



SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

CONSOLIDATED FINANCIAL STATEMENTS

with

SUPPLEMENTARY INFORMATION

September 30, 2017 and 2016

With Independent Auditor's Report

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

September 30, 2017 and 2016

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Southern Vermont Health Services Corporation

We have audited the accompanying consolidated financial statements of Southern Vermont Health Services Corporation (a Vermont not-for-profit corporation) and Subsidiary, which comprise the consolidated 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 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 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 Southern Vermont Health Services Corporation and Subsidiary as of September 30, 2017 and 2016, 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

Report on Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information is presented for purposes of additional analysis rather than to present the financial position, results of operations and changes in net assets of the individual entities, and is not a required part of the consolidated 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 23, 2018
Registration No. 92-0000278

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidated Balance Sheets

September 30, 2017 and 2016

ASSETS

	<u>2017</u>	<u>2016</u>
Current assets		
Cash and cash equivalents	\$ 4,371,746	\$ 5,283,152
Patient and other accounts receivable, net	10,247,913	6,450,306
Pledges and bequests receivable, net	126,914	249,862
Supplies inventory	2,438,411	2,501,303
Other current assets	<u>279,375</u>	<u>402,919</u>
Total current assets	<u>17,464,359</u>	<u>14,887,542</u>
Assets limited as to use		
Internally designated	52,848,411	52,748,689
Under bond agreement for capital acquisition	2,014,807	2,007,690
Other temporarily restricted investments - BMH	96,224	88,361
Other temporarily restricted investments - SVHSC	829,935	777,258
Other permanently restricted investments - SVHSC	<u>279,042</u>	<u>279,042</u>
Total assets limited as to use	<u>56,068,419</u>	<u>55,901,040</u>
Pledges receivable, less current portion	8,189	142,131
Deferred system development costs, net	2,775,051	2,498,247
Property and equipment, net	27,731,677	27,132,776
Interest rate swap	120,472	-
Other noncurrent assets, net	<u>731,692</u>	<u>639,353</u>
Total assets	<u>\$104,899,859</u>	<u>\$101,201,089</u>

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

LIABILITIES AND NET ASSETS

	<u>2017</u>	<u>2016</u>
Current liabilities		
Current portion of long-term debt	\$ 1,258,699	\$ 1,244,764
Accounts payable	5,283,940	2,353,399
Salaries, wages and payroll taxes payable	1,554,135	1,565,538
Accrued retirement plan contribution	1,186,918	1,082,946
Accrued compensated absences	2,726,667	2,448,405
Other accrued expenses	2,338,017	2,262,524
Deferred revenue	41,971	-
Estimated third-party payor settlements	<u>2,861,139</u>	<u>4,742,463</u>
Total current liabilities	17,251,486	15,700,039
Long-term debt, less current portion	8,949,675	10,196,739
Other long-term liabilities	250,473	172,150
Interest rate swap	<u>-</u>	<u>153,262</u>
Total liabilities	<u>26,451,634</u>	<u>26,222,190</u>
Net assets		
Unrestricted	76,993,225	73,368,803
Temporarily restricted	1,175,958	1,331,054
Permanently restricted	<u>279,042</u>	<u>279,042</u>
Total net assets	<u>78,448,225</u>	<u>74,978,899</u>
Total liabilities and net assets	<u>\$104,899,859</u>	<u>\$101,201,089</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidated Statements of Operations

Years Ended September 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Unrestricted revenues, gains, and other support		
Patient service revenue (net of contractual allowances and discounts)	\$ 78,977,578	\$ 76,939,818
Less provision for bad debts	<u>3,915,046</u>	<u>3,778,102</u>
Net patient service revenue	75,062,532	73,161,716
Meaningful use revenue	212,535	523,785
Other revenue	3,498,193	2,065,658
Contributions	635,503	135,909
Fundraising, net of expenses of \$22,305 and \$14,057 in 2017 and 2016, respectively	13,514	22,928
Net assets released from restrictions for operations	<u>46,057</u>	<u>24,776</u>
Total unrestricted revenues, gains, and other support	<u>79,468,334</u>	<u>75,934,772</u>
Expenses		
Salaries, wages, and benefits	45,195,321	42,761,857
Supplies and other	17,239,574	15,236,337
Contracted services	9,717,566	8,968,765
Depreciation and amortization	4,539,320	4,815,500
Health care improvement tax	4,420,086	4,568,419
Interest expense	<u>178,685</u>	<u>201,223</u>
Total expenses	<u>81,290,552</u>	<u>76,552,101</u>
Operating loss	<u>(1,822,218)</u>	<u>(617,329)</u>
Nonoperating gains (losses)		
Income from investments	1,637,718	625,837
Other nonoperating income	99,527	92,859
Unrealized gain (loss) on interest rate swap	273,734	(81,750)
Change in net unrealized gains on investments	3,128,223	2,839,611
Unrestricted gifts and donations	-	384,000
Loss on refinancing of long-term debt	<u>-</u>	<u>(90,285)</u>
Nonoperating gains, net	<u>5,139,202</u>	<u>3,770,272</u>
Excess of revenues, gains, and other support over expenses and nonoperating gains (losses)	3,316,984	3,152,943
Net assets released from restrictions for capital acquisitions	<u>307,438</u>	<u>451,906</u>
Increase in unrestricted net assets	<u>\$ 3,624,422</u>	<u>\$ 3,604,849</u>

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

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidated Statements of Changes in Net Assets

