

# **Gifford Health Care, Inc.**

## **Independent Auditor's Report and Consolidated Financial Statements**

**September 30, 2017 and 2016**

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**Gifford Health Care, Inc.**  
**September 30, 2017 and 2016**

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## Independent Auditor's Report

Board of Directors  
Gifford Health Care, Inc.  
Randolph, Vermont

We have audited the accompanying consolidated financial statements of Gifford Health Care, Inc. (GHC), which comprise the balance sheets as of September 30, 2017 and 2016, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Gifford Health Care, Inc. as of September 30, 2017 and 2016, and the results of its operations, the 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.

***Supplementary Information***

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements as a whole. The supplementary information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

*BKD, LLP*

Springfield, Missouri  
January 31, 2018

**Gifford Health Care, Inc.**  
**Consolidated Balance Sheets**  
**September 30, 2017 and 2016**

**Assets**

|  | <b>2017</b>    | <b>2016</b>   |
|--|----------------|---------------|
| <b>Current Assets</b>  |                |               |
| Cash and cash equivalents  | \$ 2,597,166   | \$ 2,932,437  |
| Short-term investments   | 2,167,825      | 2,113,059     |
| Patient accounts receivable, net of allowance;<br>2017 - \$1,952,261, 2016 - \$2,287,274 | 9,983,786      | 8,880,563     |
| Other receivables  | 539,344        | 755,486       |
| Estimated amounts due from third parties   | 539,373        | -             |
| Supplies   | 1,423,309      | 1,340,222     |
| Prepaid expenses and other   | 1,842,885      | 1,446,942     |
| Total current assets   | 19,093,688     | 17,468,709    |
| <b>Assets Limited as to Use - Internally Designated</b>                                  | 22,836,249     | 20,765,970    |
| <b>Long-Term Investments</b>   | 9,102,634      | 8,358,557     |
| <b>Property and Equipment, Net</b>   | 53,443,851     | 42,889,323    |
| <b>Other Assets</b>  | 4,550,403      | 4,121,738     |
| Total assets   | \$ 109,026,825 | \$ 93,604,297 |

## Liabilities and Net Assets

|   | <u>2017</u>               | <u>2016</u>              |
|---|---------------------------|--------------------------|
| <b>Current Liabilities</b>                  |                           |                          |
| Current maturities of long-term debt        | \$ 861,944                | \$ 592,832               |
| Accounts payable                            | 4,063,573                 | 3,608,324                |
| Accrued expenses                            | 7,779,031                 | 6,245,208                |
| Estimated amounts due to third-party payers | 319,554                   | 631,786                  |
| Other                                       | 108,194                   | 216,875                  |
| Total current liabilities                   | <u>13,132,296</u>         | <u>11,295,025</u>        |
| <b>Long-Term Debt</b>                       | 29,312,256                | 19,396,561               |
| <b>Other Liabilities</b>                    | 4,447,821                 | 3,769,436                |
| <b>Deferred Revenue</b>                     | 2,196,532                 | -                        |
| <b>Deferred Annuities</b>                   | 431,669                   | 414,606                  |
| <b>Interest Rate Swap Agreement</b>         | 2,508,065                 | 3,878,971                |
| Total liabilities                           | <u>52,028,639</u>         | <u>38,754,599</u>        |
| <b>Net Assets</b>                           |                           |                          |
| Unrestricted                                | 54,696,906                | 52,473,839               |
| Temporarily restricted                      | 891,702                   | 1,126,996                |
| Permanently restricted                      | 1,409,578                 | 1,248,863                |
| Total net assets                            | <u>56,998,186</u>         | <u>54,849,698</u>        |
| <br>Total liabilities and net assets        | <br><u>\$ 109,026,825</u> | <br><u>\$ 93,604,297</u> |

**Gifford Health Care, Inc.**  
**Consolidated Statements of Operations**  
**Years Ended September 30, 2017 and 2016**

|   | <u>2017</u>         | <u>2016</u>         |
|---|---------------------|---------------------|
| <b>Unrestricted Revenues, Gains and Other Support</b>                 |                     |                     |
| Patient service revenue (net of contractual discounts and allowances) | \$ 69,230,555       | \$ 69,339,713       |
| Provision for doubtful accounts                                       | <u>3,396,674</u>    | <u>3,400,723</u>    |
| Net patient service revenue less provision for doubtful accounts      | 65,833,881          | 65,938,990          |
| Other   | 4,718,904           | 5,197,547           |
| Net assets released from restrictions used for operations             | <u>183,649</u>      | <u>165,136</u>      |
| Total unrestricted revenues, gains and other support                  | <u>70,736,434</u>   | <u>71,301,673</u>   |
| <b>Expenses and Losses</b>  |                     |                     |
| Salaries and wages  | 36,941,778          | 36,147,459          |
| Employee benefits   | 9,450,420           | 10,575,943          |
| Purchased services and professional fees                              | 7,768,867           | 6,880,342           |
| Supplies and other  | 14,555,122          | 13,899,319          |
| Depreciation and amortization   | 3,940,024           | 3,772,108           |
| Interest  | <u>810,233</u>      | <u>767,112</u>      |
| Total expenses and losses   | <u>73,466,444</u>   | <u>72,042,283</u>   |
| <b>Operating Loss</b>   | <u>(2,730,010)</u>  | <u>(740,610)</u>    |
| <b>Other Income (Expense)</b>   |                     |                     |
| Investment return   | 3,032,385           | 2,492,159           |
| Change in fair value of interest rate swap agreement                  | 1,370,906           | (697,465)           |
| Other income  | <u>101,037</u>      | <u>54,783</u>       |
| Total other income (expense)  | <u>4,504,328</u>    | <u>1,849,477</u>    |
| <b>Excess of Revenues Over Expenses</b>                               | 1,774,318           | 1,108,867           |
| Net assets released for acquisition of property and equipment         | <u>448,749</u>      | <u>931,507</u>      |
| <b>Increase in Unrestricted Net Assets</b>                            | <u>\$ 2,223,067</u> | <u>\$ 2,040,374</u> |

