

**UNITED SURGEONS, LLC D/B/A
UNITY MEDICAL AND SURGICAL HOSPITAL**
Mishawaka, Indiana

CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

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INDEPENDENT AUDITOR'S REPORT

Board of Directors and Members of
United Surgeons, LLC
d/b/a Unity Medical and Surgical Hospital
Mishawaka, Indiana

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of United Surgeons, LLC d/b/a Unity Medical and Surgical Hospital, which comprise the consolidated balance sheets as of December 31, 2015 and 2014, and the related consolidated statements of operations, members' deficit, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

(Continued)

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of United Surgeons, LLC d/b/a Unity Medical and Surgical Hospital, as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter Regarding Going Concern

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 8 to the consolidated financial statements, the Company's current liabilities exceed its current assets along with a members' deficit position that raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 8. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Crowe Horwath LLP
Crowe Horwath LLP

Chicago, Illinois
September 23, 2016

UNITED SURGEONS, LLC D/B/A
 UNITY MEDICAL AND SURGICAL HOSPITAL
 CONSOLIDATED BALANCE SHEETS
 December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
ASSETS		
Current assets:		
Cash	\$ 318,481	\$ 912,477
Patient receivables, net	13,542,638	13,144,740
Inventory	693,489	608,264
Prepaid expenses and other assets	468,994	128,536
Affiliates receivables	<u>201,374</u>	<u>236,470</u>
Total current assets	15,224,976	15,030,487
Property and equipment, net	13,332,419	15,464,808
Goodwill, net	345,607	394,980
Intangibles, net	-	666,667
Deposits	<u>12,324</u>	<u>12,324</u>
	<u>13,690,350</u>	<u>16,538,779</u>
Total assets	<u>\$ 28,915,326</u>	<u>\$ 31,569,266</u>
LIABILITIES AND MEMBERS' DEFICIT		
Current liabilities:		
Line of credit agreements	\$ 4,000,000	\$ 4,000,000
Current portion of long-term debt	2,116,687	2,628,511
Current portion of capital lease obligations	128,328	783,024
Accounts payable	1,708,480	2,387,983
Accrued expenses	2,136,141	1,517,051
Affiliate payables	828,892	-
Third-party settlements	<u>7,515,656</u>	<u>8,079,490</u>
Total current liabilities	18,434,184	19,396,059
Long-term liabilities:		
Long-term debt, net of current portion	10,876,917	12,110,456
Capital lease obligations, net of current portion	<u>17,065,987</u>	<u>16,521,988</u>
Total long-term liabilities	<u>27,942,904</u>	<u>28,632,444</u>
Total liabilities	46,377,088	48,028,503
Due from Parent	(2,390,207)	(1,744,702)
Members' deficit	<u>(15,071,555)</u>	<u>(14,714,535)</u>
Total members' deficit	<u>(17,461,762)</u>	<u>(16,459,237)</u>
Total liabilities and members' deficit	<u>\$ 28,915,326</u>	<u>\$ 31,569,266</u>

See accompanying notes to consolidated financial statements.

UNITED SURGEONS, LLC D/B/A
 UNITY MEDICAL AND SURGICAL HOSPITAL
 CONSOLIDATED STATEMENTS OF OPERATIONS
 Years ended December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Revenue:		
Patient service revenue	\$ 40,715,971	\$ 27,681,299
Physician practice	4,176,745	3,276,126
Other	<u>1,284,574</u>	<u>284,861</u>
Total revenue	46,177,290	31,242,286
 Operating expenses:		
Contract services	16,049,253	14,719,179
Bad debt expense	4,961,241	1,251,125
Professional fees	723,837	860,493
Medical supplies	12,706,603	10,040,925
Office expense	421,602	359,606
Equipment rent	119,837	142,272
Building rent	448,555	434,601
Repairs and maintenance	389,562	342,777
Utilities	446,830	451,733
Insurance	503,997	447,723
Property taxes	198,000	408,000
Dues, licenses and subscriptions	155,016	119,133
Travel, meals and conferences	259,543	104,678
Depreciation and amortization expense	3,448,434	3,453,462
Collection fees	1,339,163	1,017,149
Human resource expense	42,172	44,680
Education and training	440,861	336,909
Miscellaneous expenses	<u>82,958</u>	<u>90,674</u>
Total operating expenses	<u>42,737,464</u>	<u>34,625,119</u>
 Income (loss) from operations	 3,439,826	 (3,382,833)
 Other income (expense):		
Interest expense	(3,771,462)	(3,923,834)
Rental income	8,600	14,700
Loss on disposal of assets	(610)	(25,642)
Other income (expense)	<u>2,399</u>	<u>(552)</u>
Total other expense	<u>(3,761,073)</u>	<u>(3,935,328)</u>
 Net loss	 <u>\$ (321,247)</u>	 <u>\$ (7,318,161)</u>

