prevented, or detected and corrected on a timely basis. *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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as items 2012-01 and 2012-02 that we consider to be significant deficiencies.

Board of Directors
Keystone Rural Health Center

Compliance and other Matters

As part of obtaining reasonable assurance about whether the Center's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated 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*.

The Center's Response to Findings

The Center's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Center's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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 result of that testing, and not to provide an opinion on the effectiveness of the Center'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 Center's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Smith Elliott Thomas, Company, LLC

Chambersburg, Pennsylvania
March 21, 2013



**REPORT ON COMPLIANCE FOR EACH MAJOR
FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE
AS REQUIRED BY OMB CIRCULAR A-133**

Board of Directors
Keystone Rural Health Center
Chambersburg, Pennsylvania

Report on Compliance for Each Major Federal Program

We have audited Keystone Rural Health Center's (the Center's) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Center's major federal programs for the year ended December 31, 2012. The Center's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Center's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Center's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Center's compliance.

Opinion on Each Major Federal Program

In our opinion, the Center complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Board of Directors
Keystone Rural Health Center

Report on Internal Control Over Compliance

Management of the Center is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Center's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of the Center's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect, and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Smith Elliott Hearn & Company, LLC

Chambersburg, Pennsylvania
March 21, 2013

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Schedule of Findings and Questioned Costs

A. Summary of Auditor's Results

1. The auditor's report expresses an unqualified opinion on the financial statements of Keystone Rural Health Center.
2. Two significant deficiencies were disclosed during the audit of the financial statements and are reported in the 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. No material weaknesses are reported.
3. No instances of noncompliance material to the financial statements of Keystone Rural Health Center, which would be required to be reported in accordance with Government Auditing Standards, were disclosed during the audit.
4. No significant deficiencies in internal control over major federal award programs are reported in the Report on Compliance For Each Major Federal Program and Report on Internal Control over Compliance As Required by OMB Circular A-133. No material weaknesses are reported.
5. The auditor's report on compliance for the major federal award programs for Keystone Rural Health Center expresses an unmodified opinion on all major federal programs.
6. There were no audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 as reported in the schedule.
7. The programs tested as major programs:
Community Health Centers (CFDA Number 93.224)
ARRA – Facilities Improvement Program (CFDA Number 93.703)
8. The threshold for distinguishing Type A and B programs was \$ 300,000.
9. Keystone Rural Health Center was determined to be a low-risk auditee.

B. Findings - Financial Statements Audit

Significant Deficiency

2012-01 Cardiology Billing

Criteria: The individual responsible for billing for the Cardiology hospital visits should be billing based on the procedures that the cardiologists have notated on the encounter forms. Any discrepancies between procedures billed and procedures notated on encounter forms should be communicated to the physician, and approved by the department and billing supervisor.

Condition: Procedure levels different from what was notated on encounter forms were billed without approval from the department and billing supervisor.

Effect: There is the potential for patients to be billed for procedures that were not performed by the physician or for the incorrect procedure.

Cause: The cause is due to lack of controls within the Cardiology department for approval of any changes being made while billing for patient procedures.

KEYSTONE RURAL HEALTH CENTER

d/b/a KEYSTONE HEALTH

Schedule of Findings and Questioned Costs

Recommendations: We recommend that the individual(s) responsible for Cardiology department billing consult with the physicians when billing changes are considered necessary. Also, any changes should be approved by the department supervisor and billing supervisor.

Auditee's Response: Employees responsible for Cardiology department billings will consult with the physician prior to making any changes to procedures notated on the encounter forms. All changes will be documented and approved by the department supervisor and billing supervisor.

Significant Deficiency

2012-02 Inventory

Criteria: Inventory should be counted and valued as part of the year-end financial statement closing process.

Condition: No inventory count to ascertain the correct value was conducted at year end December 31, 2012.

Effect: The valuation of inventory could be misstated at year end.

Cause: Management did not consider any changes in the value of inventory to be material to the financial statements.

Recommendations: We recommend a formal process for counting and valuing inventory at year end be implemented to assure the stated value of inventory is accurate.

Auditee's Response: We agree with the auditor's recommendation and will implement a process for the year ending December 31, 2013.

Findings and Questioned Costs - Major Federal Award Programs Audit

None

KEYSTONE RURAL HEALTH CENTER
d/b/a KEYSTONE HEALTH
Status of Prior Audit Findings



There were no findings in 2011.



Corrective Action Plan

April 1, 2013

Department of Health and Human Services

Keystone Rural Health Center respectfully submits the following corrective action plan for the year ended December 31, 2012.

Name and address of independent public accounting Firm:

Smith Elliott Kearns & Company, LLC
804 Wayne Avenue
Chambersburg, Pa 17201

Audit Period:

Year ended December 31, 2013

The findings from the December 31, 2012 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

Findings – Financial Statements Audit

Significant Deficiencies:

2012-01 Cardiology Billing

Recommendation: We recommend that the individual(s) responsible for Cardiology department billing consult with the physicians when billing changes are considered necessary. Also, any changes should be approved by the department supervisor and billing supervisor.

Action Taken: Employees responsible for Cardiology department billings will consult with the physician prior to making any changes to procedures notated on the encounter forms. All changes will be documented and approved by the department supervisor and billing supervisor.

Leading the way to a healthier community

2012-02 Inventory

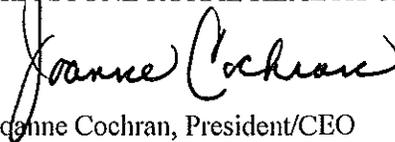
Recommendations: We recommend a formal process for counting and valuing inventory at year end be implemented to assure the stated value of inventory is accurate.

Action Taken: We agree with the auditor's recommendation and will implement a process for the year ending December 31, 2013.

Findings and Questioned Costs – Major Federal Award Programs

None

Sincerely,
KEYSTONE RURAL HEALTH CENTER



Joanne Cochran, President/CEO