BerryDunn

# PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

## CONSOLIDATED FINANCIAL STATEMENTS

**with**

## SUPPLEMENTARY INFORMATION

**September 30, 2016 and 2015**

**With Independent Auditor's Report**

**PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES**

**September 30, 2016 and 2015**

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# INDEPENDENT AUDITOR'S REPORT

Board of Directors
Porter Medical Center, Inc. and Subsidiaries

We have audited the accompanying consolidated financial statements of Porter Medical Center, Inc. and Subsidiaries (Medical Center), which comprise the consolidated balance sheets as of September 30, 2016 and 2015, 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 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 U.S. generally accepted accounting principles; 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 U.S. generally accepted auditing standards. 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 Medical Center'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 Medical Center's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the 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 Porter Medical Center, Inc. and Subsidiaries as of September 30, 2016 and 2015, and the results of their operations, changes in their net assets and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

**Other Matter**

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary consolidating information 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Berry Dunn McNeil & Parker, LLC

Manchester, New Hampshire
January 24, 2017
Registration No. 92-0000278

**PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES**

**Consolidated Balance Sheets**

**September 30, 2016 and 2015**

**ASSETS**

| | **2016** | 2015 |
|---|---|---|
| Current assets | | |
| Cash and cash equivalents | **$ 16,523,986** | $ 13,088,494 |
| Assets limited as to use | **176,315** | 83,947 |
| Patient accounts receivable, net | **10,261,486** | 10,744,637 |
| Other receivables, net | **1,197,272** | 1,464,965 |
| Supplies | **1,561,121** | 1,180,421 |
| Prepaid expenses and other | **687,862** | 1,241,936 |
| Resident deposits | **25,425** | 16,786 |
| Total current assets | **30,433,467** | 27,821,186 |
| Assets limited as to use, deferred compensation plan assets | **1,693,172** | 1,875,401 |
| Long-term investments | **5,768,919** | 4,987,942 |
| Property and equipment, net | **22,159,113** | 23,264,963 |
| Beneficial interest in perpetual trusts | **3,327,709** | 3,431,932 |
| Total assets | **$ 63,382,380** | $ 61,381,424 |

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

## LIABILITIES AND NET ASSETS

| | **2016** | 2015 |
|---|---|---|
| Current liabilities | | |
| Current portion of long-term debt | **$ 960,128** | $ 933,803 |
| Accounts payable and accrued expenses | **2,696,485** | 3,034,858 |
| Resident deposits | **25,425** | 16,786 |
| Accrued payroll and related liabilities | **3,722,968** | 2,443,871 |
| Accrued compensated absences | **3,116,667** | 3,221,503 |
| Estimated third-party settlements | **1,161,165** | 1,625,181 |
| Total current liabilities | **11,682,838** | 11,276,002 |
| Liability for pension benefits | **7,570,325** | 6,474,323 |
| Deferred compensation | **1,692,498** | 1,874,728 |
| Long-term debt, net of current portion | **14,922,387** | 15,872,864 |
| Total liabilities | **35,868,048** | 35,497,917 |
| Net assets | | |
| Unrestricted | **23,719,205** | 21,848,132 |
| Temporarily restricted | **349,736** | 485,761 |
| Permanently restricted | **3,445,391** | 3,549,614 |
| Total net assets | **27,514,332** | 25,883,507 |
| Total liabilities and net assets | **$ 63,382,380** | $ 61,381,424 |

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

### Consolidated Statements of Operations

### Years Ended September 30, 2016 and 2015

| | 2016 | 2015 |
|---|---|---|
| Unrestricted revenues, gains and other support | | |
| Patient service revenue (net of contractual allowances and discounts) | **$ 86,672,267** | $ 83,761,851 |
| Less provision for bad debts | **2,754,861** | 3,310,896 |
| Net patient service revenue | **83,917,406** | 80,450,955 |
| Other operating revenue | **2,840,458** | 3,828,874 |
| Net assets released from restrictions used for operations | **3,172** | 12,711 |
| Total unrestricted revenues, gains and other support | **86,761,036** | 84,292,540 |
| Expenses | | |
| Professional care of patients | **47,590,193** | 46,567,977 |
| General services | **4,971,298** | 5,323,643 |
| Administrative and fiscal services | **26,753,652** | 25,654,006 |
| Health care improvement tax | **4,730,715** | 4,563,438 |
| Depreciation and amortization | **3,212,878** | 3,387,317 |
| Interest | **483,135** | 406,587 |
| Total expenses | **87,741,871** | 85,902,968 |
| Operating loss | **(980,835)** | (1,610,428) |
| Nonoperating gains (losses) | | |
| Contributions | **562,633** | 459,609 |
| Investment return | **61,000** | 155,144 |
| Other program income, net | **2,972,889** | 3,364,930 |
| Loss on debt refinancing | **-** | (189,876) |
| Nonoperating gains, net | **3,596,522** | 3,789,807 |
| Excess of revenues, gains, other support and nonoperating gains (losses) over expenses | **2,615,687** | 2,179,379 |
| Net assets released from restrictions used for purchase of property and equipment | **179,942** | 128,333 |
| Change in net assets to recognize funded status of pension plan | **(924,556)** | (1,527,100) |
| Increase in unrestricted net assets | **$ 1,871,073** | $ 780,612 |

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

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

## Consolidated Statements of Changes in Net Assets

## Years Ended September 30, 2016 and 2015

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| Balances, October 1, 2014 | $ 21,067,520 | $ 366,904 | $ 3,603,171 | $ 25,037,595 |
| Excess of revenues, gains, other support and nonoperating gains (losses) over expenses | 2,179,379 | - | - | 2,179,379 |
| Net assets released from restrictions for operations | - | (12,711) | - | (12,711) |
| Net assets released from restrictions used for purchase of property and equipment | 128,333 | (128,333) | - | - |
| Change in net assets to recognize funded status of pension plan | (1,527,100) | - | - | (1,527,100) |
| Contributions | - | 259,901 | - | 259,901 |
| Change in beneficial interest in perpetual trusts | - | - | (53,557) | (53,557) |
| Net increase (decrease) in net assets | 780,612 | 118,857 | (53,557) | 845,912 |
| Balances, September 30, 2015 | 21,848,132 | 485,761 | 3,549,614 | 25,883,507 |
| Excess of revenues, gains, other support and nonoperating gains (losses) over expenses | **2,615,687** | **-** | **-** | **2,615,687** |
| Net assets released from restrictions used for operations | **-** | **(3,172)** | **-** | **(3,172)** |
| Net assets released from restrictions used for purchase of property and equipment | **179,942** | **(179,942)** | **-** | **-** |
| Change in net assets to recognize funded status of pension plan | **(924,556)** | **-** | **-** | **(924,556)** |
| Contributions | **-** | **47,089** | **-** | **47,089** |
| Change in beneficial interest in perpetual trusts | **-** | **-** | **(104,223)** | **(104,223)** |
| Net increase (decrease) in net assets | **1,871,073** | **(136,025)** | **(104,223)** | **1,630,825** |
| Balances, September 30, 2016 | **$ 23,719,205** | **$ 349,736** | **$ 3,445,391** | **$ 27,514,332** |