See accompanying notes to consolidated financial statements.

UNITED SURGEONS, LLC D/B/A
 UNITY MEDICAL AND SURGICAL HOSPITAL
 CONSOLIDATED STATEMENTS OF MEMBERS' DEFICIT
 Years ended December 31, 2015 and 2014

	<u>Due from Parent</u>	<u>Members' Deficit</u>	<u>Total</u>
Balances, January 1, 2014	\$ (990,565)	\$ (7,392,487)	\$ (8,383,052)
Net loss	-	(7,318,161)	(7,318,161)
Advances to Parent (Note 6)	(754,137)	-	(754,137)
Distributions	<u>-</u>	<u>(3,887)</u>	<u>(3,887)</u>
Balances, December 31, 2014	(1,744,702)	(14,714,535)	(16,459,237)
Net income	-	(321,247)	(321,247)
Advances to Parent (Note 6)	(645,505)	-	(645,505)
Distributions	<u>-</u>	<u>(35,773)</u>	<u>(35,773)</u>
Balances, December 31, 2015	<u>\$ (2,390,207)</u>	<u>\$ (15,071,555)</u>	<u>\$ (17,461,762)</u>

See accompanying notes to consolidated financial statements.

UNITED SURGEONS, LLC D/B/A
 UNITY MEDICAL AND SURGICAL HOSPITAL
 CONSOLIDATED STATEMENTS OF CASH FLOWS
 Years ended December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:		
Net loss	\$ (321,247)	\$ (7,318,161)
Adjustments to reconcile net loss to net cash from operating activities		
Depreciation and amortization expense	3,448,434	3,453,462
Bad debt expense	4,961,241	1,251,125
Loss on disposal of assets	610	25,642
Excess of interest over capital lease payments	445,929	485,458
Change in assets and liabilities		
Patient receivables	(5,359,139)	(2,665,117)
Third party settlements	(563,834)	5,746,011
Affiliate receivables and payables	400,112	(193,233)
Prepaid expenses and other assets	(340,458)	256,888
Inventory	(85,225)	(53,471)
Deposits	-	12,500
Accounts payable	(215,627)	2,134,216
Accrued expenses	<u>619,090</u>	<u>345,220</u>
Net cash from operating activities	2,989,886	3,480,540
Cash flows from investing activities:		
Proceeds from the sale of fixed assets	-	3,176
Purchase of property and equipment	<u>(133,765)</u>	<u>(393,140)</u>
Net cash from investing activities	(133,765)	(389,964)
Cash flows from financing activities:		
Line of credit agreements	-	1,000,000
Payments on long-term debt	(1,745,363)	(2,975,000)
Payments on capital lease obligations	(1,023,476)	(1,234,059)
Distributions	(35,773)	(207,810)
Due from Parent	<u>(645,505)</u>	<u>(754,137)</u>
Net cash from financing activities	<u>(3,450,117)</u>	<u>(4,171,006)</u>
Net change in cash	(593,996)	(1,080,430)
Cash at beginning of year	<u>912,477</u>	<u>1,992,907</u>
Cash at end of year	<u>\$ 318,481</u>	<u>\$ 912,477</u>
Supplemental disclosures of cash flow information		
Cash paid during the year for interest	\$ 3,379,236	\$ 3,600,453
Supplemental disclosures of non-cash flow activity		
Assets acquired under capital lease agreements	\$ 233,425	\$ -

See accompanying notes to consolidated financial statements.

