

ARcare

Independent Auditor's Reports and Financial Statements

December 31, 2012 and 2011

ARcare
December 31, 2012 and 2011

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Independent Auditor's Report on Financial Statements and Supplementary Information

Board of Directors
ARcare
Augusta, Arkansas

Report on the Financial Statements

We have audited the accompanying financial statements of ARcare (the Organization), which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of operations and 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 entity'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 entity'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 ARcare as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information, including the schedules of expenditures of federal required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, as listed in the table of contents, 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. The 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.

Report on Other Legal and Regulatory Requirements

In accordance with *Government Auditing Standards*, we also have issued our report dated March 26, 2013, on our consideration of the Organization's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

BKD, LLP

ARcare
Balance Sheets
December 31, 2012 and 2011

Assets

	<u>2012</u>	<u>2011</u>
Current Assets		
Cash and cash equivalents	\$ 9,471,043	\$ 5,905,493
Restricted cash	55,656	36,293
Short-term investments	-	2,503,265
Patient accounts receivable, net of allowance; 2012 – \$2,309,966; 2011 – \$1,519,228	1,272,691	885,428
Grants receivable	1,054,685	731,437
FQHC cost settlement receivable	497,977	468,715
Other receivable	390,808	236,541
Inventories	383,876	356,320
Prepaid expenses and other	<u>137,179</u>	<u>91,329</u>
Total current assets	<u>13,263,915</u>	<u>11,214,821</u>
Property and Equipment, at Cost		
Land	817,730	662,049
Buildings and leasehold improvements	12,056,670	8,691,227
Construction in progress	949,082	888,299
Equipment	<u>3,392,744</u>	<u>2,319,065</u>
	17,216,226	12,560,640
Less accumulated depreciation	<u>3,255,287</u>	<u>2,623,232</u>
	<u>13,960,939</u>	<u>9,937,408</u>
Total assets	<u>\$ 27,224,854</u>	<u>\$ 21,152,229</u>

Liabilities and Unrestricted Net Assets

Current Liabilities		
Current maturities of long-term debt	\$ 1,405,490	\$ 1,270,449
Deferred grant revenue	90,614	64,031
Accounts payable	311,331	538,082
Accrued liabilities	<u>1,221,920</u>	<u>1,058,077</u>
Total current liabilities	3,029,355	2,930,639
Long-term Debt		
	<u>4,246,751</u>	<u>2,823,549</u>
Total liabilities	<u>7,276,106</u>	<u>5,754,188</u>
Net Assets		
Unrestricted	14,961,561	11,548,531
Unrestricted – board designated	<u>4,987,187</u>	<u>3,849,510</u>
Total net assets	<u>19,948,748</u>	<u>15,398,041</u>
Total liabilities and net assets	<u>\$ 27,224,854</u>	<u>\$ 21,152,229</u>

ARcare
Statements of Operations and Changes in Net Assets
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Unrestricted Revenues, Gains and Other Support		
Patient service revenue (net of contractual allowances and discounts)	\$ 12,813,597	\$ 9,451,771
Provision for uncollectible accounts	<u>(1,145,087)</u>	<u>(671,509)</u>
Net patient service revenue less provision for uncollectible accounts	11,668,510	8,780,262
Federal grant funds	9,213,214	8,793,070
State grant funds	1,299,073	1,400,214
Private grant funds	950,786	694,888
Baptist Health grant funds	876,000	876,000
Other revenue (net)	2,430,608	1,749,746
In-kind revenue	<u>1,564,139</u>	<u>3,292,595</u>
 Total unrestricted revenues, gains and other support	 <u>28,002,330</u>	 <u>25,586,775</u>
 Expenses		
Salaries and wages	12,121,406	10,931,043
Employee benefits	2,672,660	2,348,547
Contractual services	1,013,796	1,118,239
Depreciation	718,809	606,823
Interest	228,895	200,168
Supplies	1,457,190	1,119,556
Facilities rent	410,805	326,357
Travel	577,338	567,366
In-kind expense	1,564,139	3,292,595
Utilities	842,401	758,521
Repairs and maintenance	180,044	160,906
Insurance	248,987	176,405
Other	<u>1,666,069</u>	<u>1,534,237</u>
 Total expenses	 <u>23,702,539</u>	 <u>23,140,763</u>
 Excess of Revenues Over Expenses and Changes in Net Assets	 4,299,791	 2,446,012
 Grants for acquisition of property and equipment	 <u>250,916</u>	 <u>-</u>
 Increase in Unrestricted Net Assets	 4,550,707	 2,446,012
 Unrestricted Net Assets, Beginning of Year	 <u>15,398,041</u>	 <u>12,952,029</u>
 Unrestricted Net Assets, End of Year	 <u>\$ 19,948,748</u>	 <u>\$ 15,398,041</u>