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

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

### Consolidated Statements of Cash Flows

### Years Ended September 30, 2016 and 2015

| | 2016 | 2015 |
|---|---|---|
| Cash flows from operating activities | | |
| Change in net assets | **$ 1,630,825** | $ 845,912 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities | | |
| Loss on disposal of property and equipment | **339,513** | 155,032 |
| Depreciation and amortization | **3,212,878** | 3,387,317 |
| Provision for bad debts | **2,754,861** | 3,310,896 |
| Loss on debt refinancing | **-** | 189,876 |
| Net realized and unrealized gains on investments | **-** | (131,006) |
| Change in net assets to recognize funded status of pension plan | **924,556** | 1,527,100 |
| Change in beneficial interest in perpetual trusts | **104,223** | 53,557 |
| Restricted contributions for long-term purposes | **(142,090)** | (181,275) |
| (Increase) decrease in | | |
| Patient accounts receivable, net | **(2,271,710)** | (3,581,030) |
| Assets limited as to use | **(109,164)** | - |
| Supplies, prepaids and other current assets | **441,067** | 2,019,068 |
| Increase (decrease) in | | |
| Accounts payable and accrued expenses | **(338,373)** | (1,680,174) |
| Accrued payroll and related liabilities | **1,174,261** | 306,155 |
| Estimated third-party settlements | **(464,016)** | (501,683) |
| Other current liabilities | **171,446** | 352,429 |
| Net cash provided by operating activities | **7,428,277** | 6,072,174 |
| Cash flows from investing activities | | |
| Purchase of investments | **(143,588)** | (122,130) |
| Proceeds from sale of investments | **244,132** | 4,668,081 |
| Change in investments held at Middlebury College | **(864,725)** | (4,776,553) |
| Purchase of property and equipment | **(2,438,076)** | (3,122,820) |
| Proceeds from sale of property and equipment | **200** | 1,950 |
| Net cash used by investing activities | **(3,202,057)** | (3,351,472) |
| Cash flows from financing activities | | |
| Restricted contributions for long-term purposes | **142,090** | 181,275 |
| Payment of debt issuance costs | **-** | (173,024) |
| Proceeds from issuance of long-term debt | **-** | 15,673,923 |
| Principal payments on long-term debt | **(932,818)** | (17,115,761) |
| Net cash used by financing activities | **(790,728)** | (1,433,587) |
| Net increase in cash and cash equivalents | **3,435,492** | 1,287,115 |
| Cash and cash equivalents, beginning of year | **13,088,494** | 11,801,379 |
| Cash and cash equivalents, end of year | **$ 16,523,986** | $ 13,088,494 |
| Supplemental cash flows information | | |
| Interest paid | **$ 483,181** | $ 406,515 |
| Noncash transaction - acquisition of fixed assets in exchange for long-term debt | **$ -** | $ 393,213 |

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

## Nature of Operations and Principles of Consolidation

Porter Medical Center, Inc. (PMC) was organized in 1986 to serve as a parent holding company for the following subsidiaries:

*Porter Hospital, Inc. (Hospital)*: The Hospital operates a 25-bed not-for-profit critical access hospital.

*Helen Porter Nursing Home, Inc. (HPNH)*: HPNH operates a 105-bed not-for-profit long-term community oriented skilled healthcare and rehabilitation center.

*Porter Real Estate Holdings, LLC (PREH)*: PREH is a single-member LLC real estate holding company that is owned 100% by PMC.

All of the companies are Vermont corporations and operate out of facilities in Middlebury, Vermont, and surrounding areas. All subsidiaries are 100% owned and/or controlled by PMC.

The consolidated financial statements include the accounts of PMC, the Hospital, HPNH, and PREH (collectively, Medical Center). Significant intercompany accounts and transactions have been eliminated in consolidation.

## 1. Summary of Significant Accounting Policies

### Basis of Presentation

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification Topic (ASC) 958, *Not-For-Profit Entities*. Under FASB ASC 958 and FASB ASC 954, *Health Care Entities*, all not-for-profit healthcare organizations are required to provide a balance sheet, a statement of operations, a statement of changes in net assets, and a statement of cash flows. FASB ASC 954 requires reporting amounts for an organization's total assets, liabilities, and net assets in a balance sheet; reporting the change in an organization's net assets in statements of operations and changes in net assets; and reporting the change in its cash and cash equivalents in a statement of cash flows.

### Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP) 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

Cash and cash equivalents include all liquid investments with original maturities of three months or less, other than deferred compensation plan investments and long-term investments, to be cash equivalents. At September 30, 2016 and 2015, cash equivalents consisted primarily of money market accounts with brokers and certificates of deposit.

## Investments and Investment Return

Investments in equity securities having a readily determinable fair value and all investments in debt securities are measured at fair value in the balance sheets. Investment return or loss (including realized gains and losses on investments, interest and dividends) is included in nonoperating gains unless the income or loss is restricted by donor or law. The Medical Center adopted FASB ASC 825, *Financial Instruments*, effective October 1, 2008, and has elected the fair value option relative to its investments which consolidates all investment performance activity within the nonoperating gains section of the statements of operations.

Investments are exposed to various risks, such as interest rate, credit, and overall market volatility. As such, it is reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the balance sheets.

## Assets Limited as to Use

Assets limited as to use are HPNH restricted donations and assets held by trustees under indenture agreements and deferred compensation plan assets and are comprised of cash and short-term investments at September 30, 2016 and 2015. Amounts required to meet current liabilities of the Medical Center are included in current assets.

## Patient Accounts Receivable

Patient accounts receivable are stated at the amount management expects to collect for services rendered from third-party payors, patients and others. Management provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions. Accounts are considered delinquent and subsequently written off as uncollectible based on individual credit evaluation and specific circumstances of the account.

In evaluating the collectibility of accounts receivable, the Medical Center analyzes past results and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts. For receivables associated with self-pay patients (which include both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Medical Center records a provision for bad debts in the period of service based on past experience, which indicates that many patients are unable or unwilling to pay amounts for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or eligible) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged against the allowance for doubtful accounts.

**Supplies**

The Medical Center records 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, or, if contributed, at fair market value determined at the date of donation. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the asset's estimated useful life. Such amortization is included in depreciation and amortization in the financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from the excess of revenues, gains, other support and nonoperating gains (losses) over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

**Land Lease**

The Medical Center has multiple land lease agreements with Middlebury College, upon which the entire main campus is located, inclusive of HPNH and outer lying modular office buildings. The terms of the leases are renewed and extended from year to year, indefinitely, until one party gives to the other party written notice of termination.

**Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are those whose use by the Medical Center 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 the Medical Center in perpetuity.

## Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered and includes estimated retroactive revenue adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and are adjusted in future periods as final settlements are determined.

## Charity Care

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

## Contributions

Unconditional promises to give cash and other assets are recorded at estimated fair value at the date each promise is received. 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. Conditional contributions are reported as liabilities until the condition is eliminated or the contributed assets are returned to the donor. Donor-restricted contributions whose restrictions are met within the same year as received are included in other operating revenue in the accompanying financial statements.

## Excess of Revenues, Gains, Other Support and Nonoperating Gains (Losses) Over Expenses

The statements of operations include excess of revenues, gains and other support over expenses and nonoperating gains. Changes in unrestricted net assets which are excluded from this measure, consistent with industry practice, include defined benefit plan adjustments, permanent transfers of assets 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).