Years Ended September 30, 2017 and 2016

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Balances, October 1, 2015	\$ <u>69,763,954</u>	\$ <u>1,522,504</u>	\$ <u>278,171</u>	\$ <u>71,564,629</u>
Excess of revenues, gains, and other support over expenses and nonoperating gains (losses)	3,152,943	-	-	3,152,943
Change in net unrealized gains on investments	-	70,133	351	70,484
Investment income	-	19,740	495	20,235
Contributions	-	182,364	25	182,389
Provision for uncollectible pledges and change in discounted present value	-	12,995	-	12,995
Net assets released from restrictions for operations	-	(24,776)	-	(24,776)
Net assets released from restrictions for capital acquisitions	<u>451,906</u>	<u>(451,906)</u>	<u>-</u>	<u>-</u>
Change in net assets	<u>3,604,849</u>	<u>(191,450)</u>	<u>871</u>	<u>3,414,270</u>
Balances, September 30, 2016	<u>73,368,803</u>	<u>1,331,054</u>	<u>279,042</u>	<u>74,978,899</u>
Excess of revenues, gains, and other support over expenses and nonoperating gains (losses)	3,316,984	-	-	3,316,984
Change in net unrealized gains on investments	-	74,373	-	74,373
Investment income	-	55,124	-	55,124
Contributions	-	80,912	-	80,912
Provision for uncollectible pledges and change in discounted present value	-	(12,010)	-	(12,010)
Net assets released from restrictions for operations	-	(46,057)	-	(46,057)
Net assets released from restrictions for capital acquisitions	<u>307,438</u>	<u>(307,438)</u>	<u>-</u>	<u>-</u>
Change in net assets	<u>3,624,422</u>	<u>(155,096)</u>	<u>-</u>	<u>3,469,326</u>
Balances, September 30, 2017	<u>\$ 76,993,225</u>	<u>\$ 1,175,958</u>	<u>\$ 279,042</u>	<u>\$ 78,448,225</u>

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

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidated Statements of Cash Flows

Years Ended September 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities		
Change in net assets	\$ 3,469,326	\$ 3,414,270
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation and amortization	4,539,320	4,815,500
Amortization of debt issuance costs, included in interest expense	15,852	9,826
Gain on sale of equipment	(2,500)	(250)
Net unrealized gain on investments	(3,202,596)	(2,910,095)
Net realized (gain) loss on investments	(1,000,677)	7,256
Unrealized (gain) loss on interest rate swap	(273,734)	153,262
Realized gain on termination of interest rate swap	-	(71,512)
Contributions and investment income restricted for long-term purposes	(70,377)	(93,599)
Provision for uncollectible pledges and change in discounted present value	(34,085)	(44,339)
Provision for bad debts	3,915,046	3,778,102
Increase in value of life insurance contract	(14,016)	(13,608)
Loss on refinancing of long-term debt	-	90,285
Decrease (increase) in		
Pledges and bequests receivable, net	290,975	1,316,057
Receivables, net	(7,712,653)	(4,572,068)
Inventories and other current assets	186,436	(493,942)
Increase (decrease) in		
Accounts payable and accrued expenses	3,197,400	(34,295)
Other current liabilities	179,465	(619,625)
Deferred revenues	41,971	-
Estimated third-party payor settlements	<u>(1,881,324)</u>	<u>3,758,250</u>
Net cash provided by operating activities	<u>1,643,829</u>	<u>8,489,475</u>
Cash flows from investing activities		
Purchase of property and equipment	(5,135,721)	(1,674,177)
Additions to deferred system development costs	(276,804)	(2,498,247)
Proceeds from sale of investments	17,570,947	14,394,366
Purchase of investments	<u>(13,535,053)</u>	<u>(19,435,924)</u>
Net cash used by investing activities	<u>(1,376,631)</u>	<u>(9,213,982)</u>
Cash flows from financing activities		
Additions to deferred financing costs, net	-	(78,800)
Proceeds from contributions and investment income restricted for long-term purposes	70,377	93,599
Repayment of interest rate swap liability upon termination	-	(585,250)
Proceeds from issuance of long-term debt	-	12,930,886
Repayments of long-term debt	<u>(1,248,981)</u>	<u>(9,950,867)</u>
Net cash (used) provided by financing activities	<u>(1,178,604)</u>	<u>2,409,568</u>
Net (decrease) increase in cash and cash equivalents	(911,406)	1,685,061
Cash and cash equivalents, beginning of year	<u>5,283,152</u>	<u>3,598,091</u>
Cash and cash equivalents, end of year	\$ <u>4,371,746</u>	\$ <u>5,283,152</u>
Supplemental disclosures of cash flow information		
Cash payment for interest	\$ <u>227,267</u>	\$ <u>212,127</u>

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

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Nature of Business

Southern Vermont Health Services Corporation and Subsidiary (SVHSC) is a Vermont not-for-profit organization that provides fundraising and management services for its not-for-profit subsidiary. SVHSC is the sole corporate member of Brattleboro Memorial Hospital, Inc. (Hospital or BMH), a Vermont not-for-profit organization. The Hospital is a provider of health services with facilities in Brattleboro, Vermont.

1. Summary of Significant Accounting Policies

Basis of Presentation

SVHSC's financial statements are presented in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification Topic (ASC) 958, *Not-For-Profit Entities*. Under FASB ASC 958, all not-for-profit organizations are required to provide a balance sheet, a statement of activities, and a statement of cash flows. The ASC and related guidance for healthcare entities require reporting amounts for SVHSC'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.

FASB ASC 958 also requires net assets and its revenues, expenses, gains, and losses be classified based on the existence or absence of donor-imposed restrictions. It requires that the amounts for each of the three classes of net assets - permanently restricted, temporarily restricted, and unrestricted - be displayed in a balance sheet and that the amounts of change in each of those classes of net assets be displayed in a statement of changes in net assets.

Principles of Consolidation

The consolidated financial statements represent the activities of the Hospital and SVHSC after eliminating all material intercompany balances and transactions.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (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 certain investments in highly liquid debt instruments with original maturities of three months or less.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Patient Accounts Receivable

Patient accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to operations and a credit to a valuation allowance based on its assessment of individual accounts and historical adjustments. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to patient accounts receivable.

In evaluating the collectibility of accounts receivable, SVHSC 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, SVHSC analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary. 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), SVHSC 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.

During 2017, SVHSC decreased its estimate from \$5,719,983 to \$5,414,985 in the allowance for doubtful accounts relating to self-pay patients and during 2016 SVHSC increased its estimate from \$5,266,350 to \$5,719,983 in the allowance for doubtful accounts relating to self-pay patients. During 2017, self-pay write-offs increased from \$3,567,049 to \$4,407,730 and during 2016 self-pay write-offs decreased from \$4,069,764 to \$3,567,049. The changes resulted from trends experienced in the collection of amounts from self-pay patients and quality of the aging of self-pay receivables based on fluctuations in amounts written-off each year.

Supplies Inventory

Supplies inventory is carried at the lower of cost (determined by the first-in, first-out method) or market.

Investments and Investment Income

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheets. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in the excess of revenues, gains, and other support over expenses and nonoperating gains (losses), unless the income or loss is restricted by donor or law.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

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 sheet.