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Statements of Cash Flows
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Operating Activities		
Change in unrestricted net assets	\$ 4,550,707	\$ 2,446,012
Items not requiring cash		
Depreciation	718,809	606,823
Loss on disposal of capital assets	111,533	5,643
Changes in		
Receivables	(894,040)	(42,886)
Prepaid expenses	(45,850)	(22,716)
Inventories	(27,556)	85,506
Accounts payable	(226,751)	63,682
Accrued expenses	163,843	(55,488)
Deferred grant revenues	26,583	353
	<u>4,377,278</u>	<u>3,086,929</u>
Net cash provided by operating activities		
Investing Activities		
Capital expenditures	(4,853,873)	(2,053,218)
Purchase of investments	2,503,265	(29,579)
	<u>(2,350,608)</u>	<u>(2,082,797)</u>
Net cash used in investing activities		
Financing Activities		
Principal payments on debt and capital lease obligations	(250,820)	(305,564)
Proceeds from issuance of long-term debt	1,809,063	540,000
	<u>1,558,243</u>	<u>234,436</u>
Net cash provided by financing activities		
Increase in Cash and Cash Equivalents	3,584,913	1,238,568
Cash and Cash Equivalents, Beginning of Year	<u>5,941,786</u>	<u>4,703,218</u>
Cash and Cash Equivalents, End of Year	<u>\$ 9,526,699</u>	<u>\$ 5,941,786</u>
Reconciliation of Cash to the Balance Sheet		
Cash and cash equivalents	\$ 9,471,043	\$ 5,905,493
Restricted cash	55,656	36,293
	<u>\$ 9,526,699</u>	<u>\$ 5,941,786</u>
Total cash and cash equivalents		
Supplemental Cash Flows Information		
Interest paid	\$ 228,895	\$ 200,168

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Notes to Financial Statements

December 31, 2012 and 2011

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

Nature of Operations

ARcare (the Organization) was created for nonprofit purposes to promote the general health of citizens in Augusta, Bald Knob, Batesville, Bentonville, Brinkley, Carlisle, Conway, Cotton Plant, Des Arc, El Dorado, England, Fayetteville, Forrest City, Fort Smith, Hazen, Heber Springs, Hot Springs, Jonesboro, Kensett, Lake City, Little Rock, McCrory, Melbourne, Mountain Home, Newport, Parkin, Searcy, Swifton, Texarkana, West Memphis, Wynne and surrounding communities in Arkansas. The Organization expanded operations in 2012 into Kentucky. Its principal objectives are to establish and maintain clinic facilities for the care of persons suffering from illness or disabilities, providing comprehensive services, including preventive care, and to carry on educational activities related to rendering care to the sick and promotion of health by educating the public. The primary sources of funds for operation are grants from the U.S. Department of Health and Human Services, the acceptance of which requires compliance with prescribed grant conditions and other special requirements, including the receipt of certain amounts of revenues from nonfederal sources. Additional operating funds are realized from a grant received from the Arkansas Department of Health, a grant received through an affiliation with Baptist Health and charges to patients. Under the terms of grant agreements, the Organization is subject to the uniform administrative requirements of the Office of Management and Budget Circular No. A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (the Circular). Accordingly, management policies and procedures are designed to be in compliance with the provisions of the Circular.