UNITED SURGEONS, LLC D/B/A
UNITY MEDICAL AND SURGICAL HOSPITAL
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization: United Surgeons, LLC d/b/a Unity Medical and Surgical Hospital, LLC ("UMASH"), a subsidiary of Physician's ASC Management, LLC ("PAM" or "Parent"), operates a 29 bed outpatient / inpatient surgical hospital located in Mishawaka, Indiana.

Basis of Consolidation: The accompanying consolidated financial statements include the accounts of UMASH and their wholly owned subsidiaries (collectively "the Company"), and have been prepared in conformity with accounting principles generally accepted in the United States of America. All material intercompany accounts and transactions have been eliminated in consolidation.

Industry: The Company derives a significant portion of its revenue from third-party payer programs. The receipt of future revenues by the Company is subject to, among other factors, federal and state policies affecting the health care industry, economic conditions that may include an inability to control expenses in periods of inflation, increased competition, market pressures on premium rates and other conditions which are impossible to predict.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Estimates associated with the allowances for contractual adjustments and uncollectible patient accounts, third-party settlements, and medical malpractice are particularly susceptible to material change in the near term.

Total patient accounts receivable concentrations by payer at December 31 are as follows:

	<u>2015</u>	<u>2014</u>
Commercial, self pay and other	47 %	46 %
Blue Cross	35	28
Medicare	<u>18 %</u>	<u>26 %</u>
	<u>100 %</u>	<u>100 %</u>

The Company does not perform credit evaluations of its payers, but does inquire of patients regarding their access to insurance and ability to pay. The Company does not require collateral from its patients, third-party payers or others.

Cash: The Company maintains cash balances with financial institutions which, at times, may exceed federally insured limits.

Patient Receivables and Allowances: Patient receivables represent charges to patients, primarily on open account. The Company does not accrue interest on any of its patient receivables. Adjustments to patient accounts are made in amounts estimated to maintain an adequate allowance to cover contractual allowances and anticipated losses. Patient receivables represent estimated net realizable amounts from patients, third-party payers and others. Estimated third-party payor contractual adjustments, based on existing contractual relationships, are recorded at the time charges are posted and are adjusted to reflect actual contractual adjustments as claims are settled.

(Continued)

UNITED SURGEONS, LLC D/B/A
UNITY MEDICAL AND SURGICAL HOSPITAL
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Management periodically reviews patient receivables and records an allowance for uncollectible accounts based on current circumstances. Allowance estimates are based on historical experience and other relevant factors. Accounts are charged against the allowance when all attempts to collect the receivable have failed. Patient receivables are shown net of allowances for contractual and doubtful accounts of \$21,417,729 and \$16,200,246 on the consolidated balance sheets at December 31, 2015 and 2014, respectively.

Settlements: Settlements under cost reimbursement agreements with third-party payers are estimated and recorded in the period in which the related services are rendered and are adjusted in future periods as final settlements are determined. Final determination of amounts earned under the Medicare and Medicaid programs often occur in subsequent years because of audits by the programs, rights of appeal, and the application of numerous technical provisions.

Cost report settlements result from the adjustment of interim payments to final reimbursement under third-party payors that are subject to audit by fiscal intermediaries. Laws and regulations governing the Medicare program are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Final reimbursement under the Medicare program is subject to audit by fiscal intermediaries. Although these audits may result in some changes in these amounts, they are not expected to have a material effect on the accompanying consolidated financial statements. The effect of settlements and other cost report matters reports resulted in an increase in patient service revenue of approximately \$437,445 in 2015 and a decrease in patient service revenue of approximately \$5,636,804 in 2014, respectively. These changes in estimate are related primarily to Medicare outliers and estimate to actual settlements.