SVHSC has elected the fair value option in FASB ASC 825, *Financial Instruments*, relative to its investments to simplify the presentation of all investment activity for unrestricted investments within the nonoperating gains (losses) section of the statements of operations.

Assets Limited as to Use

Assets limited as to use primarily consist of assets held by trustees under indenture agreements and designated assets set aside by SVHSC's Board of Trustees (Board), over which the Board retains control and which it may at its discretion subsequently use for other purposes.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to SVHSC are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received and the conditions are met, subject to a present value discount and an allowance for uncollectible amounts. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements.

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. 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, and other support over expenses and nonoperating gains (losses), 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-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Interest Rate Swap

The Hospital uses an interest rate swap contract to mitigate the cash flow exposure of interest rate movements on variable-rate debt. The Hospital has adopted FASB ASC 815, *Derivatives and Hedging*, to account for its interest rate swap contract. The interest rate swap has not been designated as a cash flow hedge and thus changes in fair value are included within nonoperating gains (losses).

Temporarily and Permanently Restricted Net Assets

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

Net Patient Service Revenue

SVHSC has agreements with third-party payors that provide for payments to SVHSC at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Changes in these estimates resulted in an increase in net patient service revenue of approximately \$867,000 in 2017 and a decrease in net patient service revenue of approximately \$1,476,000 in 2016.

Charity Care

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

Employee Fringe Benefits

SVHSC has an "earned time" plan which provides benefits to employees for paid leave hours. Under this plan, each employee earns paid leave for each period worked. These hours of paid leave may be used for vacations, holidays, or illnesses. Hours earned, but not used, are vested with the employee. SVHSC accrues a liability for such paid leave as it is earned. The earned time plan does not cover any contracted employees.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

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

The consolidated statements of operations include excess of revenues, gains, and other support over expenses and nonoperating gains (losses). Changes in unrestricted net assets which are excluded from this measure, consistent with industry practice, include 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

The Hospital and SVHSC 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.

Functional Expenses

SVHSC provides general healthcare services to residents within its geographic location. Expenses related to providing these services were as follows for the years ended:

	<u>2017</u>	<u>2016</u>
Healthcare services	\$ 67,516,895	\$ 61,929,610
General and administrative	<u>13,773,657</u>	<u>14,622,491</u>
	<u>\$ 81,290,552</u>	<u>\$ 76,552,101</u>

Newly Adopted Accounting Pronouncement and Reclassifications

The Hospital adopted the provisions of FASB Accounting Standards Update (ASU) 2015-03 - *Interest-Imputation of Interest, Simplifying the Presentation of Debt Issuance Costs* during 2017. The ASU is limited to simplifying the presentation of debt issuance costs, and the recognition and measurement guidance for debt issuance costs is not affected by the ASU. As a result of the adoption, the Hospital reclassified \$163,801 in unamortized bond issuance costs from other long-term assets in the accompanying September 30, 2016 balance sheet to be presented as a reduction of the long-term debt and reclassified \$9,826 in amortization to interest expense in the 2016 statement of operations, as required by the ASU. The adoption of ASU 2015-03 had no effect on the Hospital's statements of changes in net assets or cash flows for the year ended September 30, 2016.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Subsequent Events

For purposes of the preparation of these consolidated financial statements in conformity with GAAP, management has considered transactions or events occurring through January 23, 2018, the date the consolidated financial statements were available to be issued.

2. Community Benefit

SVHSC's charity care program is designed to assist those patients who are either uninsured, are underinsured or have limited financial resources that impact their ability to fully pay for their hospital care. Before completing an application for charity care, patients are first asked to investigate whether or not they may be eligible for Medicare, Medicaid, Veteran's Benefits or other governmental or public assistance programs.

SVHSC's qualifications for charity care are as follows:

- Charity care is limited to medically necessary services. Patients receiving certain elective services, such as those considered cosmetic, investigational or experimental, are expected to make payment arrangements in advance, as these types of services are not covered by the charity care program.
- The patient's family income must be at or below 300% of the current Federal Poverty Income Guidelines for their applicable family size.

SVHSC maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy, the estimated cost of those services and supplies and equivalent service statistics. The following information measures the level of the charity care provided during the years ended September 30:

	<u>2017</u>	<u>2016</u>
Charges foregone, based on established rates	\$ <u>1,188,000</u>	\$ <u>874,000</u>
Estimated costs and expenses incurred to provide charity care ¹	\$ <u>643,000</u>	\$ <u>449,000</u>
Equivalent percentage of charity care services to all services	<u>0.79%</u>	<u>0.59%</u>
Number of patients receiving charity care (unaudited)	<u>5,899</u>	<u>4,689</u>

¹The cost estimate is based on an overall cost to charge ratio applied to charges written off as charity care.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

In addition, SVHSC incurs a payment shortfall in the treatment of Medicaid patients. This government program reimburses for medical services at less than the costs incurred to provide those services. In 2017 and 2016, respectively, SVHSC incurred a shortfall of approximately \$9,219,000 and \$8,788,000, related to treating Medicaid patients.

SVHSC also provided other community benefits upon which no monetary value has been placed.

3. Patient and Other Accounts Receivable and Net Patient Service Revenue

Patient and Other Accounts Receivable

Patient and other accounts receivable is stated net of contractual allowances and allowance for doubtful accounts and is comprised of the following as of September 30:

	<u>2017</u>	<u>2016</u>
Patient accounts receivable	\$ 30,307,046	\$ 24,531,904
Other accounts receivable	743,932	527,288
Contractual allowance	(15,388,080)	(12,888,903)
Allowance for doubtful accounts	<u>(5,414,985)</u>	<u>(5,719,983)</u>
Patient accounts receivable, net	\$ <u>10,247,913</u>	\$ <u>6,450,306</u>

Net Patient Service Revenue

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

	<u>2017</u>	<u>2016</u>
Patient services		
Inpatient services	\$ 31,591,853	\$ 29,309,983
Outpatient services	<u>118,626,618</u>	<u>119,681,998</u>
	<u>150,218,471</u>	<u>148,991,981</u>
Less (plus):		
Medicare and Medicaid allowances	58,372,738	59,474,518
State disproportionate share	(866,228)	(918,389)
Other contractual allowances	12,546,408	12,621,738
Charity care allowances	<u>1,187,975</u>	<u>874,296</u>
	<u>71,240,893</u>	<u>72,052,163</u>
Patient service revenue (net of contractual allowances and discounts)	78,977,578	76,939,818
Less: Provision for bad debts	<u>3,915,046</u>	<u>3,778,102</u>
Net patient service revenue	\$ <u>75,062,532</u>	\$ <u>73,161,716</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

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SVHSC has agreements with the Centers for Medicare & Medicaid Services (CMS or Medicare) and the State of Vermont Department of Health and Human Services (DVHA or Medicaid) that provide for payments at amounts different from their established rates. Revenue from the Medicare and Medicaid programs accounted for approximately 51% and 50% of SVHSC's net patient service revenue for the years ended September 30, 2017 and 2016, respectively.