Use of Estimates

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

Cash and Cash Equivalents

The Organization considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2012 and 2011, cash equivalents consisted primarily of money markets and certificates of deposit.

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to \$250,000. At December 31, 2012, the Organization's exceeded federally insured limits by approximately \$8,600,000.

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Notes to Financial Statements

December 31, 2012 and 2011

Restricted Cash

Restricted cash includes cash deposits required as part of the Organization's loan agreements with the United States Department of Agriculture – Rural Development. The loan agreement requires the Organization to fund a cash reserve with \$286 in monthly deposits until the reserve accumulates to a minimum of \$33,720, which has been met since 2006. Under the terms of the agreement, the Organization can use the funds to make payments on the note or, with prior written approval, make improvements to the related real estate.

Investments and Investment Return

Investments in certificates of deposits, which totaled \$0 and \$2,503,265, at December 31, 2012 and 2011, respectively, are valued at cost, which approximates fair value. Investment return consists of interest earned.

Patient Accounts Receivable

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the Organization analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Organization analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely).

For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Organization records a significant provision for uncollectible accounts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or provided by policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Inventories

Supply inventories are stated at the lower of cost (determined on a first-in, first-out basis) or market. As of December 31, 2012 and 2011, inventories consisted of medical, laboratory, x-ray, dental and pharmaceutical supplies.

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Notes to Financial Statements
December 31, 2012 and 2011

Property and Equipment

Property and equipment are depreciated on a straight-line basis over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives.

The estimated useful lives for each major depreciable classification of property and equipment are as follows:

Buildings and leasehold improvements	40 years
Equipment	5 years

Property acquired with federal grant funds is considered owned by the Organization while used in the program for which it was purchased or in future authorized programs. In addition, the federal government has a reversionary interest in the property. The disposition of property purchased with federal grant funds, as well as any proceeds from its sale, are subject to federal regulation.

Long-Lived Asset Impairment

The Organization evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimate future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended December 31, 2012 and 2011.

Net Patient Service Revenue

The Organization recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, the Organization recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of the Organization's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Organization records a significant provision for uncollectible accounts related to uninsured patients in the period the services are provided. This provision for bad debts is presented on the statements of operations and changes in net assets as a component of net patient service revenue.

In accordance with grant requirements, the Organization provides care at amounts less than its established rates using sliding fee scale adjustments to patients who meet certain criteria. These adjustments are a component of net patient service revenue.

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Notes to Financial Statements

December 31, 2012 and 2011

Professional Liability Claims

The Organization recognizes an accrual for claim liabilities based on estimated ultimate losses and costs associated with settling claims and a receivable to reflect the estimated insurance recoveries, if any. Professional liability claims are described more fully in *Note 7*.

Income Taxes

The Organization is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the Organization is subject to federal income tax on any unrelated business taxable income.

The Organization files tax returns in the U.S. federal jurisdiction. With a few exceptions, the Organization is no longer subject to U.S. federal examinations by tax authorities for years before 2009.

Electronic Health Records Incentive Program

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible federally qualified health centers that demonstrate meaningful use of certified electronic health records technology (EHR). Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to six years based upon a statutory formula, as determined by the State, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs are contingent on the Organization continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the state, fiscal intermediary or Medicare Administrative Contractor. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Organization recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

During the year ended December 31, 2012, the Organization completed the first-year requirements under the Medicaid program for certain providers and has recorded revenue of approximately \$761,000, which is included in other revenue in the statements of operations.

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Notes to Financial Statements
December 31, 2012 and 2011

Compensated Absences

Employees receive between one and two days of accrued leave per month, which is available to be taken the next month. Any accrued leave not taken by the end of the year is carried forward to the next year. However, no employee may carry forward more than 20 days of annual leave to the subsequent year. The amount of accrued leave at December 31, 2012 and 2011, was \$415,665 and \$380,699, respectively, and is included in accrued liabilities in the financial statements.