An estimated Medicare and Medicaid settlement payable of \$7,515,656 and \$8,079,490 was recorded at December 31, 2015 and 2014, respectively, in third-party settlements on the consolidated balance sheets.

On April 21, 2016 the Company repaid the 2012 Medicare cost report final reimbursement settlement in the amount of \$683,866 which was accrued by the Company in third-party settlements on the consolidated balance sheet as of December 31, 2015. At December 31, 2014, the Company's accrued estimate of the settlement amount was \$715,000.

On May 16, 2016, the Company was notified that the 2013 Medicare cost report reimbursement settlement was finalized in the amount of \$4,664,061 which was accrued by the Company in third-party settlements on the consolidated balance sheet as of December 31, 2015. At December 31, 2014, the Company's accrued estimate of the settlement amount was \$4,825,000. The Company is working with their fiscal intermediary to enter into an extended repayment plan on the 2013 Medicare cost settlement. Without an extended repayment plan, the Company's Medicare payments will be withheld along with interest charged on the unpaid and outstanding balance at a rate of 10%.

In anticipation of entering into an extended repayment plan with Medicare, the Company made payments in the amount of \$99,100 in May and June 2016.

In July 2016, Medicare began to recoup 100% of Medicare claims payments owed to the Company and applied those amounts against the outstanding cost report reimbursement settlement. Medicare will continue to do so until an extended payment plan is approved by Medicare. The Company anticipates entering into an extended repayment plan with Medicare in October 2016. See Note 8 related to Management's Plan.

(Continued)

UNITED SURGEONS, LLC D/B/A
UNITY MEDICAL AND SURGICAL HOSPITAL
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Inventory: Inventory consists primarily of medical and pharmaceutical supplies and is stated at the lower of cost (first-in, first-out) or market value.

Property and Equipment: Property and equipment are stated at cost. Depreciation of property and equipment is provided using the straight-line method over the estimated useful lives of the assets and includes depreciation on assets leased under capital lease arrangements. When properties are retired or otherwise disposed of, the appropriate accounts are relieved of cost and accumulated depreciation, and any resulting gain or loss is recognized.

Estimated lives used in computing depreciation are as follows:

Building	24 years
Software, computer and medical equipment	3 - 7 years
Furniture, fixtures and office equipment	3 - 7 years
Leasehold improvements	Lesser of life of lease or economic useful life

On an on-going basis, long-lived assets, such as property and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the carrying amount of an asset exceeds its estimated discounted future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. As of December 31, 2015 and 2014, no such impairment existed.

Goodwill: Goodwill represents the excess of the purchase price over the fair value of the net assets of businesses acquired in a business combination.

In January 2014, the Financial Accounting Standards Board (FASB) issued guidance that provides private companies with an alternative for the subsequent measurement of goodwill. Under this alternative, goodwill is amortized and is only tested for impairment when a triggering event occurs that indicates the fair value may be below the carrying amount. Entities that adopt the alternative are required to make a policy decision to test goodwill for impairment either at the entity level or at the reporting unit level. The alternative must be applied to all existing and future goodwill.

The Company adopted this goodwill accounting alternative and applied its provisions prospectively beginning January 1, 2013, and elected to test goodwill for impairment at the reporting unit level. The effects of adopting this standard resulted in recording goodwill amortization expense of \$49,373 for the years ended December 31, 2015 and 2014, and accumulated goodwill amortization of \$148,119 and \$98,746 as of December 31, 2015 and 2014, respectively. Future goodwill amortization expense is estimated to be \$49,373 each year from 2016 through 2022.

Goodwill impairment testing is performed at the reporting unit level only when a triggering event indicates that the carrying value of the reporting unit may exceed its estimated fair value. Management believes no goodwill was impaired at December 31, 2015 and 2014.

Intangible Assets: These assets are amortized on a straight-line basis over their period of expected benefits. The Company entered into a business acquisition and identified a non-compete agreement in the amount of \$2,000,000. The Company recorded amortization expense of \$666,666 in 2015 and 2014, and the non-compete is presented net of accumulated amortization of \$1,333,332 at December 31, 2014, on the consolidated balance sheets. The non-compete was fully amortized in 2015.