**Gifford Health Care, Inc.**  
**Consolidated Statements of Changes in Net Assets**  
**Years Ended September 30, 2017 and 2016**

|   | <b>2017</b>   | <b>2016</b>   |
|---|---------------|---------------|
| <b>Unrestricted Net Assets</b>                                |               |               |
| Excess of revenues over expenses                              | \$ 1,774,318  | \$ 1,108,867  |
| Net assets released for acquisition of property and equipment | 448,749       | 931,507       |
| Increase in unrestricted net assets                           | 2,223,067     | 2,040,374     |
| <b>Temporarily Restricted Net Assets</b>                      |               |               |
| Investment return and contributions                           | 397,104       | 1,386,932     |
| Net assets released from restrictions                         | (632,398)     | (1,096,643)   |
| Increase (decrease) in temporarily restricted net assets      | (235,294)     | 290,289       |
| <b>Permanently Restricted Net Assets</b>                      |               |               |
| Contributions   | 160,715       | 120,323       |
| Increase in permanently restricted net assets                 | 160,715       | 120,323       |
| <b>Change in Net Assets</b>                                   | 2,148,488     | 2,450,986     |
| <b>Net Assets, Beginning of Year</b>                          | 54,849,698    | 52,398,712    |
| <b>Net Assets, End of Year</b>                                | \$ 56,998,186 | \$ 54,849,698 |



**Gifford Health Care, Inc.**  
**Consolidated Statements of Cash Flows**  
**Years Ended September 30, 2017 and 2016**

|   | <u>2017</u>         | <u>2016</u>         |
|---|---------------------|---------------------|
| <b>Operating Activities</b>                             |                     |                     |
| Change in net assets                                    | \$ 2,148,488        | \$ 2,450,986        |
| Items not requiring (providing) cash                    |                     |                     |
| Depreciation and amortization                           | 3,940,024           | 3,772,108           |
| Net gain on investments                                 | (2,362,689)         | (1,778,621)         |
| Change in fair value of interest rate swap agreement    | (1,370,906)         | 697,465             |
| Restricted contributions received                       | (557,819)           | (1,507,255)         |
| Changes in  |                     |                     |
| Patient accounts receivable, net                        | (1,103,223)         | 575,308             |
| Inventories   | (83,087)            | (73,524)            |
| Estimated amounts due from and to third-party payers    | (851,605)           | (584,540)           |
| Accounts payable and accrued expenses                   | 1,245,460           | (2,053,268)         |
| Other assets and liabilities                            | (48,239)            | 29,714              |
|   | <u>956,404</u>      | <u>1,528,373</u>    |
| Net cash provided by operating activities               |                     |                     |
| <b>Investing Activities</b>                             |                     |                     |
| Purchases of property and equipment                     | (13,724,400)        | (6,673,273)         |
| Purchase of investments                                 | (2,581,589)         | (1,355,625)         |
| Proceeds from disposition of investments                | 2,075,156           | 4,059,062           |
|   | <u>(14,230,833)</u> | <u>(3,969,836)</u>  |
| Net cash used in investing activities                   |                     |                     |
| <b>Financing Activities</b>                             |                     |                     |
| Proceeds from advanced funds received                   | 2,196,532           | -                   |
| Restricted contributions and investment income received | 557,819             | 1,507,255           |
| Proceeds from issuance of long-term debt                | 11,883,187          | 320                 |
| Principal payments on long-term debt                    | (1,698,380)         | (636,614)           |
|   | <u>12,939,158</u>   | <u>870,961</u>      |
| Net cash provided by financing activities               |                     |                     |
| <b>Decrease in Cash and Cash Equivalents</b>            | (335,271)           | (1,570,502)         |
| <b>Cash and Cash Equivalents, Beginning of Year</b>     | <u>2,932,437</u>    | <u>4,502,939</u>    |
| <b>Cash and Cash Equivalents, End of Year</b>           | <u>\$ 2,597,166</u> | <u>\$ 2,932,437</u> |
| <b>Supplemental Cash Flows Information</b>              |                     |                     |
| Interest paid   | \$ 771,997          | \$ 794,879          |
| Purchase of property and equipment in accounts payable  | \$ 2,097,168        | \$ 1,353,556        |

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

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

***Nature of Operations and Principles of Consolidation***

Gifford Health Care (GHC) is a not-for-profit organization incorporated under the laws of the State of Vermont for the purpose of providing health care services in Randolph, Vermont, and surrounding communities. GHC is a federally qualified health center (FQHC).

GHC includes Gifford Medical Center Inc. (GMC), a 25-bed critical access hospital (CAH), providing general and specialty services.

During 2015, GHC created Gifford Retirement Community (GRC) with GMC transferring certain operations to GRC. GMC and GRC are under common control, both prior to and after the transfer and organization of GRC. The transfer of operations was accounted for at carryover basis. GRC provides skilled nursing services. GRC began operating an independent living retirement community in 2017.

Collectively GHC, GMC and GRC are referred to as GHC. The consolidated financial statements include the accounts of GHC, GMC and GRC. All material intercompany accounts and transactions have been eliminated in consolidation.

***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***

GHC considers all liquid investments with original maturities of three months or less to be cash equivalents. At September 30, 2017 and 2016, cash equivalents consisted primarily of sweep products. GHC utilizes repurchase and sweep products as part of their cash management policy, which are not FDIC insured, but may be covered by separate agreements with the financial institution.

At September 30, 2017 and 2016, GHC's cash accounts did not exceed federally insured limits.

At September 30, 2017 and 2016, GHC held \$2,993,611 and \$3,531,803, respectively, in repurchase and sweep accounts.

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

***Investments and Investment Return***

Investments in equity securities having a readily determinable fair value and in all debt securities are carried at fair value. Other investments are valued at the lower of cost (or fair value at time of donation, if acquired by contribution) or fair value. Investment return includes dividend, interest and other investment income; realized and unrealized gains and losses on investments carried at fair value; and realized gains and losses on other investments.

Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year is included in unrestricted net assets. Other investment return is reflected in the statements of operations and changes in net assets as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

***Assets Limited As To Use***

Assets limited as to use include 1) assets set aside by the Board of Directors for future capital improvements which the Board retains control and may at its discretion subsequently use for other purposes and 2) assets held by trustee and restricted for the purchase of property and equipment. Amounts required to meet current liabilities are included in current assets.

***Patient Accounts Receivable***

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, GHC 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 doubtful accounts. 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, GHC analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for doubtful accounts, if necessary (for example, for expected doubtful 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), GHC records a significant provision for doubtful 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.

