



# Goshen Health System, Inc. and Subsidiaries d/b/a Goshen Health

Consolidated Financial Report  
December 31, 2016

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RSM US LLP

## Independent Auditor's Report

The Board of Directors  
Goshen Health System, Inc.  
d/b/a Goshen Health  
Goshen, Indiana

### Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Goshen Health System, Inc. and Subsidiaries, d/b/a Goshen Health (Goshen Health), formerly known as Indiana University Health Goshen, which comprise the consolidated balance sheet as of December 31, 2016, the related consolidated statements of operations and changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements (collectively, the financial statements).

### Management's Responsibility for the Financial Statements

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

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 financial statements are free from material misstatement.

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

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

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Goshen Health System, Inc. and Subsidiaries, d/b/a Goshen Health as of December 31, 2016, and the results of their operations, changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**THE POWER OF BEING UNDERSTOOD**  
**AUDIT | TAX | CONSULTING**

The Board of Directors  
Goshen Health System, Inc.  
d/b/a Goshen Health

**Other Matter**

The consolidated financial statements of Indiana University Health Goshen, as of and for the year ended December 31, 2015, were audited by other auditors, whose report, dated April 21, 2016, expressed an unmodified opinion on those statements.

*RSM US LLP*

Elkhart, Indiana  
March 22, 2017

**Goshen Health System, Inc. and Subsidiaries  
d/b/a Goshen Health**

**Consolidated Balance Sheets  
December 31, 2016 and 2015  
(In Thousands)**

	2016	2015
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 3,154	\$ 16,403
Patient accounts receivable, less allowance for uncollectible accounts of \$7,421 and \$7,038 in 2016 and 2015 respectively	33,466	31,809
Prepaid expenses and other	7,034	4,737
Inventories	7,316	7,022
<b>Total current assets</b>	<b>50,970</b>	<b>59,971</b>
Assets limited as to use	201,070	174,018
Property and equipment:		
Cost of property and equipment in service	254,655	235,897
Less accumulated depreciation	(146,109)	(136,366)
	108,546	99,531
Construction-in-progress	7,369	9,054
	115,915	108,585
Other assets	778	1,122
<b>Total assets</b>	<b>\$ 368,733</b>	<b>\$ 343,696</b>

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**Goshen Health System, Inc. and Subsidiaries  
d/b/a Goshen Health**

**Consolidated Balance Sheets  
December 31, 2016 and 2015  
(In Thousands)**

	2016	2015
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 11,881	\$ 9,690
Accrued salaries, wages and related liabilities	13,688	13,333
Estimated amounts due to third-party payors	334	300
Current portion of long-term debt	183	2,660
<b>Total current liabilities</b>	<b>26,086</b>	<b>25,983</b>
Noncurrent liabilities:		
Long-term debt, less current portion	45,348	28,607
Other	165	1,066
	<b>45,513</b>	<b>29,673</b>
<b>Total liabilities</b>	<b>71,599</b>	<b>55,656</b>
Net assets:		
Unrestricted net assets	295,680	286,659
Temporarily restricted net assets	1,454	1,381
	<b>297,134</b>	<b>288,040</b>
<b>Total liabilities and net assets</b>	<b>\$ 368,733</b>	<b>\$ 343,696</b>

See notes to consolidated financial statements.

**Goshen Health System, Inc. and Subsidiaries**  
**d/b/a Goshen Health**

**Consolidated Statements of Operations and Changes in Net Assets**  
**Years Ended December 31, 2016 and 2015**  
*(In Thousands)*

	2016	2015
<b>Revenues:</b>		
Patient service revenue (net of contractuals and discounts)	\$ 279,697	\$ 263,407
Provision for uncollectible accounts	<b>(23,288)</b>	(22,741)
Net patient service revenue	<b>256,409</b>	240,666
Other revenue	<b>9,018</b>	10,483
	<b>265,427</b>	251,149
<b>Expenses:</b>		
Salaries, wages and benefits	<b>131,376</b>	120,354
Supplies, drugs, purchased services and other	<b>101,592</b>	87,982
Hospital assessment fee	<b>5,131</b>	3,915
Depreciation and amortization	<b>11,400</b>	11,045
Interest	<b>1,187</b>	1,215
	<b>250,686</b>	224,511
<b>Operating income</b>	<b>14,741</b>	26,638
<b>Nonoperating income (loss):</b>		
Investment income (loss), net	<b>12,084</b>	(4,151)
Loss on interest rate swaps, net	<b>(45)</b>	(29)
Other	<b>217</b>	335
	<b>12,256</b>	(3,845)
<b>Excess of revenues over expenses</b>	<b>26,997</b>	22,793
<b>Other changes in unrestricted net assets:</b>		
Net asset transfer to Indiana University Health	<b>(17,976)</b>	-
Increase in unrestricted net assets	<b>9,021</b>	22,793
<b>Temporarily restricted net assets:</b>		
Contributions	<b>234</b>	369
Net assets released from restriction	<b>(161)</b>	(741)
Increase (decrease) in temporarily restricted net assets	<b>73</b>	(372)
<b>Increase in net assets</b>	<b>9,094</b>	22,421
Net assets at beginning of year	<b>288,040</b>	265,619
Net assets at end of year	<b>\$ 297,134</b>	\$ 288,040