SVHSC 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, SVHSC 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 SVHSC's uninsured patients will be unable or unwilling to pay for the services rendered. Thus, SVHSC 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 year ended September 30, 2017 totaled \$78,977,578, of which \$74,014,703 was revenue from third-party payors and \$4,962,875 was revenue from self-pay patients, and during the year ended September 30, 2016 totaled \$76,939,818, of which \$71,588,598 was revenue from third-party payors and \$5,351,220 was revenue from self-pay patients.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs. During 2016, SVHSC identified and submitted a voluntary refund as a result of an error in the use of a particular billing code. The impact of this billing error, estimated at \$595,000, was reflected as an amount due to Medicare within the estimated third-party payor settlements amount in the financial statements at September 30, 2016, and was paid during 2017. Also during 2016, SVHSC identified and submitted a self-disclosure that certain claims were made in error to Medicare and other government payors between 2012 and 2014. The impact of these billing errors resulted in an overpayment to SVHSC estimated to be in the amount of \$1,700,000 and has been reflected within the estimated third-party payor settlements amount in the consolidated financial statements. The federal government has requested additional information which has been provided. SVHSC has assessed the risk and financial impact of any other errors it believes may exist, and has reflected their estimated impact in its estimated third-party payor settlements in the consolidated financial statements. Differences between amounts previously estimated and amounts subsequently determined to be recoverable or payable are included in net patient service revenues in the year that such amounts become known.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

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

Medicare

Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2014, with the exception of the year ended September 30, 2011 which remains open.

In 2012, SVHSC entered into an agreement with OneCare Vermont Accountable Care Organization, LLC (ACO), formed by University of Vermont Medical Center and Dartmouth-Hitchcock Medical Center. The ACO participates in the Medicare, Medicaid, and Community Exchange Shared Savings Programs.

Under each of the Shared Savings Programs, the payor (CMS, DVHA or Blue Cross Blue Shield Vermont) assesses an ACO's quality and financial performance based on a population of assigned beneficiaries to determine whether the ACO has met the quality performance standards and reduced growth in expenditures compared to a historical financial benchmark. ACOs that meet or exceed a minimum savings rate and satisfy minimum quality performance standards are eligible to receive a portion of the savings they generated (shared savings). This methodology provides an ACO with an incentive to improve the coordination and quality of care for all patients seen by its participating providers and suppliers. SVHSC received a payment of \$133,841 through the ACO from DVHA during fiscal year 2016 for meeting or exceeding the minimum savings rate and performance standards for the 2014 Performance Year.

SVHSC was a participant in the Medicare and Community Exchange (BCBSVT) Shared Savings Programs in 2017. SVHSC was not a participant in the DVHA Risk Contract in 2017. SVHSC received no shared savings payment from the ACO in 2017.

Effective January 1, 2018, SVHSC has entered into a new Risk Bearing Participant & Affiliate Agreement with the ACO. This agreement was developed to serve as the basis for the development of risk bearing agreements between the ACO and payors who would be inclined to participate in these types of agreements. The agreement included a Medicare Next Generation Model ACO Program Addendum that established the foundation for a capitated agreement.

Medicaid

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors and are not subject to retroactive adjustment.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Other Arrangements

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

4. Meaningful Use Revenue

The Medicare and Medicaid electronic health record (EHR) incentive programs provide a financial incentive for achieving "meaningful use" of certified EHR technology. The Medicare criteria for meaningful use will be staged in three steps with stage three beginning in fiscal year 2018. The Medicaid program will provide incentive payments to hospitals and eligible professionals as they adopt, implement, and upgrade or demonstrate meaningful use in the first year of participation and demonstrate meaningful use for up to five remaining participation years. SVHSC has recorded meaningful use revenue of approximately \$213,000 and \$524,000 in 2017 and 2016, respectively.

The Medicare EHR 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. There are no payment adjustments under the Medicaid EHR incentive program.

5. Supplies Inventory

The major classes of supplies inventory consisted of the following as of September 30:

	<u>2017</u>	<u>2016</u>
Central storeroom	\$ 220,569	\$ 168,939
Operating room	1,518,053	1,730,720
Pharmacy	520,988	379,305
Other	<u>178,801</u>	<u>222,339</u>
	<u>\$ 2,438,411</u>	<u>\$ 2,501,303</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

6. Investments

Investments consisted of the following as of September 30:

	<u>2017</u>	<u>2016</u>
Pooled investments		
Cash and cash equivalents	\$ 4,901,149	\$ 2,027,228
Marketable equity securities	22,075,350	19,549,802
Mutual funds	10,275,417	8,977,324
Corporate bonds	1,224,887	1,242,049
U.S. Treasury securities and other government securities	<u>15,480,585</u>	<u>22,008,586</u>
	<u>\$ 53,957,388</u>	<u>\$ 53,804,989</u>
Internally designated	\$ 52,848,411	\$ 52,748,689
Temporarily restricted investments - SVHSC	829,935	777,258
Permanently restricted investments - SVHSC	<u>279,042</u>	<u>279,042</u>
	<u>\$ 53,957,388</u>	<u>\$ 53,804,989</u>
Assets limited as to use under bond agreement for capital acquisition		
Cash and cash equivalents	<u>\$ 2,014,807</u>	<u>\$ 2,007,690</u>
Other temporarily restricted assets - BMH		
Cash and cash equivalents	\$ 58,571	\$ 49,647
U.S. Treasury securities and other government securities	<u>37,653</u>	<u>38,714</u>
	<u>\$ 96,224</u>	<u>\$ 88,361</u>

Investment income and (losses) gains on assets limited as to use and other temporarily restricted investments are comprised of the following:

	<u>2017</u>	<u>2016</u>
Income		
Interest and dividend income		
Assets limited as to use	\$ 637,041	\$ 633,093
Restricted investments	<u>55,124</u>	<u>20,235</u>
Total	692,165	653,328
Net realized gain (loss) on investments		
Assets limited as to use internally designated	<u>1,000,677</u>	<u>(7,256)</u>
Total investment income	<u>\$ 1,692,842</u>	<u>\$ 646,072</u>
Change in net unrealized gains on investments		
Assets limited as to use internally designated	\$ 3,128,223	\$ 2,839,611
Restricted investments	<u>74,373</u>	<u>70,484</u>
Total	<u>\$ 3,202,596</u>	<u>\$ 2,910,095</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

7. Property and Equipment

As of September 30, the cost and accumulated depreciation of depreciable assets by major classes of assets were as follows:

	<u>2017</u>	<u>2016</u>
Land	\$ 84,099	\$ 84,099
Land improvements	2,335,937	2,039,357
Building and improvements	45,782,822	44,886,868
Major moveable equipment	23,883,084	23,015,465
Construction-in-progress	<u>573,473</u>	<u>509,023</u>
	72,659,415	70,534,812
Less accumulated depreciation	<u>44,927,738</u>	<u>43,402,036</u>
	<u>\$ 27,731,677</u>	<u>\$ 27,132,776</u>

Depreciation expense for the years ended September 30, 2017 and 2016 was \$4,368,548 and \$-, respectively.

8. Long-Term Debt

On February 1, 2008, the Hospital entered into a loan agreement with Vermont Educational and Health Buildings Finance Agency (VEHBFA) issuing \$11,180,000 in bonds (Brattleboro Memorial Hospital Project Series 2008 A). The proceeds were used to advance refund previously issued bonds. Interest on the Bonds was based on available daily rates as determined by the remarketing agent based on prevailing market conditions, not to exceed 10% per annum. The Hospital could, at any time, exercise an option to convert to an irrevocably fixed rate. No conversion would be effective unless all Bonds had been remarketed and sold. The Hospital could prepay certain of the bonds according to the terms of the loan and trust agreement. The bonds were collateralized by the assets of the Hospital. The Series 2008 A bonds were advance refunded during 2016.

On June 1, 2016, the Hospital entered into a loan agreement with VEHBFA issuing \$10,500,000 in direct placement bonds (Brattleboro Memorial Hospital Project Series 2016 A). The proceeds were used to advance refund the previously issued Series 2008 A bonds, terminate the associated swap agreement and finance the Hospital's capital expenditures. Interest on the Bonds is based on monthly rates as determined by the loan and trust agreement. The Hospital may prepay certain of the bonds according to the terms of the loan and trust agreement. The bonds are collateralized by the assets of the Hospital.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

There are various restrictive covenants, which include compliance with certain financial ratios and a detail of events constituting defaults. The Hospital is in compliance with these requirements at September 30, 2017.

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

	<u>2017</u>	<u>2016</u>
Series 2016 A bonds with variable rate interest (1.48731% at September 30, 2017), payable in monthly installments, including interest, of approximately \$89,796 through February 2027.	\$ 9,362,855	\$ 10,274,712
Unsecured note payable, due in quarterly installments of \$83,162 through September 2020, including interest calculated at 3.5%.	<u>993,468</u>	<u>1,330,592</u>
Total long-term debt before unamortized bond issuance costs	10,356,323	11,605,304
Less: unamortized bond issuance costs	<u>147,949</u>	<u>163,801</u>
Total long-term debt	10,208,374	11,441,503
Less current portion	<u>1,258,699</u>	<u>1,244,764</u>
Total long-term debt, excluding current portion	<u>\$ 8,949,675</u>	<u>\$ 10,196,739</u>

Maturities for long-term debt in subsequent fiscal years ending September 30 are as follows:

2018 (included in current liabilities)	\$ 1,258,699
2019	1,275,879
2020	1,291,504
2021	975,403
2022	991,900
Thereafter	<u>4,562,938</u>
	<u>\$ 10,356,323</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Interest Rate Swaps

In connection with the issuance of the Series 2008 A Bonds, the Hospital entered into an interest rate swap agreement for 15 years for \$6,996,000, or 60% of the original bond issue, for the first 15 years of the bond issue to hedge the interest rate risk associated with the Series 2008 A Bonds. The interest rate swap agreement required the Hospital to pay a bank, the swap counterparty, a fixed rate of 3.30% in exchange for the counterparty's payment to the Hospital of a variable rate based on 68% of the one-month LIBOR rate. This swap agreement was terminated on June 1, 2016 and a termination fee of \$585,250 was paid by the Hospital to the bank.

In connection with the issuance of the Series 2016 A Bonds, the Hospital entered into an interest rate swap agreement for 10 years for \$10,500,000, or 100% of the original bond issue, to hedge the interest rate risk associated with the Series 2016 A Bonds. The notional amount of the swap will amortize such that it is equal to 100% of the outstanding bond balance. The interest rate swap agreement requires the Hospital to pay a bank, the swap counterparty, a fixed rate of 1.0375% in exchange for the counterparty's payment to the Hospital of a variable rate based on 68% of the one-month USD-LIBOR-BBA rate.

The Hospital is required to include the fair value of swaps in the balance sheet, and annual changes, if any, in the fair value of the swaps in the statements of operations. For example, during the term of the swap, the annually calculated value of the swap will be reported as an asset if interest rate expectations increase above those expected on the date the swap was entered into (as an unrealized gain in the statements of operations), which will generally be indicative that the net fixed rate the Hospital is paying is below market expectations of rates during the remaining term of the swap. The swap will be reported as a liability (as an unrealized loss in the statements of operations) if interest rate expectations decrease below those expected on the date the swap was entered into, which will generally be indicative that the net fixed rate the Hospital is paying on the swap is above market expectations of rates during the remaining term of the swap. These annual accounting adjustments of value changes in the swap transaction are non-cash recognition requirements, the net effect of which will be zero at the end of the swap's term. The Hospital retains the sole right to terminate the swap agreement should the need arise. The Hospital recorded the swap at its asset position of \$120,472 and liability position of \$153,262 at September 30, 2017 and 2016, respectively.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