## Income Taxes

PMC, the Hospital, and HPNH are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code and are exempt from federal income taxes on related income. PREH is a single member LLC owned 100% by PMC and is considered a disregarded entity for tax purposes.

### Subsequent Events

For purposes of the preparation of these financial statements in conformity with U.S. GAAP, the Medical Center has considered transactions or events occurring through January 24, 2017, which was the date the financial statements were issued.

Effective October 5, 2016, the Medical Center signed a non-binding letter of intent to become an affiliate of the University of Vermont Health Network as early as the spring of 2017.

## 2. Net Patient Service Revenue and Patient Accounts Receivable

### Net Patient Service Revenue

Patient service revenue and contractual and other allowances consisted of the following for the years ended September 30:

| | **2016** | 2015 |
|---|---|---|
| Inpatient | **$ 48,821,846** | $ 48,630,348 |
| Outpatient | **119,862,035** | 106,628,515 |
| Gross patient service revenue | **168,683,881** | 155,258,863 |
| Less Medicare and Medicaid allowances | **55,913,478** | 47,671,729 |
| Less other contractual allowances | **24,659,172** | 22,653,763 |
| Less charity care and other discounts | **1,438,964** | 1,171,520 |
| | **82,011,614** | 71,497,012 |
| Patient service revenue (net of contractual allowances and discounts) | **86,672,267** | 83,761,851 |
| Less provision for bad debts | **2,754,861** | 3,310,896 |
| Net patient service revenue | **$ 83,917,406** | $ 80,450,955 |

## Patient Accounts Receivable

Patient accounts receivable consisted of the following at September 30:

| | **2016** | 2015 |
|---|---|---|
| Gross patient accounts receivable | **$ 21,585,145** | $ 21,599,308 |
| Less: Estimated contractual allowances | **7,561,768** | 7,356,659 |
| Estimated allowance for doubtful accounts and charity care | **3,761,891** | 3,498,012 |
| Net patient accounts receivable | **$ 10,261,486** | $ 10,744,637 |

During 2016, the Medical Center increased its estimate from $2,321,483 to $2,703,150 in the allowance for doubtful accounts relating to self-pay patients and decreased such estimate from $1,176,529 to $1,058,741 for doubtful accounts relating to third-party payors. During 2015, the Hospital increased its estimate from $2,038,245 to $2,321,483 in the allowance for doubtful accounts relating to self-pay patients and increased such estimate from $776,237 to $1,176,529 for doubtful accounts relating to third-party payors. During 2016, self-pay write-offs decreased from $3,050,571 to $2,738,470. During 2015, self-pay write-offs increased from $2,328,416 to $3,050,571. Such variations resulted from changes experienced in the collection of amounts from self-pay patients and third-party payors. The increase in the allowance for doubtful accounts relating to self-pay patients is due to the deterioration in the age of such accounts.

The Medical Center has agreements with third-party payors that provide for payments to the Medical Center at amounts different from its established rates. These payment arrangements include:

## Medicare

On December 31, 2005, the Hospital became a critical access hospital (CAH). As a CAH, the Hospital is reimbursed at 101% of reasonable allowable costs for its inpatient and outpatient services, excluding ambulance services, provided to Medicare patients. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Centers for Medicare & Medicaid Services (Medicare or CMS) fiscal intermediary. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2013.

HPNH is paid under a prospective payment system for Medicare Part A services. Under the prospective payment system, there is no additional settlement on the difference between the interim rates paid and actual costs. HPNH is paid on a fee schedule basis for Medicare Part B therapy services; therefore, there will be no additional settlement on the difference between payments received and actual costs for Part B therapy services.

**Medicaid**

The Hospital's inpatient services rendered to Office of Vermont Health Access (Medicaid) program beneficiaries are reimbursed at prospectively-determined rates. The prospectively-determined rates are not subject to retroactive adjustment. Outpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively-determined rates and therefore are not subject to retroactive adjustments. The Hospital's Medicaid cost reports have been audited through September 30, 2012.

HPNH is reimbursed for services rendered to Title XIX Medicaid patients on the basis of prospectively-determined per diem rates, subject to a quarterly case mix index adjustment established by the State of Vermont. The reimbursement plan is on a prospective basis and, subject to certain limitations, no additional settlement will be made on the difference between the estimated per diem rates paid and actual costs.

**Other Arrangements**

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

Approximately 60% and 59% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended September 30, 2016 and 2015, respectively. The Hospital has agreements with Medicare and Medicaid. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs. Differences between amounts previously estimated and amounts subsequently determined to be recoverable or payable are included in net patient service revenues in the year the amounts become known. Net patient service revenue increased by approximately $66,000 and $899,000 in 2016 and 2015, respectively, due to removal of allowances or recognition of settlements no longer subject to audits, reviews and investigations.

The Hospital recognizes patient service revenue associated with services rendered to patients who have third-party payor coverage on the basis of contractual rates for such services. For uninsured patients that do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates (or on the basis of discounted rates, if negotiated or provided by policy). Based on historical trends, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services rendered. Thus, the Hospital records a provision for bad debts related to uninsured patients in the period the services are rendered. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized during the fiscal year ended September 30, 2016 totaled $86,672,267, of which $83,162,952 was revenue from third-party payors and $3,509,315 was revenue from self-pay patients. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized during the fiscal year ended September 30, 2015 totaled $83,761,851, of which $79,561,652 was revenue from third-party payors and $4,200,199 was revenue from self-pay patients.

## 3. Community Benefit

The Hospital provides services without charge, or at amounts less than its established rates, to patients who meet the criteria of its charity care policy. The criteria for charity care, which is granted on a sliding scale, consider gross income and family size as compared to the federal poverty guidelines (FPL). The maximum of 100% charity care will be granted if the gross income of the individual is up to 200% of FPL.

The net cost of charity care provided was approximately $698,344 in 2016 and $618,135 in 2015. The total cost estimate is based on an overall financial statement cost to charge ratio applied against gross charity care charges. In 2016 and 2015, .92% and .82%, respectively, of all services as defined by percentage of gross revenue was provided on a charity basis.

80 inpatients received their entire episode of service on a charity case basis in 2016 and 2015.

In 2016, a total of 2,232 outpatients received their entire episode of service on a charity case basis. In 2015, a total of 2,044 outpatients received their entire episode of service on a charity case basis.

## 4. Investments and Investment Return

Assets limited as to use consisted of the following at September 30:

| | **2016** | 2015 |
|---|---|---|
| Helen Porter - Restricted Donations | | |
| Cash and cash equivalents | **$ 176,315** | $ 83,947 |
| Deferred compensation | | |
| Mutual funds | **$ 1,693,172** | $ 1,875,401 |

Long-term investments consisted of the following at September 30:

| | **2016** | 2015 |
|---|---|---|
| Cash and cash equivalents | **$ 124,797** | $ 211,389 |
| Marketable equity securities | **2,845** | - |
| Investments held by Middlebury College | **5,641,277** | 4,776,553 |
| | **$ 5,768,919** | $ 4,987,942 |

Investments by Middlebury College are part of a pooled fund.