(Continued)

UNITED SURGEONS, LLC D/B/A
UNITY MEDICAL AND SURGICAL HOSPITAL
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition: Revenue is recorded when medical services are rendered. Management fee and contracted service revenues are recorded as services are rendered. Provisions for estimated third-party payer settlements and adjustments are made in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Other Revenue: The American Recovery and Reinvestment Act of 2009 included provisions for implementing health information technology under the Health Information Technology for Economic and Clinical Health Act (HITECH). These provisions were designed to increase the use of electronic health records (EHR) technology and establish the requirements for a Medicare and Medicaid incentive payments program beginning in 2011 for eligible hospitals and providers that adopt and meaningfully use certified EHR technology. Eligibility for annual Medicare incentive payments is dependent on providers demonstrating meaningful use of EHR technology in each period over a four-year period. Initial Medicaid incentive payments are available to providers that adopt, implement, or upgrade certified EHR technology; but providers must demonstrate meaningful use of such technology in subsequent years to qualify for additional incentive payments. Medicaid EHR incentive payments are fully funded by the federal government and administered by the states; however, the states are not required to offer EHR incentive payments to providers. The Company recognized \$995,513 and \$149,393 on the consolidated statements of operations for 2015 and 2014, respectively.

Medical Malpractice: The Indiana Medical Malpractice Act limits the maximum recovery for professional liability to \$750,000 per occurrence, \$250,000 of which would be paid through the Company's malpractice insurance coverage, and the balance would be paid by the State of Indiana Patient Compensation Fund. The Company maintains professional liability insurance coverage on a claims-incurred basis. Premiums are expensed in the period to which they relate.

Fair Value of Financial Instruments: The Company's carrying amount for its financial instruments, which include cash, patient accounts receivable, accounts payable, and long-term debt approximates fair value.

Income Taxes: The Company is a limited liability company formed under state statutes and taxed for federal and state purposes as a partnership. Therefore, each member reports their proportionate share of the Company's taxable income or loss on their respective income tax returns.

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

The Company recognizes interest and penalties related to unrecognized tax benefits in interest and income tax expense, respectively. The Company has no amounts accrued for interest or penalties as of December 31, 2015 and 2014. Due to its pass-through status, the Company is not subject to U.S. federal income tax or state income tax. The Company is no longer subject to examination by U.S. federal and State of Indiana taxing authorities for years before January 1, 2012. The Company does not expect the total amount of unrecognized tax benefits to significantly change in the next 12 months.

(Continued)

UNITED SURGEONS, LLC D/B/A
 UNITY MEDICAL AND SURGICAL HOSPITAL
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 December 31, 2015 and 2014

NOTE 2 - PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at December 31:

	<u>2015</u>	<u>2014</u>
Building	\$ 14,379,799	\$ 14,379,799
Software, computer and medical equipment	12,885,483	12,412,050
Furniture, fixtures and office equipment	1,659,621	1,576,410
Leasehold improvements	<u>853,683</u>	<u>810,770</u>
	29,778,586	29,179,029
Accumulated depreciation	<u>(16,446,167)</u>	<u>(13,714,221)</u>
	<u>\$ 13,332,419</u>	<u>\$ 15,464,808</u>

Depreciation expense was \$2,732,394 and \$2,737,425 in 2015 and 2014, respectively.

NOTE 3 - LINE OF CREDIT AGREEMENTS

The Company maintained a line of credit with Lake City Bank with available credit of \$4,000,000. At December 31, 2015 and 2014, the line of credit had principal outstanding of \$4,000,000. Interest accrues daily at bank prime rate. Interest was 3.50% and 3.25% at December 31, 2015 and 2014, respectively.

On April 15, 2015, the Company entered into a loan agreement amendment and received proceeds in the amount of \$1,000,000 under a short-term revolving line of credit arrangement maturing on September 5, 2015. The Company repaid the short-term borrowings on October 15, 2015. On October 21, 2015, the Company entered into a loan agreement amendment that cured the default for the delayed repayment of the short-term borrowings.