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

GHC's allowance for doubtful accounts for self-pay was 92% and 91% of self-pay accounts receivable at September 30, 2017 and 2016, respectively. GHC's write-offs increased from \$2,640,265 for the year ended September 30, 2016, to \$3,731,687 for the year ended September 30, 2017. Allowance for doubtful accounts activity for 2017 and 2016, is shown in the following table:

|                                  | <b>2017</b>  | <b>2016</b>  |
|----------------------------------|--------------|--------------|
| Balance, beginning of year       | \$ 2,287,274 | \$ 1,526,816 |
| Provision for year               | 3,396,674    | 3,400,723    |
| Accounts charged off during year | (3,731,687)  | (2,640,265)  |
| Balance, end of year             | \$ 1,952,261 | \$ 2,287,274 |

***Supplies***

GHC states supply inventories at the lower of cost, determined using the first-in, first-out method, or market.

***Property and Equipment***

Property and equipment acquisitions are recorded at cost and are depreciated using the straight-line method 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.

|                                     |              |
|-------------------------------------|--------------|
| Land improvements                   | 3 - 25 years |
| Buildings and building improvements | 5 - 40 years |
| Equipment                           | 3 - 25 years |

Donations of property and equipment are reported at fair value as an increase in unrestricted net assets unless use of the assets is restricted by the donor. Monetary gifts that must be used to acquire property and equipment are reported as restricted support. The expiration of such restrictions is reported as an increase in unrestricted net assets when the donated asset is placed in service.

***Long-Lived Asset Impairment***

GHC 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 estimated 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 September 30, 2017 and 2016.

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

***Deferred Financing Costs***

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt using the straight-line method.

***Deferred Revenue***

GRC recognizes revenue for the fees charged to residents for rental, housekeeping and dietary services provided which is recorded at the estimated net realized amounts.

GRC also records deferred revenue from the occupancy of units in the retirement community as follows: Upon entry in the retirement community, residents pay a deposit to GRC. The deposit is 80% refundable to the resident contingent upon the reoccupancy of a resident's unit after the resident leaves the community. The refunded deposit is equal to the lesser of the original purchase price or resale price. Twenty percent of each deposit is nonrefundable and is amortized into income over the life expectancy of the resident.

There was no revenue reported as net patient service revenue in 2017 or 2016. GRC received proceeds from the sale of new units totaling \$2,196,532 in 2017. No amounts were received in 2016. GRC did not refund any amounts in 2017 or 2016.

As of September 30, 2017 and 2016, GRC is contingently liable for \$1,671,910 and \$0, respectively, which represents the 80% portion of current residents' entrance deposits.

As of September 30, 2017 and 2016, the portion of advance fees representing deferred revenue \$524,622 and \$0, respectively, which represents the 20% portion of current residents' entrance deposits.

Based on the current fee structure and existing residency agreements, management expects that future monthly service charges will be reflective of related operating costs and, accordingly, GRC has not recorded a liability to provide future services to current residents.

***Deferred Annuities***

Annuity obligations represent the amount of various planned giving instruments where GRC has fiduciary responsibility for the safekeeping, investment management and distribution of such funds to designated individuals. Annuity obligations are valued at the actuarial present value of the expected payments based upon the life expectancy for the annuitants. The present value of the estimated future payments at September 30, 2017 and 2016, was \$498,054 and \$473,991, respectively, and is presented in accrued expenses and deferred annuities. At September 30, 2017 and 2016, the corresponding assets to satisfy the future payments were \$1,315,009 and \$1,392,709, respectively.

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

***Temporarily and Permanently Restricted Net Assets***

Temporarily restricted net assets are those whose use by GHC has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by GHC in perpetuity.

***Net Patient Service Revenue***

GHC has agreements with third-party payers that provide for payments to GHC at amounts different from their established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known. Net patient service revenue increased by \$300,000 and \$0 in 2017 and 2016, respectively, due to changes in amounts previously estimated.

***Grant Revenue***

GHC is the recipient of a Consolidated Health Centers (CHC) grant from the U.S. Department of Health and Human Services (the “granting agency”). The general purpose of the grant is to provide expanded health care service delivery for residents of Randolph, Vermont, and surrounding areas. Terms of the grant generally provide for funding of GHC’s operations based on an approved budget.

Grant revenue is recognized as qualifying expenditures are incurred over the grant period. During the years ended September, 30, 2017 and 2016, GHC recognized CHC grant revenue of \$1,505,676 and \$1,071,983, respectively. GHC’s present CHC grant award covers the grant period ended January 31, 2018, and is approved at \$1,661,921. Future funding will be determined by the granting agency based on an application to be submitted by GHC prior to expiration of the present grant period.

***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 hospitals and FQHC’s that demonstrate meaningful use of certified electronic health records technology (EHR).

CAH’s are eligible to receive incentive payments in the cost reporting period beginning in the federal fiscal year in which meaningful use criteria have been met. The Medicare incentive payment is for qualifying costs of the purchase of certified EHR technology multiplied by GMC’s Medicare share fraction, which includes a 20% incentive. This payment is an acceleration of amounts that would have been received in future periods based on reimbursable costs incurred, including depreciation. If meaningful use criteria are not met in future periods, GMC is subject to penalties that would reduce future payments for services.

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. The final amount for any payment year under both programs is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

GMC recognized the incentive payment revenue received for qualified EHR technology expenditures during 2017, which was the period during which management was reasonably assured meaningful use was achieved and the earnings process was complete. Management believes the incentive payments reflect a change in how “allowable costs” are determined in paying CAHs for providing services to Medicare beneficiaries.

GHC 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.

GHC recorded revenue of \$195,000 and \$582,000, which is included in other revenue within operating revenues in the statements of operations as of the years ended September 30, 2017 and 2016, respectively.

***Contract Pharmacy Program***

GHC participates in the 340B outpatient drug discount program administered by the Office of Pharmacy Affairs of the Health Resources and Services Administration (HRSA). GHC contracts with local retail pharmacies under the program, which resulted in additional revenues and discounts on outpatient pharmaceuticals. Net revenue from this program was approximately \$1,254,000 and \$1,439,000 greater than the cost of operating the program for 2017 and 2016, respectively. Laws and regulations surrounding the 340B drug program are complex and are subject to interpretation and change.

***Charity Care***

GHC provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because GHC does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

***Contributions***

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are initially reported at fair value determined using the discounted present value of estimated future cash flows technique. The resulting discount is amortized using the level-yield method and is reported as contribution revenue.

**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

Gifts received with donor stipulations are reported as either temporarily or permanently restricted support. When a donor restriction expires, that is, when a time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified and reported as an increase in unrestricted net assets. Donor-restricted contributions whose restrictions are met within the same year as received are initially reported as temporarily restricted contributions. Conditional contributions are reported as liabilities until the condition is eliminated or the contributed assets are returned to the donor.