Total investment return is comprised of the following for the years ending September 30:

| | **2016** | 2015 |
|---|---|---|
| Interest and dividend income | **$ 196,276** | $ 247,585 |
| Net unrealized losses | **-** | (396,175) |
| Realized gains | **-** | 527,181 |
| Net depreciation of investments held at Middlebury College | **(135,276)** | (223,447) |
| | **$ 61,000** | $ 155,144 |

## 5. Property and Equipment

The major categories of property and equipment are as follows at September 30:

| | **2016** | 2015 |
|---|---|---|
| Land and land improvements | **$ 2,559,801** | $ 2,563,883 |
| Buildings and leasehold improvements | **32,419,237** | 32,174,033 |
| Equipment | **24,016,133** | 26,407,707 |
| Construction in progress | **254,325** | 428,826 |
| | **59,249,496** | 61,574,449 |
| Less accumulated depreciation | **(37,090,383)** | (38,309,486) |
| Property and equipment, net | **$ 22,159,113** | $ 23,264,963 |

## 6. Beneficial Interest in Perpetual Trusts

The Hospital is an income beneficiary of two perpetual trusts controlled by an unrelated third-party trustee. The beneficial interests in the assets of these trusts are included in the Medical Center's financial statements as permanently restricted net assets. Income is distributed in accordance with the individual trust documents and is included in investment return. Trust income distributed to the Medical Center for the years ended September 30, 2016 and 2015 was $162,396 and $151,446, respectively.

## 7. Borrowings

Long-term debt consists of the following as of September 30:

| | **2016** | 2015 |
|---|---|---|
| Vermont Educational and Health Buildings Finance Agency (VEHBFA) Revenue Bond Refunding Series 2015A, with fixed interest at 2.85%, payable in monthly payments of $69,211 including principal and interest, through August 2035; collateralized by the gross receipts of the Hospital. These bonds are puttable by the purchaser on or after August 1, 2025. | **$12,133,512** | $ 12,609,832 |
| VEHBFA Demand Revenue Bonds Series 2015A bonds with fixed interest at 2.85%, due in monthly payments of $16,961 including principal and interest through August 2035; collateralized by gross receipts of HPNH. The bonds are puttable by the purchaser on or after August 1, 2025. | **2,973,430** | 3,090,156 |
| Variable rate note payable to a bank (3.0% at September 30, 2016), due in monthly payments of $2,345 including principal and interest, due in full February 2021; collateralized by property, guaranteed by the Hospital. | **116,374** | 140,828 |
| Note payable at a fixed interest rate of 2.78%, monthly payments of $5,690 including principal and interest, due in full February 2020; collateralized by certain property. | **221,860** | 282,975 |
| Note payable at a variable interest rate (4.0% at September 30, 2016), monthly payments of $1,743 including principal and interest with the remaining principal due in March 2019; collateralized by certain property. | **136,755** | 151,588 |
| Note payable at a fixed interest rate of 4.0%, monthly payments of $2,597 including principal and interest, due in full in September 2018; collateralized by certain property. | **59,764** | 87,825 |
| Capital lease obligations, at various rates with monthly payments ranging from $134 to $14,317 due 2017 through 2019; collateralized by leased equipment. | **404,022** | 615,330 |
| Total long-term debt before debt issuance costs | **16,045,717** | 16,978,534 |
| Unamortized debt issuance costs | **(163,202)** | (171,867) |
| Total long-term debt | **15,882,515** | 16,806,667 |
| Less current portion | **960,128** | 933,803 |
| | **$14,922,387** | $ 15,872,864 |

Aggregate annual maturities of long-term debt and payments on capital lease obligations at September 30, 2016 are:

| | Long-term Debt (Excluding Capital Lease Obligations) | Capital Lease Obligations |
|---|---|---|
| 2017 | $ 744,100 | $ 225,037 |
| 2018 | 766,200 | 189,854 |
| 2019 | 845,400 | 2,889 |
| 2020 | 721,100 | - |
| 2021 | 696,600 | - |
| Thereafter | 11,868,295 | - |
| | $15,641,695 | 417,780 |
| Less amount representing interest | | (13,758) |
| | | $ 404,022 |

In connection with the bond issuance, the Hospital, PMC and HPNH are all members of an Obligated Group. The Obligated Group is required to meet certain financial covenants. The Obligated Group is in compliance with these financial covenants at September 30, 2016 as defined in the Master Trust Indenture and its supplements.

The Hospital guarantees certain third-party debts of PREH. The guarantee terms are for periods of nine and fourteen years. Should the Hospital be obligated to perform under the guarantee agreements, the Hospital may seek reimbursement from the related organization of amounts expended under the guarantees. At September 30, 2016 and 2015, the total outstanding balances on the guaranteed loans were approximately $116,000 and $140,000, respectively.

## 8. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at September 30:

| | **2016** | 2015 |
|---|---|---|
| Health care services | **$ 110,700** | $ 247,924 |
| Purchase of equipment | **2,657** | 2,657 |
| Indigent care | **236,379** | 235,180 |
| | **$ 349,736** | $ 485,761 |

Permanently restricted net assets are restricted to the following at September 30:

| | **2016** | 2015 |
|---|---|---|
| Investments to be held in perpetuity, the income is restricted for indigent care | **$ 117,682** | $ 117,682 |
| Beneficial interests in perpetual trusts, the income is unrestricted | **3,327,709** | 3,431,932 |
| | **$ 3,445,391** | $ 3,549,614 |

## 9. Assets Held in Trust

The Hospital is the income beneficiary of various trusts, over which the trustee has variance power (the power to direct both corpus and income). Because the Medical Center has only a contingent interest in the assets of these trusts, they are not included in the Medical Center's financial statements. The fair value of the assets totaled approximately $4,040,000 and $4,160,000 on September 30, 2016 and 2015, respectively. Distributions of income are made at the discretion of the trustees. Income distributed to the Hospital by the trust is restricted for indigent care and amounted to $235,338 in 2016 and $185,186 in 2015.

## 10. Other Program Income, Net

Other program income, net, predominantly represents the net income resulting from the federal 340(b) Drug Pricing Program (Program). The Program provides for discounts and reduced prices on medications because the Hospital is a qualified federal grantee (as a CAH). In addition to savings for medications used within the Hospital, the Hospital has also established contracts with five local pharmacies during 2016. Revenue from prescriptions filled by these contract pharmacies is recorded as "other program revenue." The Hospital paid all expenses for the drugs dispensed by the contract pharmacies at wholesaler cost. The Hospital also paid the contract pharmacies a dispensing fee for filling the prescriptions. These expenses are treated as "other expense" by the Hospital. Program income of $4,520,244 and $4,917,052 was recorded for the years ended September 30, 2016 and 2015, respectively. Program expenses of $1,545,933 and 1,647,340 were recorded for the years ended September 30, 2016 and 2015, respectively.

## 11. Functional Expenses

The Medical Center provides health care services primarily to residents within its geographic area. Expenses related to providing these services are as follows for the years ended September 30:

| | **2016** | 2015 |
|---|---|---|
| Health care services | **$ 78,776,593** | $ 76,408,037 |
| General and administrative | **8,965,278** | 9,494,931 |
| | **$ 87,741,871** | $ 85,902,968 |

## 12. Concentrations of Credit Risk

Credit Risk

The Medical Center grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at September 30:

| | **2016** | 2015 |
|---|---|---|
| Medicare | **29 %** | 27 % |
| Medicaid | **14** | 17 |
| Other third-party payors | **37** | 36 |
| Patients | **20** | 20 |
| | **100 %** | 100 % |

The Medical Center maintains a substantial portion of its cash and cash equivalents in bank accounts which at times may exceed federally insured limits. The Medical Center has not experienced any losses in such accounts. The Medical Center believes it is not exposed to any significant risk on cash and cash equivalents.