Subsequent Events

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

Note 2: Net Patient Service Revenue

The Organization is approved as a Federally Qualified Health Center (FQHC) for both Medicare and Medicaid reimbursement purposes. The Organization has agreements with third-party payers that provide for payments to the Organization at amounts different from its established rates. These payment arrangements include:

Medicare. Covered FQHC services rendered to Medicare program beneficiaries are paid based on a cost reimbursement methodology. The Organization is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of an annual cost report by the Organization and audit thereof by the Medicare fiscal intermediary. Services not covered under the FQHC benefit are paid based on established fee schedules.

Medicaid. Covered FQHC services rendered to Medicaid program beneficiaries are paid based on a prospective reimbursement methodology. The Organization is reimbursed a set encounter rate for all services provided under the plan.

Approximately 77% and 80% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2012 and 2011, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

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Notes to Financial Statements
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Net patient service revenue consists of charges to patients and third-party payers adjusted for contractual adjustments and fee reductions due to the inability of the patient to pay. Components of net patient service revenue at December 31, 2012 and 2011, are as follows:

	<u>2012</u>	<u>2011</u>
Gross patient fees	\$ 16,970,429	\$ 12,919,936
Adjustments of gross patient fees		
Contractual adjustments	(439,659)	(156,804)
Sliding fee scale adjustments	(3,717,173)	(3,311,361)
Provision for uncollectible accounts	<u>(1,145,087)</u>	<u>(671,509)</u>
	<u>\$ 11,668,510</u>	<u>\$ 8,780,262</u>

Note 3: Concentrations of Credit Risk

The Organization grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer agreements. The mix of receivables from patients and third-party payers for the years ended December 31, 2012 and 2011, was as follows:

	<u>2012</u>	<u>2011</u>
Medicare	19 %	26 %
Medicaid	8	41
Other third-party payers	11	12
Patient fees	<u>62</u>	<u>21</u>
	<u>100 %</u>	<u>100 %</u>

Note 4: Grant and Contract Revenue

Grant revenues are recognized for financial statement purposes to the extent of allowable program expenditures. Grant proceeds were less than grant expenditures for certain grants, resulting in a grant receivable of \$1,054,685 and \$731,437 at December 31, 2012 and 2011, respectively. Additionally, grant proceeds have exceeded grant expenditures for certain grants, resulting in deferred grant revenue of \$90,614 and \$64,031 at December 31, 2012 and 2011, respectively.

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Notes to Financial Statements
December 31, 2012 and 2011

Note 5: Functional Expenses

Expenses incurred by the Organization, classified by functional categories, for the years ended December 31, 2012 and 2011, were as follows:

	2012	2011
Clinical services and related costs	\$ 20,669,714	\$ 18,178,449
Administrative and general	3,032,825	4,962,314
	\$ 23,702,539	\$ 23,140,763

Note 6: Nonmonetary Transactions

The Organization received in-kind contributions of \$1,564,139 and \$3,292,595 during the years ended December 31, 2012 and 2011, respectively. Contributions received in 2012 and 2011 consisted of donated medications through the Indicare and Care program.

Note 7: Professional Liability Claims

The U.S. Department of Health and Human Services has deemed the Organization and its participating providers covered under the *Federal Torts Claims Act* (FTCA) for damage for personal injury, including death, resulting from the performance of medical, surgical, dental and related functions. FTCA coverage is comparable to an occurrence policy without a monetary cap.

In 2012, the Organization adopted the provisions of Accounting Standards Update (ASU) 2010-24 *Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries*, which eliminates the practice of netting claim liabilities with expected insurance recoveries for balance sheet presentation. Claim liabilities are to be determined without consideration of insurance recoveries. Expected recoveries are presented separately. Prior to the adoption of ASU 2010-24, accounting principles generally accepted in the United States of America require a health care provider to accrue only an estimate of the malpractice claims cost for both reported claims and claims incurred but not reported where the risk of loss had not been transferred to a financially viable insurer. There was no impact of the ASU adoption to the Organization's financial statements.