***Estimated Self-Insurance Costs***

GHC records an estimated liability for self-insured employee health claims, which is included in accrued expenses, and includes an estimate of both reported claims and claims incurred but not reported.

***Professional Liability Claims***

GHC 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 6*.

***Income Taxes***

GHC, GMC and GRC have been recognized as exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, GHC, GMC and GRC are subject to federal income tax on any unrelated business taxable income. GHC files tax returns in the U.S. federal jurisdiction.

With a few exceptions, GHC is no longer subject to U.S. federal examinations by tax authorities for years before 2014.

***Excess of Revenues Over Expenses***

The statements of operations include excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, permanent transfers to and from affiliates for other than goods and services and contributions of long-lived assets including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets.

***Transfers Between Fair Value Hierarchy Levels***

Transfers in and out of Level 1 (quoted market prices), Level 2 (other significant observable inputs) and Level 3 (significant unobservable inputs) are recognized on the period ending date.



**Gifford Health Care, Inc.**  
**Notes to Consolidated Financial Statements**  
**September 30, 2017 and 2016**

**Subsequent Events**

Subsequent events have been evaluated through January 31, 2018, which is the date the financial statements were available to be issued.

**Reclassifications**

Certain reclassifications have been made to the 2016 financial statements for the adoption of Accounting Standards Update 2015-03, *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, that were deemed to be immaterial, and to conform to the 2017 financial statement presentation. These reclassifications had no effect on the change in net assets.

**Note 2: Net Patient Service Revenue**

GHC 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, GHC recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of GHC's uninsured patients will be unable or unwilling to pay for the services provided. Thus, GHC records a significant provision for doubtful accounts related to uninsured patients in the period the services are provided. This provision for doubtful accounts is presented on the statement of operations as a component of net patient service revenue.

GHC has agreements with third-party payers that provide for payments to GHC at amounts different from its established rates. These payment arrangements include:

*Medicare – GMC.* GMC is a 25-bed facility certified by Medicare as a critical access hospital (CAH). Medicare inpatient and outpatient reimbursement as a CAH is based on the defined allowable costs of services rendered. This certification places several restrictions on a CAH's operations, including a 96-hour average annual acute-care length of stay restriction and a limit of 25 medical/surgical beds.

*Medicare - GHC.* Covered FQHC services rendered to Medicare program beneficiaries are paid in accordance with provisions of Medicare's Prospective Payment System (PPS) for FQHCs. Medicare payments, including patient coinsurance, are paid on the lesser of GHC's actual charge or the applicable PPS rate. Services not covered under the FQHC benefit are paid based on established fee schedules.

*Medicare - GRC.* Facility residents eligible for "Part A" Medicare benefits are paid on a prospective basis, with no retrospective settlement. The prospective payment is based on the scoring attributed to the acuity level of the resident at a rate determined by federal guidelines.

*Medicaid – GMC, GHC and GRC.* Inpatient, outpatient, clinic and skilled nursing services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates.

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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.

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

Patient service revenue, net of contractual allowances and discounts (but before the provision for doubtful accounts), recognized in the years ended September 30, 2017 and 2016, was approximately:

|   | <b>2017</b>          | <b>2016</b>          |
|---|----------------------|----------------------|
| Medicare                                | \$ 24,262,103        | \$ 22,861,960        |
| Medicaid                                | 11,573,354           | 12,207,729           |
| Blue Cross and other third-party payers | 31,357,431           | 32,323,993           |
| Patients                                | 2,037,667            | 1,946,031            |
|   | <u>\$ 69,230,555</u> | <u>\$ 69,339,713</u> |

**Note 3: Concentration of Credit Risk**

GHC grants credit without collateral to their patients, most of whom are area residents and are insured under third-party payer agreements. The mix of receivables from patients and third-party payers at September 30, 2017 and 2016, is:

|   | <b>2017</b> | <b>2016</b> |
|---|-------------|-------------|
| Medicare                                | 31%         | 32%         |
| Medicaid                                | 18%         | 19%         |
| Blue Cross and other third-party payers | 49%         | 46%         |
| Patients                                | 2%          | 3%          |
|   | <u>100%</u> | <u>100%</u> |

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**Note 4: Investments and Investment Return**

Investments, at September 30, include:

|                                   | <b>2017</b>          | <b>2016</b>          |
|-----------------------------------|----------------------|----------------------|
| Cash equivalents                  | \$ 1,199,900         | \$ 1,164,580         |
| Certificates of deposit           | 1,087,123            | 1,078,604            |
| Municipal obligations             | -                    | 60,323               |
| U.S. Treasury obligations         | -                    | 482,757              |
| U.S. agency obligations           | 1,385,328            | 1,770,811            |
| Corporate and foreign obligations | 8,734,243            | 7,674,204            |
| Equity securities                 |                      |                      |
| Consumer discretionary            | 1,645,247            | 2,439,101            |
| Consumer staples                  | 1,753,361            | 1,266,052            |
| Energy                            | 1,346,963            | 1,127,506            |
| Financial                         | 3,146,770            | 2,788,537            |
| Health care                       | 3,136,286            | 2,881,924            |
| Industrials                       | 1,802,513            | 2,446,255            |
| Information technology            | 5,359,176            | 3,556,682            |
| International                     | 2,966,419            | 1,537,380            |
| Materials                         | 250,790              | 237,354              |
| Telecommunications                | 200,484              | 210,571              |
| Utilities                         | -                    | 344,945              |
| Other                             | 92,105               | 170,000              |
|                                   | <u>\$ 34,106,708</u> | <u>\$ 31,237,586</u> |

Investments are included in the consolidated balance sheets as follows:

|                          | <b>2017</b>          | <b>2016</b>          |
|--------------------------|----------------------|----------------------|
| Short-term investments   | \$ 2,167,825         | \$ 2,113,059         |
| Assets limited as to use | 22,836,249           | 20,765,970           |
| Long-term investments    | <u>9,102,634</u>     | <u>8,358,557</u>     |
|                          | <u>\$ 34,106,708</u> | <u>\$ 31,237,586</u> |