**Labor Force**

The Hospital's unionized labor workforce are members of the Porter Federation of Nurses and Health Professionals, AFT Vermont Local Unit # 5753. The Union contract has been negotiated through September 30, 2017.

## 13. Commitments and Contingencies

**Medical Malpractice Claims**

The Medical Center carries malpractice insurance coverage under a claims-made policy on a fixed premium basis. The Medical Center intends to renew its coverage on a claims-made basis and anticipates such coverage will be available. The Medical Center is subject to complaints, claims and litigation due to potential claims which arise in the normal course of business. U.S. GAAP requires the Medical Center to accrue the ultimate estimated cost of malpractice claims when the incident that gives rise to the claim occurs, without consideration of insurance recoveries. Expected recoveries are presented as a separate asset. Amounts accrued under this provision are included in other receivables and accounts payable and accrued expenses on the balance sheets.

**Self-Insurance**

Effective January 1, 2016, PMC began its self-insurance program and terminated a fully insured health insurance program for its employees. The Medical Center is self-insured for employee health care benefits. The Medical Center accrues a liability for employee health care by charging the statements of operations for certain known claims and reasonable estimates for incurred, but not reported, claims based on claims experience. The amount of actual losses incurred could differ materially from these estimates in the near term.

**Litigation**

In the normal course of business, the Medical Center is, from time-to-time, subject to allegations that may or do result in litigation. The Medical Center 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.

## 14. Benefit Plans

**Defined Contribution Plan**

The Medical Center has a 403(b) defined contribution pension plan covering substantially all employees. The Medical Center makes an employer contribution to the plan. In order to receive the contribution, employees must meet certain eligibility requirements. The Medical Center makes contributions between 3% and 6% of covered payroll based on the employee's years of service and the employee's age as of January 1, 2016.

The Medical Center has estimated a liability of approximately $1,168,000 and $1,066,000 at September 30, 2016 and 2015, respectively, related to the 403(b) plan. This amount has been included in accrued payroll and related liabilities. Contributions are calculated on a calendar year basis, and are paid following the end of the calendar year. Expense under the plan was approximately $1,080,000 and $1,186,000 for the years ended 2016 and 2015, respectively.

**Deferred Compensation Plan**

The Medical Center has a nonqualified deferred compensation plan established under Section 457 of the Internal Revenue Code. These plans cover key employees of the Medical Center. Estimated amounts are accrued at September 30 with amounts transferred to accounts recorded in deferred compensation plan investments on a calendar year basis. Expense under such plans amounted to $19,800 and $79,200 for the years ended 2016 and 2015, respectively.

## Defined Benefit Plan

The Medical Center has a noncontributory defined benefit pension plan covering all employees who meet the eligibility requirements. The Medical Center's funding policy is to make the minimum annual contribution that is required by applicable regulations, plus such amounts as PMC may determine to be appropriate from time-to-time. The Medical Center expects to contribute to the plan in 2016.

The Medical Center has adopted FASB ASC 958-715, *Compensation-Retirement Benefits*. The defined benefit pension plan has been frozen since April 2007; therefore, the adoption of these provisions had no effect on the balance sheets and statements of operations and changes in net assets of the Medical Center, and the accumulated benefit obligation is equal to the projected benefit obligation.

The Medical Center uses a September 30, 2016 measurement date for the plan. Significant balances for the plan as a whole are:

| | **2016** | 2015 |
|---|---|---|
| Benefit obligations | **$ (17,292,540)** | $ (16,013,887) |
| Fair value of plan assets | **9,722,215** | 9,539,564 |
| Funded status | **$ (7,570,325)** | $ (6,474,323) |

The tables below present details about the plan, including components of net periodic benefit cost and certain assumptions used to determine the funded status and cost:

| | **2016** | 2015 |
|---|---|---|
| Change in benefit obligation | | |
| Benefit obligation at beginning of year | **$ 16,013,887** | $ 14,919,052 |
| Interest cost | **672,265** | 624,183 |
| Actuarial loss | **1,669,596** | 962,615 |
| Benefits paid | **(1,063,208)** | (491,963) |
| Benefit obligation at end of year | **$ 17,292,540** | $ 16,013,887 |
| Change in plan assets | | |
| Fair value of plan assets at beginning of year | **$ 9,539,564** | $ 10,324,258 |
| Actual return (loss) on plan assets | **950,079** | (254,295) |
| Employer contributions | **353,839** | - |
| Benefits paid | **(1,063,208)** | (491,963) |
| Expenses paid | **(58,059)** | (38,436) |
| Fair value of plan assets at end of year | **$ 9,722,215** | $ 9,539,564 |

| | **2016** | 2015 |
|---|---|---|
| Components of net periodic benefit cost | | |
| Administrative expense cost | **$ 50,000** | $ - |
| Interest cost | **672,265** | 624,183 |
| Expected return on plan assets | **(537,512)** | (563,214) |
| Amortization of net loss | **340,532** | 291,460 |
| Net periodic benefit cost | **$ 525,285** | $ 352,429 |

Other amounts recognized in the statements of operations relate entirely to actuarial losses.

| | | |
|---|---|---|
| Weighted average assumptions used to determine benefit obligation | | |
| Discount rate | **3.56 %** | 4.35 % |
| Weighted average assumptions used to determine benefit cost | | |
| Discount rate | **4.35** | 4.26 |
| Expected return on assets | **5.70** | 5.60 |

The Medical Center has estimated the long-term rate of return on plan assets based primarily on historical returns on plan assets, adjusted for changes in target portfolio allocations and recent changes in long-term interest rates based on publicly available information.

The following benefit payments are expected to be paid over the next ten years as of September 30, 2016:

| | |
|---|---|
| 2017 | $ 655,394 |
| 2018 | 704,807 |
| 2019 | 757,563 |
| 2020 | 822,144 |
| 2021 | 842,382 |
| 2022 - 2026 | 4,760,113 |

Plan assets are held by a bank-administered trust fund, which invests the plan assets in accordance with the provisions of the plan agreement. The plan agreement permits investment in common stocks, corporate bonds and debentures, U.S. government securities, certain insurance contracts, real estate and other specified investments, based on certain target allocation percentages.

Asset allocation is primarily based on a strategy to provide stable earnings while still permitting the plan to recognize potentially higher returns through a limited investment in equity securities. Plan assets are rebalanced quarterly. At September 30, plan assets by category are as follows:

| | 2016 | 2015 |
|---|---|---|
| Equity funds | **55 %** | 52 % |
| Debt funds | **33** | 29 |
| Cash and cash equivalents | **2** | 3 |
| International funds | **10** | 16 |
| | **100 %** | 100 % |

The targeted asset allocation ranges for the plan are as follows:

| | Ranges |
|---|---|
| Equity funds | 0 - 60% |
| Fixed income funds | 30 - 100 |
| Short-term investments or funds | 0 - 20 |
| Alternative investments or funds | 0 - 10 |

In the next year, $406,929 is expected to be recognized as a component of net periodic benefit cost related to net actuarial loss previously recognized in unrestricted net assets. The total amount to be amortized into pension expense in future years is $5,500,000. No plan assets are expected to be returned to the Medical Center in 2017. The Medical Center expects to contribute $645,557 to the plan in 2017.