See notes to consolidated financial statements.

**Goshen Health System, Inc. and Subsidiaries**  
**d/b/a Goshen Health**

**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2016 and 2015**  
*(In Thousands)*

	2016	2015
Cash flows from operating activities:		
Increase in net assets	\$ 9,094	\$ 22,421
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Net asset transfer to Indiana University Health	17,976	-
Change in fair value of interest rate swaps	245	43
Loss on interest rate swaps	(45)	(72)
Provision for uncollectible patient accounts	23,288	22,741
Depreciation and amortization	11,400	11,045
Change in restricted net assets	(73)	372
Trading securities	(9,052)	(10,833)
Changes in operating assets and liabilities:		
Patient accounts receivable	(24,945)	(24,464)
Prepaid expenses, inventories, and other assets	(2,247)	(1,369)
Accounts payable, accrued expenses and other liabilities	1,090	(428)
Accrued salaries, wages and related liabilities	355	(620)
Estimated amounts due to third-party payors	34	(1,200)
<b>Net cash provided by operating activities</b>	<b>27,120</b>	<b>17,636</b>
Cash flows from investing activities:		
Purchase of property and equipment, net of disposals	(18,730)	(14,649)
Restricted funds placed in escrow	(18,000)	-
<b>Net cash used in investing activities</b>	<b>(36,730)</b>	<b>(14,649)</b>
Cash flows from financing activities:		
Change in restricted net assets	73	(372)
Proceeds from issuance of long-term debt	28,086	-
Repayments on and refinancing of long-term debt	(31,798)	(1,443)
<b>Net cash used in financing activities</b>	<b>(3,639)</b>	<b>(1,815)</b>
<b>(Decrease) increase in cash and cash equivalents</b>	<b>(13,249)</b>	<b>1,172</b>
Cash and cash equivalents:		
Beginning of year	16,403	15,231
End of year	<b>\$ 3,154</b>	<b>\$ 16,403</b>

See notes to consolidated financial statements.



**Goshen Health System, Inc. and Subsidiaries  
d/b/a Goshen Health**

**Notes to Consolidated Financial Statements  
(Dollars in Thousands)**

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**Mission Statement**

*The mission of Goshen Health is to improve the health of our communities by providing innovative, outstanding care and services, through exceptional people doing exceptional work.*

*Compassion – and commitment to service with empathy.*

*Accountability – with integrity and action.*

*Respect – through treating others as you wish to be treated.*

*Excellence – in all we do.*

*Building upon our mission and values, Goshen Health will deliver exceptional healthcare to the communities we serve using an integrated model of care and achieving excellence through a commitment to quality, leadership and innovation. By 2020, we will achieve this vision by focusing on the following strategic priorities:*

- 1. Lead the region in clinical integration and the management of population health.*
- 2. Deliver high value to our patients, providers, payers and Colleagues.*
- 3. Goshen's Oncology and Heart & Vascular service lines become the destination of choice in our broader region.*
- 4. Cultivate a culture for Colleagues where personal and professional missions are aligned.*
- 5. Inspire a spirit of partnership and generosity by engaging our community with opportunities that meet regional health needs.*

**Note 1. Organization and Nature of Operations**

The accompanying consolidated financial statements represent the accounts of Goshen Health System, Inc. d/b/a Goshen Health and its various affiliated corporations under the control of Goshen Health. Goshen Health is an Indiana not-for-profit corporation exempt from federal income tax under Internal Revenue Code (IRC) Section 501(a) as an organization described in Section 501(c)(3) and a public charity as described in Section 509(a)(3).