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Total investment return is comprised of the following:

|   | <b>2017</b>         | <b>2016</b>         |
|---|---------------------|---------------------|
| Interest and dividend income                          | \$ 669,696          | \$ 713,538          |
| Net realized gains on sales of securities             | 190,300             | 1,791,430           |
| Net unrealized gains and losses on trading securities | <u>2,172,389</u>    | <u>(12,809)</u>     |
| Total   | <u>\$ 3,032,385</u> | <u>\$ 2,492,159</u> |

**Note 5: Property and Equipment**

Property and equipment consists of the following at September 30, 2017 and 2016:

|                                     | <b>2017</b>          | <b>2016</b>          |
|-------------------------------------|----------------------|----------------------|
| Land and land improvements          | \$ 6,020,606         | \$ 4,106,317         |
| Buildings and building improvements | 51,139,847           | 38,443,069           |
| Equipment                           | 38,873,578           | 37,342,330           |
| Construction in progress            | <u>1,448,410</u>     | <u>4,046,439</u>     |
|                                     | 97,482,441           | 83,938,155           |
| Less accumulated depreciation       | <u>44,038,590</u>    | <u>41,048,832</u>    |
| Property and equipment, net         | <u>\$ 53,443,851</u> | <u>\$ 42,889,323</u> |

At September 30, 2017, construction in progress represents costs incurred in connection with the construction of various additions and alterations to GHC's facilities and equipment. The primary project at September 30, 2017, is the remodel of the emergency department. Completion is expected during 2018, with approximately \$340,000 of additional construction costs expected after September 30, 2017. Anticipated funding is through internally designated funds.

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**Note 6: Professional Liability Claims**

GHC purchases medical malpractice insurance under a claims-made policy. Under such a policy, only claims made and reported to the insurer during the policy term, regardless of when the incidents giving rise to the claims occurred, are covered. GHC also purchases excess umbrella liability coverage, which provides additional coverage above the basic policy limits up to the amount specified in the umbrella policy.

Based upon GHC's claims experience, an accrual had been made for the GHC's estimated medical malpractice costs, including costs associated with litigating or settling claims, under its malpractice insurance policy, amounting to approximately \$1,053,000 and \$1,033,000 as of September 30, 2017 and 2016, respectively, which is included in accrued expenses. It is reasonably possible that this estimate could change materially in the near term.

**Note 7: Long-Term Debt**

|                                      | <b>2017</b>   | <b>2016</b>   |
|--------------------------------------|---------------|---------------|
| Series 2014 Bonds (A)                | \$ 19,108,013 | \$ 19,743,007 |
| Note payable (B)                     | 296,607       | 304,621       |
| Note payable (C)                     | 76,084        | 78,890        |
| Note payable (D)                     | 10,804,080    | -             |
|                                      | 30,284,784    | 20,126,518    |
| Less current maturities              | 861,944       | 592,832       |
| Less unamortized debt issuance costs | 110,584       | 137,125       |
|                                      | \$ 29,312,256 | \$ 19,396,561 |

A) In December 2014, the Vermont Educational and Health Buildings Financing Agency (the "Agency") issued \$20,840,000 of tax-exempt revenue bonds. Proceeds were used to extinguish the existing Series 2010 Bonds, pay certain costs incurred in the authorization and issuance of the Bonds and fund future capital projects. The Bonds require monthly principal and interest payments, at a variable rate of 70% of one-month LIBOR plus 1.23%. The rates as of September 30, 2017 and 2016, was 2.09% and 1.59%, respectively. The Bonds mature in December 2036, but contain a provision allowing early redemption in December 2021, 2028 and 2035, at a price equal to 100% of the amount outstanding.

GHC has granted a security interest in gross receipts. The Bonds contain certain covenants including maintaining a minimum amount of days cash on hand and debt service ratio.

GHC has entered into an interest rate swap agreement to help mitigate exposure to future changes in interest rates on this Bond, see *Note 8*.

B) Monthly payments of \$2,364 including interest at 6.5%, due in March 2035, secured by property.

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- C) Monthly payments of \$450 including interest at 2.27%, due in April 2034, secured by property.
- D) Interest only payments on outstanding amounts are due through July 2018 at 4.35%. From July 2018 through January 2024, monthly payments are due including interest at 4.35%. From January 2024 through maturity in June 2028, monthly payments are due including interest at a variable rate based on a Federal Home Loan Bank index plus 1.75%. Due in June 2028, secured by property.

Aggregate annual maturities of long-term debt and principal payments on capital lease obligations at September 30, 2017, are:

|            |                      |
|------------|----------------------|
| 2018       | \$ 861,944           |
| 2019       | 1,696,849            |
| 2020       | 1,771,325            |
| 2021       | 1,849,078            |
| 2022       | 1,930,253            |
| Thereafter | <u>22,175,335</u>    |
|            | <u>\$ 30,284,784</u> |

GHC also has a \$1,000,000 line-of-credit agreement available, expiring on June 1, 2018. No amounts were outstanding at September 30, 2017 and 2016. If drawn, interest payments are due monthly at 4%. The line is unsecured.

GHC also has a \$6,000,000 line-of-credit agreement as of September 30, 2016. The line is to help fund construction expenditures at GRC (*Note 5*). No amounts were outstanding as of September 30, 2016. If drawn, interest payments are due at the expiration date at a variable interest rate, which was 3.5% as of September 30, 2016. The line is secured by investments. The line expired in December 2016.

**Note 8: Interest Rate Swap Agreement**

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations on its own debt, GMC entered into an interest rate swap agreement. The notional amount is adjusted every October 1. The notional amount was \$17,845,000 and \$18,385,000 at September 30, 2017 and 2016, respectively. The agreement provides for GMC to receive interest from the counterparty equivalent to the sum of 68% of three-month LIBOR and pay interest to the counterparty at a fixed rate of 3.08%. The swap expires on October 1, 2036.

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The table below presents certain information regarding GHC's interest rate swap agreement.

|  | <b>2017</b>  | <b>2016</b>  |
|--|--------------|--------------|
| <b>Other Liabilities</b>   |              |              |
| Fair value of interest rate swap agreement   | \$ 2,508,065 | \$ 3,878,971 |
| <b>Interest Expense</b>  |              |              |
| Loss reclassified from unrestricted net assets into excess of revenues over expenses | 411,323      | 492,458      |
| <b>Other Income</b>  |              |              |
| Change in interest rate swap agreement   | 1,370,906    | (697,465)    |

**Note 9: Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are available for health care services and capital purposes. The portion restricted for capital purposes was \$408,694 and \$809,991 at September 30, 2017 and 2016, respectively.