9. Temporarily and Permanently Restricted Net Assets

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

	<u>2017</u>	<u>2016</u>
Auxiliary programs	\$ 57,186	\$ 48,164
Time restriction - Life Income Trust	192,727	186,399
Charity care	63,827	54,730
Other programs	642,891	599,362
Capital acquisition	<u>219,327</u>	<u>442,399</u>
	<u>\$ 1,175,958</u>	<u>\$ 1,331,054</u>

Permanently restricted net assets were made up of the following at September 30:

	<u>2017</u>	<u>2016</u>
Income restricted for:		
Medical library	\$ 1,202	\$ 1,202
Capital	20,000	20,000
Income unrestricted	<u>257,840</u>	<u>257,840</u>
	<u>\$ 279,042</u>	<u>\$ 279,042</u>

10. Concentration of Credit Risk

SVHSC grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at September 30, 2017 and 2016 was as follows:

	<u>2017</u>	<u>2016</u>
Medicare	40 %	35 %
Other third-party payors	15	16
Patient	13	19
Blue Cross	13	12
Medicaid	<u>19</u>	<u>18</u>
	<u>100 %</u>	<u>100 %</u>

SVHSC maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. SVHSC has not experienced any losses in such accounts. SVHSC believes it is not exposed to any significant risk on cash and cash equivalents.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

11. Health Care Improvement Tax

Effective July 1, 1991, a healthcare improvement tax was imposed on hospitals, 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 healthcare improvement trust fund and federal matching funds. Hospitals in Vermont are assessed a certain percentage of net patient service revenue which is determined annually by the General Assembly. The following tax was paid and disproportionate share funds received for the years ended September 30:

	<u>2017</u>	<u>2016</u>
Disproportionate share	\$ 866,228	\$ 918,389
Medicaid assessment expensed	<u>4,420,086</u>	<u>4,568,419</u>
	<u>\$ (3,553,858)</u>	<u>\$ (3,650,030)</u>

12. Commitments and Contingencies

Self-Funded Insurance Plans - SVHSC is self-insured with respect to healthcare coverage. This coverage is used to provide medical health benefits to its eligible employees and their eligible dependents. An accrual for management's estimate of healthcare claims incurred, but not reported, has been recorded as a liability and is included in other accrued expenses in the balance sheets.

Professional Liability Insurance - SVHSC is insured against malpractice loss contingencies under a claims-made insurance policy. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrence during its term, but reported subsequently, will be uninsured. SVHSC has also created a tail coverage reserve in the event that insurance providers are changed. This reserve was \$1,015,977 and \$1,097,631 as of September 30, 2017 and 2016, respectively. SVHSC is subject to complaints, claims and litigation due to potential claims which arise in the normal course of business. FASB ASC 954-450, *Health Care Entities - Contingencies*, provides clarification to companies in the healthcare industry on the accounting for professional liability and similar insurance. ASC 954-450 states that insurance liabilities should not be presented net of insurance recoveries and that an insurance receivable should be recognized on the same basis as the liabilities, subject to the need for a valuation allowance for uncollectible accounts. SVHSC has evaluated its exposure to losses arising from potential claims and has properly accounted for them in the consolidated balance sheets for the years ended September 30, 2017 and 2016. SVHSC intends to renew coverage on a claims-made basis and anticipates that such coverage will be available.

Litigation - In the normal course of business, SVHSC may be involved in litigation and annual third-party audits. Management, as part of its ongoing risk management, consults with its legal counsel to assess the impact of these matters on SVHSC.

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

Emergency Department Physician Staffing - SVHSC has an agreement with Dartmouth-Hitchcock Clinic to provide twenty-four hour per day physician staffing for its emergency department. Contract rates are reviewed annually and adjusted, if required, by the mutual consent of both parties. The agreement can be terminated at any time by mutual consent of both parties or by either party with 60-day prior written notification. The agreement renews on an annual basis.

Certificate of Need Approval - In December 2016, SVHSC filed a certificate of need application with the State of Vermont to build a new four story medical office building, renovate the existing operating room suite and perioperative area, and replace the hospital's three boilers. The total anticipated cost of the project is approximately \$23 million. In October 2017, the State of Vermont approved the certificate of need application. SVHSC expects to fund the project using internally designated investments and new tax-exempt borrowings.

Deferred System Development Costs - During 2016, SVHSC entered into an agreement with Cerner Corporation (Cerner) to implement a hospital-wide EHR system. The Cerner agreement has an initial term of seven years with successive 12-month terms. The costs incurred by SVHSC related to the implementation of the EHR system through June 1, 2017, the date the EHR system was placed in service, have been deferred and are being amortized over the remaining term of the Cerner agreement. Net deferred system development costs as of September 30, 2017 and 2016 were \$2,775,051 and \$2,498,247, respectively. Associated amortization expense was \$170,772 and \$0 in 2017 and 2016, respectively. The following is a schedule of future amortization of deferred system development costs as of September 30, 2017:

2018	\$ 512,317
2019	512,317
2020	512,317
2021	512,317
2022	512,317
2023	<u>213,466</u>
	<u>\$ 2,775,051</u>

The following schedule reflects SVHSC's future minimum payments under the Cerner agreement as of September 30, 2017:

2018	\$ 772,336
2019	772,336
2020	772,336
2021	772,336
2022	756,096
2023	<u>121,331</u>
	<u>\$ 3,966,771</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

13. Related Party Transactions

The Hospital contracts with SVHSC for management services. The Hospital recorded \$1,575,000 and \$1,603,000 in management service expenses and SVHSC recognized management service revenue of the same in 2017 and 2016, respectively. These transactions have been eliminated in the consolidation.

In accordance with FASB ASC 958, the Hospital has recognized an interest in the net assets of SVHSC for assets donated to SVHSC with the Hospital designated as beneficiary. This interest has been eliminated in the consolidation.

14. Retirement Plans

The Hospital has a defined contribution plan for active employees to which the Hospital contributes 5% of the annual salary of the participating employee. Plan expense for the years ended September 30, 2017 and 2016 was \$1,327,706 and \$1,182,482, respectively. SVHSC also participates in the Plan and recorded expense of \$53,417 and \$47,977 for the years ended September 30, 2017 and 2016, respectively.