The line of credit agreement is secured by all assets of the Company and the personal guarantees of certain members. The line of credit agreement expires on November 11, 2016.

The line of credit agreement is subject to certain financial and non-financial covenants (see Note 4).

NOTE 4 - LONG-TERM DEBT

Long-term debt consists of the following at December 31:

	<u>2015</u>	<u>2014</u>
Lake City Bank - note payable in monthly installments of \$328,564 including interest at 4.25%, maturing on December 23, 2018. On October 21, 2015, the monthly installment was amended and reduced to \$219,000.	\$ 12,993,604	\$ 14,738,967
Current portion of long-term debt	<u>(2,116,687)</u>	<u>(2,628,511)</u>
Long-term debt, net of current portion	<u>\$ 10,876,917</u>	<u>\$ 12,110,456</u>

(Continued)

UNITED SURGEONS, LLC D/B/A
UNITY MEDICAL AND SURGICAL HOSPITAL
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 4 - LONG-TERM DEBT (Continued)

On December 19, 2014, the Company entered into a waiver of principal and interest payments which allowed the December 2014 and January 2015 scheduled payments to be deferred to the maturity of the loan.

On April 14, 2015, the Company entered into a loan agreement amendment which allowed the March, April and May 2015 scheduled principal and interest payments to be deferred to the maturity of the loan.

On October 21, 2015, the Company entered into a loan agreement amendment that adjusted the monthly amount of principal and interest payments due.

The Lake City Bank Loan Restructuring Agreement is secured by all assets of the Company. Certain members also guarantee 56% of the outstanding balance of the note payable with Lake City Bank. The Company makes payments for an irrevocable life insurance policy on a member for which Lake City Bank is the beneficiary, of up to \$5,000,000, in accordance with the terms of the Loan Restructuring Agreement.

The Company is required to maintain certain financial and non-financial covenants under the Loan Restructuring Agreement. As of December 31, 2015, the Company was not in compliance. The Company obtained the appropriate waivers in 2016, respectively, curing covenant non-compliance.

Future principal maturities of outstanding debt at December 31, 2015 are as follows:

2016	\$ 2,116,687
2017	2,191,764
2018	8,685,153

NOTE 5 - LEASES

The Company entered into non-cancelable operating leases for medical and office equipment and facility space through March 2020. Rent and lease expense was \$568,392 and \$576,873 in 2015 and 2014, respectively.

Future payments under operating leases with initial non-cancelable terms of one year or more consisted of the following:

2016	\$ 419,814
2017	134,214
2018	51,597
2019	50,475
2020	<u>4,419</u>
	<u>\$ 660,519</u>

(Continued)

UNITED SURGEONS, LLC D/B/A
 UNITY MEDICAL AND SURGICAL HOSPITAL
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 December 31, 2015 and 2014

NOTE 5 - LEASES (Continued)

The Company has a capital lease with Unity Realty, LLC ("UR"), a party related through common ownership, for the building, and also maintains capital leases for certain medical and office equipment with unrelated various parties. Following is a summary of the capital leases at December 31:

	<u>2015</u>	<u>2014</u>
Building	\$ 14,379,799	\$ 14,379,799
Software, computer and medical equipment	3,452,391	3,218,966
Furniture, fixtures and office equipment	<u>11,036</u>	<u>11,036</u>
	17,843,226	17,609,801
Accumulated depreciation	<u>(6,221,553)</u>	<u>(5,412,278)</u>
	<u>\$ 11,621,673</u>	<u>\$ 12,197,523</u>

Future minimum payments on the capital leases are as follows:

2016	\$ 2,695,884
2017	2,756,864
2018	2,824,240
2019	2,926,229
2020	3,012,221
Thereafter	<u>55,430,455</u>
	69,645,893
Amount representing interest	<u>(52,451,578)</u>
Present value of net minimum lease payments (including current portion of \$128,328)	<u>\$ 17,194,315</u>

Interest expense in excess of capital lease payments of \$445,929 and \$485,458, relative to the UR lease, was recognized as interest expense in 2015 and 2014, respectively.