**Risks**

The plan 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 changes could materially affect the amounts reported.

## 15. Health Care Improvement Tax

Effective July 1, 1991, a health care improvement tax was imposed on medical centers, nursing homes and home health agencies as part of a program to upgrade services in Vermont. The State of Vermont pays the Hospital with funds received from the health care improvement trust fund and federal matching funds. The assessment rate for subsequent years will be determined annually by the Vermont General Assembly.

## 16. Operating Leases

Noncancelable operating leases at the Hospital for primary care outpatient offices expire in various years through September 2020. These leases generally contain renewal options for periods ranging from three to six years and require the Hospital to pay all executory costs.

Future minimum lease payments at September 30 are as follows:

| | |
|---|---|
| 2017 | $ 632,700 |
| 2018 | 505,800 |
| 2019 | 490,500 |
| 2020 | 490,500 |
| 2021 | 312,500 |
| Thereafter | 423,100 |
| | $ 2,855,100 |

Rent expense during 2016 and 2015 amounted to $809,674 and $968,471, respectively.

## 17. Fair Value Measurements and Disclosures

FASB ASC 820, *Fair Value Measurement*, defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

**Level 1:** Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

**Level 2:** Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

**Level 3:** Significant unobservable inputs that reflect an entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Assets at fair value on a recurring basis are summarized below:

| | Fair Value Measurements at September 30, 2016 | | | |
|---|---|---|---|---|
| | Total | Quoted Prices In Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| PMC Assets: | | | | |
| Investments | | | | |
| Cash and cash equivalents | **$ 124,797** | **$ 124,797** | **$ -** | **$ -** |
| Marketable equity securities | **2,845** | **2,845** | **-** | **-** |
| Investments held by Middlebury College | **5,641,277** | **-** | **-** | **5,641,277** |
| Deferred compensation plan assets | **1,693,172** | **1,693,172** | **-** | **-** |
| Beneficial interest in perpetual trusts | **3,327,709** | **-** | **-** | **3,327,709** |
| Total PMC assets | **$ 10,789,800** | **$ 1,820,814** | **$ -** | **$ 8,968,986** |
| Pension assets: | | | | |
| Cash and cash equivalents | **$ 178,750** | **$ 178,750** | **$ -** | **$ -** |
| Mutual funds | **9,543,465** | **9,543,465** | - | - |
| Total pension assets | **$ 9,722,215** | **$ 9,722,215** | $ - | $ - |

| | Fair Value Measurements at September 30, 2015 | | | |
|---|---|---|---|---|
| | Total | Quoted Prices In Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| PMC Assets: | | | | |
| Investments | | | | |
| Cash and cash equivalents | $ 211,389 | $ 211,389 | $ - | $ - |
| Investments held by Middlebury College | 4,776,553 | - | - | 4,776,553 |
| Deferred compensation plan assets | 1,875,401 | 1,875,401 | - | - |
| Beneficial interest in perpetual trusts | 3,431,932 | - | - | 3,431,932 |
| Total PMC assets | $ 10,295,275 | $ 2,086,790 | $ - | $ 8,208,485 |
| Pension assets: | | | | |
| Cash and cash equivalents | $ 300,214 | $ 300,214 | $ - | $ - |
| Mutual funds | 9,239,350 | 9,239,350 | - | - |
| Total pension assets | $ 9,539,564 | $ 9,539,564 | $ - | $ - |

Significant activity for assets measured at the fair value on a recurring basis using unobservable inputs (Level 3) is as follows:

| | Investments Held by Middlebury College | Beneficial Interest in Perpetual Trust |
|---|---|---|
| Level 3 investments at October 1, 2014 | $ - | $ 3,485,489 |
| Transfer of assets to Middlebury College | 5,000,000 | - |
| Change in value | (223,447) | (53,557) |
| Level 3 investments at September 30, 2015 | 4,776,553 | 3,431,932 |
| Transfer of assets to Middlebury College | 1,000,000 | - |
| Change in value | (135,276) | (104,223) |
| Level 3 investments at September 30, 2016 | $ 5,641,277 | $ 3,327,709 |

The fair value of Level 3 assets is based on the Medical Center's share of the quoted market prices of the underlying assets of the Middlebury pooled funds and beneficial trusts or of similar securities, as provided by the respective custodians. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. All fair values are provided by investment managers.

## 18. Meaningful Use Revenues

The Medicare and Medicaid electronic health record (EHR) incentive programs provide a financial incentive for achieving "meaningful use" of certified EHR technology. The criteria for meaningful use will be staged in three steps with stage 3 beginning in 2018. The meaningful use attestation is subject to audit by CMS in future years. As part of this process, a final settlement amount for the incentive payments could be established that differs from the initial calculation, and could result in return of a portion or all of the incentive payments received by the Hospital.

The Medicaid program will provide incentive payments to hospitals and eligible professionals as they adopt, implement, upgrade or demonstrate meaningful use in the first year of participation and demonstrate meaningful use for up to five remaining participation years. The Hospital recorded meaningful use revenues of approximately $42,500 and $528,300 in other operating revenue during 2016 and 2015, respectively.

During 2016 and 2015, the Hospital demonstrated meaningful use related to its certified EHR system, allowing the Hospital to be eligible to receive EHR payments from Medicare. The Hospital recorded meaningful use revenues of approximately $100,000 and $153,000 in other operating revenue in 2016 and 2015, respectively.

# SUPPLEMENTARY INFORMATION

**PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES**

**Consolidating - Balance Sheets**

**September 30, 2016**

| **Assets** | Porter Medical Center, Inc. | Porter Hospital, Inc. | Helen Porter Nursing Home, Inc. | Porter Real Estate Holdings, LLC | Eliminations | Consolidated |
|---|---|---|---|---|---|---|
| Current assets | | | | | | |
| Cash and cash equivalents | $ 1,470,343 | $ 14,394,887 | $ 559,481 | $ 99,275 | $ - | $ 16,523,986 |
| Assets limited as to use | 6,998 | 102,166 | 67,151 | - | - | 176,315 |
| Patient accounts receivable, net | - | 9,350,288 | 911,198 | - | - | 10,261,486 |
| Other receivables, net | 68,091 | 1,112,998 | 16,183 | - | - | 1,197,272 |
| Current portion of note receivable, related party | - | 3,497 | - | - | (3,497) | - |
| Supplies | - | 1,547,676 | 13,445 | - | - | 1,561,121 |
| Prepaid expenses and other | - | 678,754 | 9,108 | - | - | 687,862 |
| Resident deposits | - | - | 25,425 | - | - | 25,425 |
| Due from affiliates | 705,018 | 311,368 | 33,843 | 2,282 | (1,052,511) | - |
| Total current assets | 2,250,450 | 27,501,634 | 1,635,834 | 101,557 | (1,056,008) | 30,433,467 |
| Assets limited as to use, deferred compensation plan assets | 914,443 | 778,729 | - | - | - | 1,693,172 |
| Long-term investments | 50,645 | 5,718,274 | - | - | - | 5,768,919 |
| Property and equipment, net | - | 19,849,135 | 1,371,866 | 996,327 | (58,215) | 22,159,113 |
| Beneficial interest in perpetual trusts | - | 3,327,709 | - | - | - | 3,327,709 |
| Note receivable, related party | 741,973 | 16,366 | - | - | (758,339) | - |
| Investment in subsidiary | 959,377 | - | - | - | (959,377) | - |
| Total assets | $ 4,916,888 | $ 57,191,847 | $ 3,007,700 | $ 1,097,884 | $ (2,831,939) | $ 63,382,380 |