SVHSC also has a defined contribution plan for active employees to which SVHSC contributes a matching contribution. In order to receive the match, employees must meet certain eligibility requirements. SVHSC matches 100% of elective deferrals to a limit based on years of service. Participants must be employed on the last day of the calendar year in order to receive the match. Plan expense for the years ended September 30, 2017 and 2016 was \$229,348 and \$173,727, respectively.

15. Pledges and Bequests Receivable

Pledges and bequests receivable is made up of the following:

	<u>2017</u>	<u>2016</u>
Pledges and bequests receivable	\$ 215,237	\$ 506,212
Less: Allowance for uncollectible pledges	(74,207)	(89,288)
Less: Allowance for present value discount	<u>(5,927)</u>	<u>(24,931)</u>
	135,103	391,993
Less: Current portion	<u>126,914</u>	<u>249,862</u>
Long-term pledges receivable	\$ <u>8,189</u>	\$ <u>142,131</u>

The following is the payment schedule at September 30, 2017:

Less than one year	\$ 200,378
Two to five years	14,859
Less allowance for uncollectible pledges and discount	<u>(80,134)</u>
	\$ <u>135,103</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Notes to Consolidated Financial Statements

September 30, 2017 and 2016

16. 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 and liabilities measured at fair value on a recurring basis are summarized below.

	<u>Fair Value Measurements at September 30, 2017</u>		
	<u>Total</u>	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Assets:			
Investments			
Cash and short-term investments	\$ 6,974,527	\$ 6,974,527	\$ -
Corporate bonds	1,224,887	-	1,224,887
U.S. Treasury securities and other government securities	15,518,238	15,518,238	-
Marketable equity securities	22,075,350	22,075,350	-
Mutual funds	10,275,417	10,275,417	-
Investments to fund deferred compensation (reported in current assets)	250,473	250,473	-
Interest rate swap	<u>120,472</u>	<u>-</u>	<u>120,472</u>
Total assets	<u>\$ 56,439,364</u>	<u>\$ 55,094,005</u>	<u>\$ 1,345,359</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

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September 30, 2017 and 2016

	<u>Fair Value Measurements at September 30, 2016</u>		
	<u>Total</u>	Quoted Prices In Active Markets of Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Assets:			
Investments			
Cash and short-term investments	\$ 4,084,565	\$ 4,084,565	\$ -
Corporate bonds	1,242,049	-	1,242,049
U.S. Treasury securities and other government securities	22,047,300	22,047,300	-
Marketable equity securities	19,549,802	19,549,802	-
Mutual funds	8,977,324	8,977,324	-
Investments to fund deferred compensation (reported in current assets)	<u>172,150</u>	<u>172,150</u>	<u>-</u>
Total assets	<u>\$ 56,073,190</u>	<u>\$ 54,831,141</u>	<u>\$ 1,242,049</u>
Liabilities:			
Interest rate swap	<u>\$ 153,262</u>	<u>\$ -</u>	<u>\$ 153,262</u>

The fair value of Level 2 assets and liabilities is primarily based on quoted market prices of comparable securities, interest rates, and credit risk. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

SUPPLEMENTARY INFORMATION

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidating Balance Sheet

September 30, 2017
(With Comparative Totals for 2016)

ASSETS

	2017				2016 Total
	SVHSC	BMH	Eliminations	Total	
Current assets					
Cash and cash equivalents	\$ 1,775,906	\$ 2,595,840	\$ -	\$ 4,371,746	\$ 5,283,152
Patient and other accounts receivable, net	-	10,247,913	-	10,247,913	6,450,306
Pledges and bequests receivable, net	126,914	-	-	126,914	249,862
Supplies inventory	-	2,438,411	-	2,438,411	2,501,303
Other current assets	677	278,698	-	279,375	402,919
Estimated third-party payor settlements	-	-	-	-	-
Due from affiliate	-	165,373	(165,373)	-	-
Total current assets	<u>1,903,497</u>	<u>15,726,235</u>	<u>(165,373)</u>	<u>17,464,359</u>	<u>14,887,542</u>
Assets limited as to use					
Internally designated	15,276,882	37,571,529	-	52,848,411	52,748,689
Under bond agreement for capital acquisition	-	2,014,807	-	2,014,807	2,007,690
Other temporarily restricted investments - BMH	-	96,224	-	96,224	88,361
Other temporarily restricted investments - SVHSC	829,935	-	-	829,935	777,258
Other permanently restricted investments - SVHSC	279,042	-	-	279,042	279,042
Interest in net assets of SVHSC	-	882,724	(882,724)	-	-
Total assets limited as to use	<u>16,385,859</u>	<u>40,565,284</u>	<u>(882,724)</u>	<u>56,068,419</u>	<u>55,901,040</u>
Pledges and bequests receivable, less current portion	8,189	-	-	8,189	142,131
Property and equipment, net	2,537,194	25,194,483	-	27,731,677	27,132,776
Deferred system development costs, net	-	2,775,051	-	2,775,051	2,498,247
Interest rate swap	-	120,472	-	120,472	-
Other noncurrent assets, net	<u>731,692</u>	<u>-</u>	<u>-</u>	<u>731,692</u>	<u>639,353</u>
Total assets	<u>\$ 21,566,431</u>	<u>\$ 84,381,525</u>	<u>\$ (1,048,097)</u>	<u>\$ 104,899,859</u>	<u>\$ 101,201,089</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidating Balance Sheet

September 30, 2017
(With Comparative Totals for 2016)

LIABILITIES AND NET ASSETS

	2017				2016
	SVHSC	BMH	Eliminations	Total	Total
Current liabilities					
Current portion of long-term debt	\$ -	\$ 1,258,699	\$ -	\$ 1,258,699	\$ 1,244,764
Accounts payable	48,893	5,235,047	-	5,283,940	2,353,399
Salaries, wages and payroll taxes payable	121,868	1,432,267	-	1,554,135	1,565,538
Accrued retirement plan contribution	46,779	1,140,139	-	1,186,918	1,082,946
Accrued compensated absences	100,445	2,626,222	-	2,726,667	2,448,405
Other accrued expenses	27,348	2,310,669	-	2,338,017	2,262,524
Deferred revenue	-	41,971	-	41,971	-
Estimated third-party payor settlements	-	2,861,139	-	2,861,139	4,742,463
Due to affiliate	165,373	-	(165,373)	-	-
Total current liabilities	510,706	16,906,153	(165,373)	17,251,486	15,700,039
Long-term debt, less current portion	-	8,949,675	-	8,949,675	10,196,739
Other long-term liabilities	250,473	-	-	250,473	172,150
Interest rate swap	-	-	-	-	153,262
Total liabilities	761,179	25,855,828	(165,373)	26,451,634	26,222,190
Net assets					
Unrestricted	19,446,476	57,546,749	-	76,993,225	73,368,803
Temporarily restricted	1,079,734	699,906	(603,682)	1,175,958	1,331,054
Permanently restricted	279,042	279,042	(279,042)	279,042	279,042
Total net assets	20,805,252	58,525,697	(882,724)	78,448,225	74,978,899
Total liabilities and net assets	\$ 21,566,431	\$ 84,381,525	\$ (1,048,097)	\$ 104,899,859	\$ 101,201,089