NOTE 6 - RELATED PARTY TRANSACTIONS

Medical Director Agreements: The Company entered into medical director agreements ("MDA") with individuals who are members of PAM in 2013 which automatically renew for a one year period unless terminated according to the terms of the MDA. The Company incurred \$187,000 and \$313,500 of expenses for medical directory service fees in 2015 and 2014, respectively.

Lease Agreement: The Company entered into a net lease for the building with UR, a related party through common ownership (see Note 5). The term of the lease is for 300 months beginning in October 2009. The UR lease is guaranteed by the members of PAM in direct proportion to their membership in PAM.

Outsourced Billing Company Agreement: In January 2015 the Company began using the services of a related party billing company, Revenue Cycle Management Partners, which is owed by certain UMASH members and senior management.

(Continued)

UNITED SURGEONS, LLC D/B/A
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NOTE 6 - RELATED PARTY TRANSACTIONS (Continued)

Affiliate Receivables (Payables): Following is the composition of affiliate receivables (payables) at December 31:

	<u>2015</u>	<u>2014</u>
<i>Related parties through common ownership:</i>		
Michiana Multi-Specialty Medical Group	\$ 63,624	\$ 63,624
Due from physicians	137,750	30,000
Revenue Cycle Management Partners	(463,876)	-
Due (to)/from physicians	<u>(365,016)</u>	<u>142,846</u>
 Total affiliate receivables (payables)	 <u>\$ (627,518)</u>	 <u>\$ 236,470</u>

Due from Parent: Following is the composition of due from Parent at December 31:

	<u>2015</u>	<u>2014</u>
<i>Physicians ASC Management, LLC:</i>		
Due from Parent	<u>\$ 2,390,207</u>	<u>\$ 1,744,702</u>

The Company has certain transactions with its Parent and from time to time receivables due from the Parent. Management has determined that the repayment of these receivables is dependent upon future distributions received from the Company, and therefore, has classified these receivables in members' deficit on the consolidated balance sheets.

NOTE 7 - CONTINGENCIES AND COMMITMENTS

Litigation: The Company is, at times, involved in general and professional liability claims arising from the use of the hospital, and from provision of medical services in the physician practices, which are defended and handled in the ordinary course of business.

At December 31, 2015 and 2014, management believes that the Company does not have any significant claims or other litigation in which the ultimate resolution is probable and could have a material financial impact, and therefore has not reflected any liabilities, or corresponding receivables, in the consolidated balance sheets.

Settlements: The Company is working with their fiscal intermediary to enter into an extended repayment plan for the 2013 Medicare cost report reimbursement settlement. Without an extended repayment plan, the Company's Medicare payments will be withheld along with interest charged on the unpaid and outstanding balance at a rate of 10% (see Note 1 for additional details).

(Continued)

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NOTE 8 - MANAGEMENT'S PLAN

The Company's current liabilities exceed its current assets by \$3,209,208 and has a members' deficit of \$17,461,762 at December 31, 2015. Additionally, the Company did not meet their loan agreement financial covenants for 2015 and obtained a waiver from their lender in 2016 to cure the noncompliance. The Company continues to work with their lender for financing purposes and is focusing on increasing net patient service revenues along with cost reduction and margin improvement initiatives. The Company's continued existence is based upon its ability to achieve profitable operations and maintain adequate lender financing. As noted in Note 1, in July 2016 the Company is no longer receiving reimbursement related to Medicare services. The Company anticipates entering into an extended repayment plan with Medicare which has not yet been established. See Note 1 for additional settlement details.

NOTE 9 - SUBSEQUENT EVENTS

In April 2016, the Company made a \$683,000 advance payment to its Parent.

Management has performed an analysis of the activities and transactions subsequent to December 31, 2015 to determine the need for any adjustments to and/or disclosures within the financial statements for the year ended December 31, 2015. Management has performed their analysis through September 23, 2016, the date the financial statements were available for issuance and has determined that all material subsequent events have been properly disclosed.