During 2017 and 2016, net assets were released from donor restrictions by incurring expenses, satisfying the operating restricted purposes in the amounts of \$183,649 and \$165,136, respectively.

During 2017 and 2016, net assets of \$448,749 and \$931,507, respectively, were released to purchase property and equipment.

Permanently restricted net assets are restricted at September 30, 2017 and 2016, to:

|   | <b>2017</b>         | <b>2016</b>         |
|---|---------------------|---------------------|
| Investments to be held in perpetuity, the income from which is expendable to support: |                     |                     |
| Indigent care   | \$ 227,585          | \$ 227,585          |
| Community outreach initiatives  | 527,116             | 527,116             |
| Nursing   | 35,025              | 35,025              |
| Buildings and maintenance   | 40,996              | 40,996              |
| Operations  | 53,529              | 53,529              |
| Unrestricted  | 525,327             | 364,612             |
|   | <u>\$ 1,409,578</u> | <u>\$ 1,248,863</u> |

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**Note 10: Endowment**

GHC's endowment consists of various individual donor-restricted funds which were established for general operational and certain departmental purposes. As required by accounting principles generally accepted in the United States of America (GAAP), net assets associated with endowment funds, including board-designated endowment funds, are classified and reported based on the existence or absence of donor-imposed restrictions.

GHC's governing body has interpreted the Uniform Management of Institutional Funds Act (UPMIFA) as requiring preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, GHC classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, and temporarily restricted net assets, the investment earnings of the gifts donated which have not met the donor stipulations for recognition in unrestricted net assets. In accordance with UPMIFA, GHC considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of GHC and the fund
3. General economic conditions
4. Possible effect of inflation and deflation
5. Expected total return from investment income and appreciation or depreciation of investments
6. Other resources of GHC
7. Investment policies of GHC

Changes in endowment net assets for the years ended September 30, 2017 and 2016, were:

|   | <b>2017</b>         |                               |                               |                     |
|---|---------------------|-------------------------------|-------------------------------|---------------------|
|   | <b>Unrestricted</b> | <b>Temporarily Restricted</b> | <b>Permanently Restricted</b> | <b>Total</b>        |
| Endowment net assets, beginning of year | \$ 6,487,110        | \$ 346,116                    | \$ 1,248,863                  | \$ 8,082,089        |
| Investment return and contributions     | 127,826             | (13,139)                      | 160,715                       | 275,402             |
| Endowment net assets, end of year       | <u>\$ 6,614,936</u> | <u>\$ 332,977</u>             | <u>\$ 1,409,578</u>           | <u>\$ 8,357,491</u> |
|   | <b>2016</b>         |                               |                               |                     |
|   | <b>Unrestricted</b> | <b>Temporarily Restricted</b> | <b>Permanently Restricted</b> | <b>Total</b>        |
| Endowment net assets, beginning of year | \$ 5,774,084        | \$ 373,775                    | \$ 1,128,540                  | \$ 7,276,399        |
| Investment return and contributions     | 713,026             | (27,659)                      | 120,323                       | 805,690             |
| Endowment net assets, end of year       | <u>\$ 6,487,110</u> | <u>\$ 346,116</u>             | <u>\$ 1,248,863</u>           | <u>\$ 8,082,089</u> |



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GHC has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs and other items supported by its endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds GHC must hold in perpetuity or for donor-specified periods, as well as those of board-designated endowment funds. Under GHC’s policies, endowment assets are invested in a manner that is intended to produce results equal to inflation plus four percent. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate of return objectives, GHC relies on a total return strategy in which investment returns are achieved through both current yield (investment income such as dividends and interest) and capital appreciation (both realized and unrealized). GHC targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

GHC has a spending policy of appropriating for expenditure each year 4% of its endowment fund’s average fair value over the prior three years through the year end preceding the year in which expenditure is planned. It is GHC’s intent that the distribution rate will not exceed the total return of the endowment. In establishing this policy, GHC considered the long-term expected return on its endowment. This is consistent with GHC’s objective to maintain the purchasing power of endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return.

**Note 11: Charity Care**

The estimated costs of charity provided under GHC’s charity care policy were approximately \$227,000 and \$233,000 for 2017 and 2016, respectively. The cost of charity care is estimated by applying the ratio of cost to charges to the gross uncompensated care charges.

**Note 12: Functional Expenses**

GHC provides health care services primarily to residents within their geographic area. Expenses related to providing these services are as follows:

|                            | <b>2017</b>   | <b>2016</b>   |
|----------------------------|---------------|---------------|
| Health care services       | \$ 68,551,684 | \$ 66,670,843 |
| General and administrative | 4,748,558     | 5,181,932     |
| Fundraising                | 166,202       | 189,508       |
|                            | \$ 73,466,444 | \$ 72,042,283 |

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**Note 13: Pension Plan**

GHC has a defined contribution pension plan covering all employees meeting age and service requirements. The plan provides for immediate vesting of all eligible employees. Discretionary contributions by GHC are funded at 4% of covered compensation plus an additional 1% matching contribution to eligible employees. Pension expense was \$1,393,710 and \$1,328,084 for 2017 and 2016, respectively.

GHC has a deferred compensation plan for the benefit of certain employees. The assets are classified as other long-term assets and a corresponding liability. Investments held in deferred compensation plans include equity and fixed income mutual funds.

**Note 14: Disclosures About Fair Value of Assets and Liabilities**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities.
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3** Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities.

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***Recurring Measurements***

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at September 30, 2017 and 2016.