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidating Statement of Operations

Year Ended September 30, 2017
(With Comparative Totals for Year Ended 2016)

	2017				2016
	SVHSC	BMH	Eliminations	Total	Total
Unrestricted revenues, gains, and other support					
Patient service revenue (net of contractual allowances and discounts)	\$ -	\$ 78,977,578	\$ -	\$ 78,977,578	\$ 76,939,818
Less provision for bad debts	-	3,915,046	-	3,915,046	3,778,102
Net patient service revenue	-	75,062,532	-	75,062,532	73,161,716
Meaningful use revenue	-	212,535	-	212,535	523,785
Other revenue	369,179	3,590,636	(461,622)	3,498,193	2,065,658
Contributions	635,503	-	-	635,503	135,909
Management fee revenue	1,575,000	-	(1,575,000)	-	-
Fundraising, net of expenses	13,514	-	-	13,514	22,928
Net assets released from restrictions for operations	46,057	-	-	46,057	24,776
Total unrestricted revenues, gains, and other support	<u>2,639,253</u>	<u>78,865,703</u>	<u>(2,036,622)</u>	<u>79,468,334</u>	<u>75,934,772</u>
Expenses					
Salaries, wages, and benefits	1,347,169	43,848,152	-	45,195,321	42,761,857
Supplies and other	312,575	17,331,375	(404,376)	17,239,574	15,236,337
Contracted services	23,263	11,269,303	(1,575,000)	9,717,566	8,968,765
Depreciation and amortization	284,010	4,255,310	-	4,539,320	4,815,500
Health care improvement tax	-	4,420,086	-	4,420,086	4,568,419
Interest expense	-	178,685	-	178,685	201,223
Total expenses	<u>1,967,017</u>	<u>81,302,911</u>	<u>(1,979,376)</u>	<u>81,290,552</u>	<u>76,552,101</u>
Operating income (loss)	<u>672,236</u>	<u>(2,437,208)</u>	<u>(57,246)</u>	<u>(1,822,218)</u>	<u>(617,329)</u>
Nonoperating gains (losses)					
Income from investments	841,613	796,105	-	1,637,718	625,837
Other nonoperating income	14,016	85,511	-	99,527	92,859
Unrealized loss on interest rate swaps	-	273,734	-	273,734	(81,750)
Change in net unrealized gains (losses) on investments	1,367,969	1,760,254	-	3,128,223	2,839,611
Unrestricted gifts and donations	-	-	-	-	384,000
Loss on early extinguishment of long-term debt	-	-	-	-	(90,285)
Nonoperating gains, net	<u>2,223,598</u>	<u>2,915,604</u>	<u>-</u>	<u>5,139,202</u>	<u>3,770,272</u>
Excess of revenues, gains and other support over expenses and nonoperating gains (losses)	2,895,834	478,396	(57,246)	3,316,984	3,152,943
Net assets released from restrictions for capital acquisitions	307,438	-	-	307,438	451,906
Net assets transferred for capital acquisitions	(342,237)	284,991	57,246	-	-
Increase in unrestricted net assets	<u>\$ 2,861,035</u>	<u>\$ 763,387</u>	<u>\$ -</u>	<u>\$ 3,624,422</u>	<u>\$ 3,604,849</u>

SOUTHERN VERMONT HEALTH SERVICES CORPORATION AND SUBSIDIARY

Consolidating Statement of Changes in Net Assets

Year Ended September 30, 2017
(With Comparative Totals for Year Ended 2016)

	2017				2016
	SVHSC	BMH	Eliminations	Total	Total
Unrestricted net assets					
Excess of revenues, gains, and other support over expenses and nonoperating gains (losses)	\$ 2,895,834	\$ 478,396	\$ (57,246)	\$ 3,316,984	\$ 3,152,943
Net assets released from restrictions for capital acquisitions	307,438	-	-	307,438	451,906
Net assets transferred for capital acquisitions	(342,237)	284,991	57,246	-	-
Change in unrestricted net assets	<u>2,861,035</u>	<u>763,387</u>	<u>-</u>	<u>3,624,422</u>	<u>3,604,849</u>
Temporarily restricted net assets					
Change in net unrealized gains on investments	75,508	(1,135)	-	74,373	70,133
Investment income	46,127	8,997	-	55,124	19,740
Contributions	80,912	-	-	80,912	182,364
Provision for uncollectible pledges and change in discounted present value	(12,010)	-	-	(12,010)	12,995
Net assets released from restrictions for operations	(46,057)	-	-	(46,057)	(24,776)
Change in interest in SVHSC	-	37,470	(37,470)	-	-
Net assets released from restrictions for capital acquisitions	(307,438)	-	-	(307,438)	(451,906)
Change in temporarily restricted net assets	<u>(162,958)</u>	<u>45,332</u>	<u>(37,470)</u>	<u>(155,096)</u>	<u>(191,450)</u>
Permanently restricted net assets					
Change in net unrealized gains on investments	-	-	-	-	351
Investment income	-	-	-	-	495
Contributions	-	-	-	-	25
Change in permanently restricted net assets	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>871</u>
Change in net assets	2,698,077	808,719	(37,470)	3,469,326	3,414,270
Net assets, beginning of year	<u>18,107,175</u>	<u>57,716,978</u>	<u>(845,254)</u>	<u>74,978,899</u>	<u>71,564,629</u>
Net assets, end of year	<u>\$ 20,805,252</u>	<u>\$ 58,525,697</u>	<u>\$ (882,724)</u>	<u>\$ 78,448,225</u>	<u>\$ 74,978,899</u>