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

### Consolidating - Balance Sheets (Concluded)

### September 30, 2016

**Liabilities and Net Assets (Deficit)**

| | Porter Medical Center, Inc. | Porter Hospital, Inc. | Helen Porter Nursing Home, Inc. | Porter Real Estate Holdings, LLC | Eliminations | Consolidated |
|---|---|---|---|---|---|---|
| Current liabilities | | | | | | |
| Current portion of long-term debt | $ - | $ 786,177 | $ 149,206 | $ 28,202 | $ (3,457) | $ 960,128 |
| Accounts payable and accrued expenses | 166,278 | 2,381,618 | 148,589 | - | - | 2,696,485 |
| Resident deposits | - | - | 25,425 | - | - | 25,425 |
| Accrued payroll and related liabilities | 461,272 | 2,706,184 | 555,512 | - | - | 3,722,968 |
| Accrued compensated absences | 277,902 | 2,445,353 | 393,412 | - | - | 3,116,667 |
| Estimated third-party settlements | - | 1,098,085 | 63,080 | - | - | 1,161,165 |
| Due to affiliates | 210,964 | 626,219 | 213,263 | 2,065 | (1,052,511) | - |
| Total current liabilities | 1,116,416 | 10,043,636 | 1,548,487 | 30,267 | (1,055,968) | 11,682,838 |
| Liability for pension benefits | 336,943 | 6,165,058 | 1,068,324 | - | - | 7,570,325 |
| | | | | | | - |
| Deferred compensation | 914,442 | 778,056 | - | - | - | 1,692,498 |
| Residual receipts note to affiliate | - | - | 741,973 | - | (741,973) | - |
| Long-term debt, net of current portion | - | 12,003,682 | 2,826,871 | 108,240 | (16,406) | 14,922,387 |
| Total liabilities | 2,367,801 | 28,990,432 | 6,185,655 | 138,507 | (1,814,347) | 35,868,048 |
| Net assets (deficit) | | | | | | |
| Unrestricted | 2,549,087 | 24,442,649 | (3,214,316) | 959,377 | (1,017,592) | 23,719,205 |
| Temporarily restricted | - | 313,375 | 36,361 | - | - | 349,736 |
| Permanently restricted | - | 3,445,391 | - | - | - | 3,445,391 |
| Total net assets (deficit) | 2,549,087 | 28,201,415 | (3,177,955) | 959,377 | (1,017,592) | 27,514,332 |
| Total liabilities and net assets (deficit) | $ 4,916,888 | $ 57,191,847 | $ 3,007,700 | $ 1,097,884 | $ (2,831,939) | $ 63,382,380 |

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

### Consolidating - Statements of Operations

### Year Ended September 30, 2016

| | Porter Medical Center, Inc. | Porter Hospital, Inc. | Helen Porter Nursing Home, Inc. | Porter Real Estate Holdings, LLC | Eliminations | Consolidated |
|---|---|---|---|---|---|---|
| Unrestricted revenues, gains and other support | | | | | | |
| Patient service revenue (net of contractual allowances and discounts) | $ - | $ 77,198,235 | $ 9,576,975 | $ - | $ (102,943) | $ 86,672,267 |
| Less provision for bad debts | - | 2,626,646 | 128,215 | - | - | 2,754,861 |
| Net patient service revenue | - | 74,571,589 | 9,448,760 | - | (102,943) | 83,917,406 |
| Property rental income, related party | - | - | - | 118,680 | (118,680) | - |
| Other operating revenue | 6,230,301 | 2,455,188 | 111,142 | 35,478 | (5,991,651) | 2,840,458 |
| Net assets released from restrictions used for operations | - | 1,395 | 1,777 | - | - | 3,172 |
| Total unrestricted revenues, gains and other support | 6,230,301 | 77,028,172 | 9,561,679 | 154,158 | (6,213,274) | 86,761,036 |
| Expenses | | | | | | |
| Professional care of patients | - | 41,525,396 | 6,167,740 | - | (102,943) | 47,590,193 |
| General services | - | 3,390,330 | 1,699,648 | - | (118,680) | 4,971,298 |
| Administrative and fiscal services | 5,967,550 | 23,186,608 | 3,563,774 | 26,021 | (5,990,301) | 26,753,652 |
| Health care improvement tax | - | 4,214,164 | 516,551 | - | - | 4,730,715 |
| Depreciation and amortization | - | 2,871,626 | 298,440 | 42,812 | - | 3,212,878 |
| Interest | - | 389,138 | 90,108 | 5,239 | (1,350) | 483,135 |
| Total expenses | 5,967,550 | 75,577,262 | 12,336,261 | 74,072 | (6,213,274) | 87,741,871 |
| Operating income (loss) | 262,751 | 1,450,910 | (2,774,582) | 80,086 | - | (980,835) |
| Nonoperating gains (losses) | | | | | | |
| Contributions | 327,195 | 235,438 | - | - | - | 562,633 |
| Investment return | 615 | 60,385 | - | - | - | 61,000 |
| Other program income (loss), net | - | 2,974,311 | (1,422) | - | - | 2,972,889 |
| Equity in earnings of Porter Real Estate Holdings, LLC | 80,086 | - | - | - | (80,086) | - |
| Nonoperating gains (losses), net | 407,896 | 3,270,134 | (1,422) | - | (80,086) | 3,596,522 |
| Excess (deficiency) of revenues, gains, other support and nonoperating gains (losses) over expenses | 670,647 | 4,721,044 | (2,776,004) | 80,086 | (80,086) | 2,615,687 |
| Net assets released from restrictions used for purchase of property and equipment | - | 130,941 | 49,001 | - | - | 179,942 |
| Change in net assets to recognize funded status of pension plan | (85,528) | (704,322) | (134,706) | - | - | (924,556) |
| Transfer (to) from affiliates | - | (2,250,000) | 2,250,000 | - | - | - |
| Increase (decrease) in unrestricted net assets | $ 585,119 | $ 1,897,663 | $ (611,709) | $ 80,086 | $ (80,086) | $ 1,871,073 |