|   | Fair Value   | Fair Value Measurements Using   |   |  |
|---|--------------|---|---|--|
|   |              | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| <b>September 30, 2017</b>   |              |   |   |  |
| Investments and cash equivalents  |              |   |   |  |
| Cash equivalents - money market funds                                       | \$ 1,199,900 | \$ 1,199,900  | \$ -  | \$ -   |
| Equity securities   | 21,608,009   | 21,608,009  | -   | -  |
| Corporate obligations   | 8,734,243    | -   | 8,734,243   | -  |
| U.S. Treasury obligations   | -            | -   | -   | -  |
| U.S. agency obligations   | 1,385,328    | -   | 1,385,328   | -  |
| Other   | 92,105       | -   | 92,105  | -  |
| Deferred compensation plan assets -<br>equity and fixed income mutual funds | 4,447,821    | -   | 4,447,821   | -  |
| Beneficial interest in perpetual trust                                      | 71,938       | -   | 71,938  | -  |
| Interest rate swap agreement  | (2,508,065)  | -   | (2,508,065)   | -  |
| <b>September 30, 2016</b>   |              |   |   |  |
| Investments and cash equivalents  |              |   |   |  |
| Cash equivalents - money market funds                                       | \$ 1,164,580 | \$ 1,164,580  | \$ -  | \$ -   |
| Equity securities   | 18,836,307   | 18,836,307  | -   | -  |
| Corporate obligations   | 7,674,204    | -   | 7,674,204   | -  |
| U.S. Treasury obligations   | 482,757      | 482,757   | -   | -  |
| U.S. agency obligations   | 1,831,134    | -   | 1,831,134   | -  |
| Other   | 170,000      | -   | 170,000   | -  |
| Deferred compensation plan assets -<br>equity and fixed income mutual funds | 3,769,436    | -   | 3,769,436   | -  |
| Beneficial interest in perpetual trust                                      | 120,323      | -   | 120,323   | -  |
| Interest rate swap agreement  | (3,878,971)  | -   | (3,878,971)   | -  |

**Gifford Health Care, Inc.**  
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Following is a description of the valuation methodologies and inputs used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended September 30, 2017.

***Investments and Cash Equivalents***

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. GHC has no securities classified as Level 3.

***Beneficial Interest in Perpetual Trust***

Fair value is estimated at the present value of the future distributions expected to be received over the term of the agreements. Due to the nature of the valuation inputs, the interest is classified within Level 2 of the hierarchy.

***Interest Rate Swap Agreement***

The fair value is estimated using forward-looking interest rate curves and discounted cash flows that are observable or can be corroborated by observable market data and, therefore, are classified within Level 2 of the valuation hierarchy.

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying balance sheets at amounts other than fair value.

***Cash and Cash Equivalents***

The carrying amount approximates fair value.

**Gifford Health Care, Inc.**  
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**September 30, 2017 and 2016**

**Note 15: Related Party Transactions**

GHC receives support from the Gifford Medical Center Auxiliary (Auxiliary), which is a not-for-profit thrift shop. At September 30, 2017 and 2016, GHC had a \$333,000 and \$435,000, respectively, pledge receivable from the Auxiliary, which is included in other current receivables and other long-term assets.

**Note 16: 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 allowances for adjustments included in net patient service revenue are described in *Notes 1* and *2*.

***Malpractice Claims***

Estimates related to the accrual for medical malpractice claims are described in *Notes 1* and *6*.

***Self-Insurance***

GHC is self-insured for employee health care benefits. Stop loss coverage is purchased for any claimant with over \$200,000 of claims in the policy year. GHC accrues a liability for self-insured losses by charging the statement of operations for certain known claims and reasonable estimates for incurred but not reported claims based on claims experience and premiums paid. The amount of actual losses incurred could differ materially from these estimates in the near term.

***Litigation***

In the normal course of business, GHC is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by GHC's self-insurance program (discussed elsewhere in these notes) or by commercial insurance; for example, allegations regarding employment practices or performances of contracts. GHC evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of ultimate expected loss, if any, for each of these matters. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

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**September 30, 2017 and 2016**

***Investments***

GHC invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying balance sheet.

***340B Drug Pricing Program***

GHC participates in the 340B Drug Pricing Program (340B Program) which provides discounted prices from drug manufacturers on outpatient pharmaceutical purchases. The 340B Program is overseen by the Health Resources and Services Administration (HRSA) Office of Pharmacy Affairs (OPA). HRSA is currently conducting routine audits at participating health care organizations and increasing its compliance monitoring processes. Laws and regulations governing the 340B Program are complex and subject to interpretation and change. As a result, it is reasonably possible that material changes to financial statement amounts related to the 340B Program could occur in the near term.

## **Supplementary Information**

**Gifford Health Care, Inc.**  
**Consolidating Schedule – Balance Sheet Information**  
**September 30, 2017**

**Assets**

|   | <b>GMC</b>                 | <b>GRC</b>                  | <b>GHC</b>                 | <b>Eliminations</b>          | <b>Total</b>                |
|---|----------------------------|-----------------------------|----------------------------|------------------------------|-----------------------------|
| <b>Current Assets</b>                       |                            |                             |                            |                              |                             |
| Cash and cash equivalents                   | \$ 1,145,124               | \$ 1,355,056                | \$ 96,986                  | \$ -                         | \$ 2,597,166                |
| Short-term investments                      | 2,167,825                  | -                           | -                          | -                            | 2,167,825                   |
| Patient accounts receivable                 | 8,499,336                  | 447,056                     | 1,037,394                  | -                            | 9,983,786                   |
| Other receivables                           | 464,447                    | -                           | 74,897                     | -                            | 539,344                     |
| Estimated amounts due from<br>third parties | 500,000                    | -                           | 39,373                     | -                            | 539,373                     |
| Supplies                                    | 1,368,956                  | 5,713                       | 48,640                     | -                            | 1,423,309                   |
| Prepaid expenses and other                  | 1,395,466                  | 77,266                      | 370,153                    | -                            | 1,842,885                   |
| Due from affiliate                          | <u>6,412,116</u>           | <u>1,849</u>                | <u>-</u>                   | <u>(6,413,965)</u>           | <u>-</u>                    |
| Total current assets                        | 21,953,270                 | 1,886,940                   | 1,667,443                  | (6,413,965)                  | 19,093,688                  |
| <b>Assets Limited as to Use</b>             | 22,836,249                 | -                           | -                          | -                            | 22,836,249                  |
| <b>Long-Term Investments</b>                | 9,002,599                  | 100,035                     | -                          | -                            | 9,102,634                   |
| <b>Property and Equipment, Net</b>          | 39,329,212                 | 13,675,010                  | 439,629                    | -                            | 53,443,851                  |
| <b>Other Assets</b>                         | <u>4,550,403</u>           | <u>-</u>                    | <u>-</u>                   | <u>-</u>                     | <u>4,550,403</u>            |
| Total assets                                | <u><u>\$97,671,733</u></u> | <u><u>\$ 15,661,985</u></u> | <u><u>\$ 2,107,072</u></u> | <u><u>\$ (6,413,965)</u></u> | <u><u>\$109,026,825</u></u> |