Based upon the Organization's claim experience, no accrual has been made for the Organization's medical malpractice cost for the years ended December 31, 2012 and 2011. However, because of the risk in providing health care services, it is possible that an event has occurred which will be the basis of a future medical claim.

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Notes to Financial Statements
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Note 8: Long-term Debt

Long-term debt at December 31, 2012 and 2011, is summarized below:

	<u>2012</u>	<u>2011</u>
Note payable bank, due May 6, 2014; payable \$996 monthly, including interest at a variable rate (4.75% at December 31, 2012), secured by real estate.	\$ 103,680	\$ 110,451
Note payable bank, due May 1, 2024; payable \$1,185 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	135,309	144,931
Note payable bank, due January 31, 2019; payable \$939 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	62,096	71,134
Note payable bank, due September 25, 2022; payable \$1,360 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	77,939	91,409
Note payable bank, due September 24, 2022; payable \$1,747 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	100,231	117,539
Note payable bank, due July 12, 2014; payable \$1,101 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	8,619	21,301
Note payable bank, due December 17, 2017; payable \$2,732 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	98,626	127,535
Note payable United States Department of Agriculture, due July 5, 2030; payable \$2,810 monthly, including interest at 5%, secured by real estate.	393,564	407,233

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Notes to Financial Statements
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	2012	2011
Note payable United States Department of Agriculture, due May 1, 2027; payable \$1,596 monthly, including interest at 4.5%, secured by real estate.	\$ 199,109	\$ 209,057
Note payable bank, due on demand; if no demand; payable \$2,981 monthly, including interest at a variable rate (4.889% at December 31, 2012) with payment of balance due on November 3, 2013, secured by real estate.	464,822	476,060
Note payable bank, due February 28, 2023; payable \$2,364 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	196,576	221,302
Note payable City of Cabot, due October 13, 2012; payable \$54,353 in two annual installments, including interest at 5.75%, secured by real estate.	-	51,397
Note payable bank, due May 1, 2017; payable \$991 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	157,936	164,546
Note payable bank, due January 17, 2016; payable \$3,348 monthly, including interest at a variable rate (4.889% at December 31, 2012), secured by real estate.	481,585	497,718
Note payable bank, due January 10, 2017; payable \$60,000 in 5 annual payments, including interest at a variable rate (4.889% at December 31, 2012), secured by real estate.	1,500,000	-
Note payable SuccessEHS, due January 1, 2015; payable \$13,300 monthly, including interest at a variable rate (3.25% at December 31, 2012), secured by real estate.	309,063	-
Capital lease obligation on Jonesboro Clinic for approximately 25 years, including interest at 5.875%; expiring November 2034.	1,363,086	1,382,385
	5,652,241	4,093,998
Less current maturities	1,405,490	1,270,449
	\$ 4,246,751	\$ 2,823,549

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Notes to Financial Statements
December 31, 2012 and 2011

Aggregate annual maturities of long-term debt and capital lease obligations at December 31, 2012, are as follows:

	Long-term Debt (Excluding Capital Lease Obligations)	Capital Lease Obligations
2013	\$ 1,385,026	\$ 100,000
2014	352,146	100,000
2015	212,693	110,833
2016	177,057	105,000
2017	1,529,042	105,000
Thereafter	<u>633,190</u>	<u>2,007,403</u>
	<u>\$ 4,289,154</u>	
		2,528,236
Less amount representing interest		<u>1,165,149</u>
Present value of future minimum lease payments		1,363,087
Less current maturities		<u>20,464</u>
Noncurrent portion		<u>\$ 1,342,623</u>

Property and equipment include the following property under capital leases at December 31:

	2012	2011
Land	\$ 200,000	\$ 200,000
Buildings and leasehold improvements	<u>1,206,806</u>	<u>1,206,806</u>
	1,406,806	1,406,806
Less accumulated depreciation	<u>136,680</u>	<u>80,408</u>
	<u>\$ 1,270,126</u>	<u>\$ 1,326,398</u>

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Notes to Financial Statements
December 31, 2012 and 2011

Note 9: Operating Leases

The Organization has entered into numerous operating leases for clinic sites, which expire in various years through 2017. These leases generally contain renewal options for up to five years and require the Organization to pay all executory costs (utilities, maintenance and insurance). Rent expenses associated with these leases were \$410,805 and \$326,357 for the years ended December 31, 2012 and 2011, respectively.