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

### Consolidating - Balance Sheets

### September 30, 2015

| Assets | Porter Medical Center, Inc. | Porter Hospital, Inc. | Helen Porter Nursing Home, Inc. | Porter Real Estate Holdings, LLC | Eliminations | Consolidated |
|---|---|---|---|---|---|---|
| Current assets | | | | | | |
| Cash and cash equivalents | $ 523,953 | $ 11,950,916 | $ 600,516 | $ 13,109 | $ - | $ 13,088,494 |
| Assets limited as to use | - | - | 83,947 | - | - | 83,947 |
| Patient accounts receivable, net | - | 9,702,885 | 1,041,752 | - | - | 10,744,637 |
| Other receivables, net | 82,679 | 1,319,509 | 62,777 | - | - | 1,464,965 |
| Current portion of note receivable, related party | - | 3,497 | - | - | (3,497) | - |
| Supplies | - | 1,167,755 | 12,666 | - | - | 1,180,421 |
| Prepaid expenses and other | 25,734 | 1,106,119 | 110,083 | - | - | 1,241,936 |
| Resident deposits | - | - | 16,786 | - | - | 16,786 |
| Due from affiliates | 417,166 | 271,087 | 44,369 | 2,793 | (735,415) | - |
| Total current assets | 1,049,532 | 25,521,768 | 1,972,896 | 15,902 | (738,912) | 27,821,186 |
| Assets limited as to use, deferred compensation plan assets | 1,160,346 | 715,055 | - | - | - | 1,875,401 |
| Long-term investments | 45,944 | 4,941,998 | - | - | - | 4,987,942 |
| Property and equipment, net | - | 20,947,612 | 1,336,428 | 1,039,138 | (58,215) | 23,264,963 |
| Beneficial interest in perpetual trusts | - | 3,431,932 | - | - | - | 3,431,932 |
| Note receivable, related party - noncurrent | 741,973 | 20,307 | - | - | (762,280) | - |
| Investment in subsidiary | 879,291 | - | - | - | (879,291) | - |
| Total assets | $ 3,877,086 | $ 55,578,672 | $ 3,309,324 | $ 1,055,040 | $ (2,438,698) | $ 61,381,424 |

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

## Consolidating - Balance Sheets (Concluded)

## September 30, 2015

**Liabilities and Net Assets (Deficit)**

| | Porter Medical Center, Inc. | Porter Hospital, Inc. | Helen Porter Nursing Home, Inc. | Porter Real Estate Holdings, LLC | Eliminations | Consolidated |
|---|---|---|---|---|---|---|
| Current liabilities | | | | | | |
| Current portion of long-term debt | $ - | $ 763,319 | $ 146,455 | $ 27,256 | $ (3,227) | $ 933,803 |
| Accounts payable and accrued expenses | 29,986 | 2,858,001 | 146,871 | - | - | 3,034,858 |
| Resident deposits | - | - | 16,786 | - | - | 16,786 |
| Accrued payroll and related liabilities | 107,304 | 2,004,790 | 331,777 | - | - | 2,443,871 |
| Accrued compensated absences | 196,617 | 2,723,746 | 301,140 | - | - | 3,221,503 |
| Estimated third-party settlements | - | 1,558,015 | 67,166 | - | - | 1,625,181 |
| Due to affiliates | 150,044 | 382,191 | 192,063 | 11,117 | (735,415) | - |
| Total current liabilities | 483,951 | 10,290,062 | 1,202,258 | 38,373 | (738,642) | 11,276,002 |
| Liability for pension benefits | 268,821 | 5,295,827 | 909,675 | - | - | 6,474,323 |
| Deferred compensation | 1,160,346 | 714,382 | - | - | - | 1,874,728 |
| Residual receipts note to affiliate | - | - | 741,973 | - | (741,973) | - |
| Long-term debt, net of current portion | - | 12,781,987 | 2,974,078 | 137,376 | (20,577) | 15,872,864 |
| Total liabilities | 1,913,118 | 29,082,258 | 5,827,984 | 175,749 | (1,501,192) | 35,497,917 |
| Net assets (deficit) | | | | | | |
| Unrestricted | 1,963,968 | 22,544,986 | (2,602,607) | 879,291 | (937,506) | 21,848,132 |
| Temporarily restricted | - | 401,814 | 83,947 | - | - | 485,761 |
| Permanently restricted | - | 3,549,614 | - | - | - | 3,549,614 |
| Total net assets (deficit) | 1,963,968 | 26,496,414 | (2,518,660) | 879,291 | (937,506) | 25,883,507 |
| Total liabilities and net assets (deficit) | $ 3,877,086 | $ 55,578,672 | $ 3,309,324 | $ 1,055,040 | $ (2,438,698) | $ 61,381,424 |

## PORTER MEDICAL CENTER, INC. AND SUBSIDIARIES

### Consolidating - Statements of Operations

### Year Ended September 30, 2015

| | Porter Medical Center, Inc. | Porter Hospital, Inc. | Helen Porter Nursing Home, Inc. | Porter Real Estate Holdings, LLC | Eliminations | Consolidated |
|---|---|---|---|---|---|---|
| Unrestricted revenues, gains and other support | | | | | | |
| Patient service revenue (net of contractual allowances and discounts) | $ - | $ 73,905,376 | $ 10,032,151 | $ - | $ (175,676) | $ 83,761,851 |
| Less provision for bad debts | - | 3,256,616 | 54,280 | - | - | 3,310,896 |
| Net patient service revenue | - | 70,648,760 | 9,977,871 | - | (175,676) | 80,450,955 |
| Property rental income, related party | - | - | - | 118,680 | (118,680) | - |
| Other operating revenue | 3,363,824 | 3,517,840 | 32,388 | 34,429 | (3,119,607) | 3,828,874 |
| Net assets released from restrictions used for operations | - | 2,040 | 10,671 | - | - | 12,711 |
| Total unrestricted revenues, gains and other support | 3,363,824 | 74,168,640 | 10,020,930 | 153,109 | (3,413,963) | 84,292,540 |
| Expenses | | | | | | |
| Professional care of patients | - | 40,977,211 | 5,766,442 | - | (175,676) | 46,567,977 |
| General services | - | 3,673,307 | 1,769,016 | - | (118,680) | 5,323,643 |
| Administrative and fiscal services | 3,148,763 | 22,823,156 | 2,789,160 | 11,086 | (3,118,159) | 25,654,006 |
| Health care improvement tax | - | 4,046,887 | 516,551 | - | - | 4,563,438 |
| Depreciation and amortization | - | 3,055,269 | 289,236 | 42,812 | - | 3,387,317 |
| Interest | - | 322,120 | 78,126 | 7,789 | (1,448) | 406,587 |
| Total expenses | 3,148,763 | 74,897,950 | 11,208,531 | 61,687 | (3,413,963) | 85,902,968 |
| Operating income (loss) | 215,061 | (729,310) | (1,187,601) | 91,422 | - | (1,610,428) |
| Nonoperating gains (losses) | | | | | | |
| Contributions | 274,333 | 185,276 | - | - | - | 459,609 |
| Investment return | 147 | 154,997 | - | - | - | 155,144 |
| Other program income, net | - | 3,269,712 | 95,218 | - | - | 3,364,930 |
| Loss on debt refinancing | - | (119,617) | (70,259) | - | - | (189,876) |
| Equity in earnings of Porter Real Estate Holdings, LLC | 91,422 | - | - | - | (91,422) | - |
| Total nonoperating gains | 365,902 | 3,490,368 | 24,959 | - | (91,422) | 3,789,807 |
| Excess (deficiency) of revenues, gains, other support and nonoperating gains (losses) over expenses | 580,963 | 2,761,058 | (1,162,642) | 91,422 | (91,422) | 2,179,379 |
| Net assets released from restrictions used for purchase of property and equipment | - | 60,728 | 67,605 | - | - | 128,333 |
| Change in net assets to recognize funded status of pension plan | (68,473) | (1,240,510) | (218,117) | - | - | (1,527,100) |
| Transfer (to) from affiliates | (420,000) | (1,040,185) | 1,460,185 | - | - | - |
| Increase in unrestricted net assets | $ 92,490 | $ 541,091 | $ 147,031 | $ 91,422 | $ (91,422) | $ 780,612 |