## Liabilities and Net Assets

|   | <b>GMC</b>          | <b>GRC</b>           | <b>GHC</b>          | <b>Eliminations</b>   | <b>Total</b>         |
|---|---------------------|----------------------|---------------------|-----------------------|----------------------|
| <b>Current Liabilities</b>                  |                     |                      |                     |                       |                      |
| Current portion of long-term debt           | \$ 619,956          | \$ 241,988           | \$ -                | \$ -                  | \$ 861,944           |
| Accounts payable                            | 3,575,746           | 243,421              | 244,406             | -                     | 4,063,573            |
| Accrued expenses                            | 5,111,097           | 1,171,596            | 1,496,338           | -                     | 7,779,031            |
| Estimated amounts due to third-party payers | 319,554             | -                    | -                   | -                     | 319,554              |
| Other                                       | 101,194             | 7,000                | -                   | -                     | 108,194              |
| Due to affiliate                            | -                   | 2,603,333            | 3,810,632           | (6,413,965)           | -                    |
| Total current liabilities                   | <u>9,727,547</u>    | <u>4,267,338</u>     | <u>5,551,376</u>    | <u>(6,413,965)</u>    | <u>13,132,296</u>    |
| <b>Long-Term Debt</b>                       | 18,750,164          | 10,562,092           | -                   | -                     | 29,312,256           |
| <b>Other Liabilities</b>                    | 4,447,821           | -                    | -                   | -                     | 4,447,821            |
| <b>Deferred Revenue</b>                     | -                   | 2,196,532            | -                   | -                     | 2,196,532            |
| <b>Deferred Annuities</b>                   | 390,547             | 41,122               | -                   | -                     | 431,669              |
| <b>Interest Rate Swap Agreement</b>         | <u>2,508,065</u>    | <u>-</u>             | <u>-</u>            | <u>-</u>              | <u>2,508,065</u>     |
| Total liabilities                           | <u>35,824,144</u>   | <u>17,067,084</u>    | <u>5,551,376</u>    | <u>(6,413,965)</u>    | <u>52,028,639</u>    |
| <b>Net Assets</b>                           |                     |                      |                     |                       |                      |
| Unrestricted                                | 59,732,292          | (1,566,150)          | (3,469,236)         | -                     | 54,696,906           |
| Temporarily restricted                      | 705,719             | 161,051              | 24,932              | -                     | 891,702              |
| Permanently restricted                      | <u>1,409,578</u>    | <u>-</u>             | <u>-</u>            | <u>-</u>              | <u>1,409,578</u>     |
| Total net assets                            | <u>61,847,589</u>   | <u>(1,405,099)</u>   | <u>(3,444,304)</u>  | <u>-</u>              | <u>56,998,186</u>    |
| Total liabilities and net assets            | <u>\$97,671,733</u> | <u>\$ 15,661,985</u> | <u>\$ 2,107,072</u> | <u>\$ (6,413,965)</u> | <u>\$109,026,825</u> |

**Gifford Health Care, Inc.**  
**Consolidating Schedule – Statement of Operations Information**  
**September 30, 2017**

|   | <b>GMC</b>          | <b>GRC</b>          | <b>GHC</b>          | <b>Eliminations</b> | <b>Total</b>        |
|---|---------------------|---------------------|---------------------|---------------------|---------------------|
| <b>Unrestricted Revenues, Gains and Other Support</b>                 |                     |                     |                     |                     |                     |
| Patient service revenue (net of contractual discounts and allowances) | \$ 57,211,522       | \$ 3,710,435        | \$ 8,308,598        | \$ -                | \$ 69,230,555       |
| Provision for doubtful accounts                                       | 2,904,150           | -                   | 492,524             | -                   | 3,396,674           |
| Net patient service revenue less provision for doubtful accounts      | 54,307,372          | 3,710,435           | 7,816,074           | -                   | 65,833,881          |
| Other   | 1,784,770           | 55,226              | 3,292,817           | (413,909)           | 4,718,904           |
| Net assets released from restrictions used for operations             | 145,617             | 10,714              | 27,318              | -                   | 183,649             |
| Total unrestricted revenues, gains and other support                  | <u>56,237,759</u>   | <u>3,776,375</u>    | <u>11,136,209</u>   | <u>(413,909)</u>    | <u>70,736,434</u>   |
| <b>Expenses and Losses</b>  |                     |                     |                     |                     |                     |
| Salaries and wages  | 25,208,783          | 2,652,114           | 9,080,881           | -                   | 36,941,778          |
| Employee benefits   | 6,427,576           | 922,144             | 2,100,700           | -                   | 9,450,420           |
| Purchased services and professional fees                              | 6,311,733           | 566,864             | 890,270             | -                   | 7,768,867           |
| Supplies and other  | 11,481,684          | 1,543,666           | 1,943,681           | (413,909)           | 14,555,122          |
| Depreciation and amortization   | 3,333,791           | 107,782             | 498,451             | -                   | 3,940,024           |
| Interest  | 794,321             | 15,912              | -                   | -                   | 810,233             |
| Total expenses and losses   | <u>53,557,888</u>   | <u>5,808,482</u>    | <u>14,513,983</u>   | <u>(413,909)</u>    | <u>73,466,444</u>   |
| <b>Operating Income (Loss)</b>  | <u>2,679,871</u>    | <u>(2,032,107)</u>  | <u>(3,377,774)</u>  | <u>-</u>            | <u>(2,730,010)</u>  |
| <b>Other Income (Expense)</b>   |                     |                     |                     |                     |                     |
| Investment return   | 3,025,048           | 6,428               | 909                 | -                   | 3,032,385           |
| Change in fair value of interest rate swap agreement                  | 1,370,906           | -                   | -                   | -                   | 1,370,906           |
| Other income  | 88,727              | 12,310              | -                   | -                   | 101,037             |
| Total other income (expense)  | <u>4,484,681</u>    | <u>18,738</u>       | <u>909</u>          | <u>-</u>            | <u>4,504,328</u>    |
| <b>Excess (Deficiency) of Revenues Over Expenses</b>                  | 7,164,552           | (2,013,369)         | (3,376,865)         | -                   | 1,774,318           |
| Net assets released for acquisition of property and equipment         | 444,583             | 4,166               | -                   | -                   | 448,749             |
| Transfers (to) from affiliates  | (3,554,183)         | 1,010,044           | 2,544,139           | -                   | -                   |
| <b>Increase (Decrease) in Unrestricted Net Assets</b>                 | <u>\$ 4,054,952</u> | <u>\$ (999,159)</u> | <u>\$ (832,726)</u> | <u>\$ -</u>         | <u>\$ 2,223,067</u> |