Future minimum lease payments at December 31, 2012, were:

2013	\$	215,272
2014		220,461
2015		130,108
2016		115,436
2017		63,033
Future minimum lease payments	\$	744,310

Note 10: Employee Benefit Plan

The Organization adopted a defined contribution plan in accordance with Internal Revenue Code Section 403(b) and an Employee Retirement Plan and Tax Sheltered Custodial Account. Substantially all salaried employees of the Organization are eligible to participate in the retirement plans. The Organization's board of directors determines the annual contributions to the plans. During 2012 and 2011, \$645,330 and \$549,812, respectively, was contributed by the Organization to the plans. Fiscal year 2012 included an 8% discretionary contribution approved by the board of directors.

Note 11: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Allowance for Net Patient Service Revenue Adjustments

Estimates of allowance for adjustments included in net patient revenue are described in *Notes 1* and *2*.

Professional Liability Claims

Estimates related to the accrual for medical malpractice claims are described in *Notes 1* and *7*.

ARcare
Notes to Financial Statements
December 31, 2012 and 2011

Economic Dependency

The Organization is economically dependent upon revenue provided by the U.S. Department of Health and Human Services and the Arkansas Department of Health. During 2012 and 2011, 38% and 40%, respectively, of the Organization's revenues were provided by the U.S. Department of Health and Human Services and the Arkansas Department of Health.

Note 12: Affiliation With Baptist Health

The Organization is an affiliate of Baptist Health (Baptist). Under the terms of the agreement, Baptist will provide the Organization a yearly grant to assist with the daily operational costs and will provide specialty services to, and in behalf of, the Organization's patients. In return, the Organization will display the Baptist logo at all of its clinics and programs and will assist Baptist in its effort to provide quality health care and education to the rural areas of north central Arkansas. Additionally, at all times, there will be four directors actively serving on the Organization's board of directors who have been nominated by Baptist. During 2012 and 2011, the Organization recognized \$876,000 and \$876,000, respectively, in grant revenue as a result of this affiliation.

Note 13: Related Party Transaction

The Organization leases a medical and dental clinic from a board member for approximately \$40,000, on an annual basis.

The Arkansas Family Health Foundation (the Foundation) was formed in 2009 to provide grants and other resources to not-for-profits focused on health and welfare initiatives within the state of Arkansas. Two officers of ARcare serve in the same capacity for the Foundation. During 2012, the Foundation awarded ARcare a grant in the amount of approximately \$650,000 for the construction of the ARcare Center for Education and Wellness.

Supplementary Information

ARcare
Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

Cluster/Program	Federal Agency/ Pass-Through Entity	CFDA Number	Grant Identifying Number	Amount Expended
Housing Opportunities for Persons with AIDS	U.S. Department of Housing and Urban Development/ Arkansas Department of Health	14.241	None	\$ 124,099
Coordinated Services and Access to Research for Women, Infants, Children and Youth	U.S. Department of Health and Human Services	93.153	5 H12HA23018-11-00	438,080
Health Centers Cluster	U.S. Department of Health and Human Services	93.224	6 H80 CS 00207-11-12	6,636,875
Medical Assistance Program (Medicaid Outstation)	U.S. Department of Health and Human Services/Arkansas Department of Human Services	93.778	None	1,731
Rural Health Outreach and Rural Network Development Program	U.S. Department of Health and Human Services	93.912	6 D06RH21666-01-02	99,671
HIV Care Formula Grants	U.S. Department of Health and Human Services/Arkansas Department of Health	93.917	None	1,480,821
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	U.S. Department of Health and Human Services	93.918	6 H76HA00711-10-02	289,302
HIV Prevention Activities	U.S. Department of Health and Human Services/Arkansas Department of Health	93.940	None	21,261
Capital Development	U.S. Department of Health and Human Services	93.526	C8BCS23973-01-00	169,900
Capital Development	U.S. Department of Health and Human Services	93.526	C8ACS23645-01-00	81,016
Rural Health Network Development Program – Delta State	U.S. Department of Health and Human Services	93.912	None	90,262
Retired and Senior Volunteer Program	Corporation for National and Community Services	94.002	None	<u>31,112</u>
				<u><u>\$ 9,464,130</u></u>

ARcare
Schedule of Expenditures of Federal Awards (Continued)
Year Ended December 31, 2012

Notes to Schedule:

1. This schedule includes the federal awards activity of the Organization 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 financial statements.
2. Of the federal expenditures presented in this schedule, the Organization provided federal awards to subrecipients as follows:

Program	CFDA Number	Subrecipient	Amount Provided
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No awards were provided to subrecipients.

ARcare
Schedule of State Awards
Year Ended December 31, 2012

Program	State Agency	State Revenues	State Expenditures
Arkansas Community Health Centers Grant Program	Arkansas Department of Health	\$ 1,297,342	\$ 1,297,342
Medical Assistance Program (Medicaid Outstation)	Arkansas Department of Human Services	1,731	1,731
		<u>\$ 1,299,073</u>	<u>\$ 1,299,073</u>
Program	Pass-Through Entity		
Medicaid Title XIX	Arkansas Department of Human Services	<u>\$ 752,667</u> ⁽¹⁾	

⁽¹⁾ Amount represents 27% of total Medicaid eligible services rendered in 2012. Medicaid payments are included in net patient service revenue in the accompanying statements of operations and changes in net assets.

**Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters Based
on an Audit of the Financial Statements Performed in Accordance With
Government Auditing Standards**

Board of Directors
ARcare
Augusta, Arkansas

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 ARcare (the Organization) as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise ARcare's (the Organization) basis financial statements, and have issued our report thereon dated March 26, 2013.

Internal Control Over Financial Reporting

Management of the Organization is responsible for establishing and maintaining effective internal controls over financial reporting. In planning and performing our audit of the financial statements, we considered Organization'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of Organization'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 entity'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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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 entity'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 Organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Little Rock, Arkansas
March 26, 2013

**Report on Compliance For Each Major Federal Program
and Report on Internal Control Over Compliance
in Accordance With OMB Circular A-133**

Board of Directors
ARcare
Augusta, Arkansas

Compliance

We have audited the ARcare compliance of (the Organization) 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 Organization's major federal programs for the year ended December 31, 2012. The Organization'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 Organization'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 Organization'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 Organization's compliance.

Opinion on Each Major Federal Program

In our opinion, ARcare 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.

Report on Internal Control Over Compliance

Management of ARcare 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 Organization'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 internal control over compliance.

Accordingly, we do not express an opinion on the effectiveness of the Organization'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.

BKD, LLP

Little Rock, Arkansas
March 26, 2013

ARcare
Schedule of Findings and Questioned Costs (Continued)
Year Ended December 31, 2012

7. The Organization's major programs were:

Cluster/Program	CFDA Number
Health Center Cluster	93.224
Coordinated Services and Access to Research for Women, Infants, Children and Youth	93.153

8. The threshold used to distinguish between Type A and Type B programs, as those terms are defined in OMB Circular A-133, was \$300,000.

9. The Organization qualified as a low-risk auditee as that term is defined in OMB Circular A-133? Yes No

Findings Required to be Reported by *Government Auditing Standards*

Reference Number	Finding	Questioned Costs
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No matters are reportable.

Findings Required to be Reported by OMB Circular A-133

Reference Number	Finding	Questioned Costs
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No matters are reportable.

ARcare
Summary Schedule of Prior Audit Findings
Year Ended December 31, 2012

Reference Number	Finding	Status
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No matters are reportable.