Goshen Health was formerly known as Indiana University Health Goshen. From March 1, 2000, through December 31, 2016, Indiana University Health, Inc. (IUH) was the sole corporate member of Goshen Health System, Inc. (System) under an Integrated Definitive Agreement (IDA) between the organizations. In December 2016, the System executed a Separation Agreement with IUH which resulted in the termination of the IDA and the withdrawal of IUH as the System's sole corporate member effective December 31, 2016.

Goshen Health is the sole corporate member of the following entities:

- Goshen Hospital Association, Inc. d/b/a Goshen Hospital is a not-for-profit, acute-care hospital servicing Goshen, Indiana, and surrounding communities in northern Indiana.
- Parkmor Drug, Inc. and Subsidiaries d/b/a Goshen Home Medical, a for-profit corporation, operates a home medical equipment business in Goshen, Indiana.
- Indiana Lakes Managed Care Organization, LLC, a for-profit organization, provides management services for managed care arrangements entered into by Goshen Health and third parties.
- Goshen Health Surgery Center, LLC, a for-profit organization, is an outpatient surgery center in Goshen, Indiana.

**Goshen Health System, Inc. and Subsidiaries**  
**d/b/a Goshen Health**

**Notes to Consolidated Financial Statements**  
**(Dollars in Thousands)**

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**Note 1. Organization and Nature of Operations (Continued)**

- Goshen Health Foundation, Inc. (Foundation), a not-for-profit organization, is a philanthropic organization committed to partnering with individuals and organizations to address the community health needs of Goshen, Indiana, and its surrounding communities.

**Note 2. Community Benefit and Charity Care**

Goshen Health provides health care services and other financial support through various programs that are designed, among other matters, to enhance the health of the community. In addition, Goshen Health provides services intended to benefit the poor and underserved, including those persons who cannot afford health insurance because of inadequate resources or those who are uninsured or underinsured. Health care services to patients under government programs, such as Medicare and Medicaid, are also considered part of Goshen Health's benefit provided to the community since a substantial portion of such services are reimbursed at amounts less than cost.

Goshen Health's financial assistance policies are designed to provide care to patients regardless of their ability to pay, and all uninsured patients are eligible for discounts from established charges. Patients who meet certain criteria (generally based on up to 400% of federal poverty income guidelines and other patients who are victims of certain catastrophic events) are provided care without charge or at amounts less than established rates.

Patient service revenue is reported at estimated net realizable amounts for services rendered. Goshen Health recognizes patient revenue associated with patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients who do not qualify for charity care, revenue is recognized on the basis of discounted rates in accordance with an uninsured discount policy.

The amount of charity care provided is determined based on the qualifying criteria, as defined in the financial assistance policies, through approved applications completed by patients and their families or beneficiaries. Eligibility may also be determined based on analysis of patients without third-party insurance coverage who did not apply for charity and whose income was equal to or less than 200% of federal poverty income guidelines. No payment for services is anticipated for those patients whose charity care applications have been approved, as well as for those other patients whose income is equal to or less than 200% of federal poverty income guidelines and who meet certain other criteria. The cost to provide charity care, estimated by applying the consolidated cost to charge ratio to charges foregone for charity care, was \$2,650 and \$3,449 for the years ended December 31, 2016 and 2015 respectively.

In addition, Goshen Health provides a significant amount of uncompensated care to other uninsured and underinsured patients, which is included in the provision for uncollectible patient accounts.

Enacted March 23, 2010, the Patient Protection and Affordable Care Act (ACA) required, among other things, that hospital organizations establish a financial assistance policy and a policy relating to emergency medical care. Goshen Health has adopted a financial assistance policy that conforms with the ACA and includes financial assistance eligibility criteria, the basis for calculating amounts charged to patients, the method of applying for financial assistance, billing and collections policies with regard to actions that may be taken in the case of non-payment, as well as measures to widely publicize the policies within the communities served. Additionally, hospital organizations must adopt policies that require them to provide, without discrimination, care for emergency medical conditions to individuals regardless of their eligibility under the organizations' financial assistance policies. Goshen Health has also adopted policies to limit the amount charged for emergency or other medically necessary care that is provided to individuals eligible for assistance under its financial assistance policy to no more than the amounts generally billed to individuals who have insurance covering such care.

**Goshen Health System, Inc. and Subsidiaries**  
**d/b/a Goshen Health**

**Notes to Consolidated Financial Statements**  
**(Dollars in Thousands)**

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**Note 2. Community Benefit and Charity Care (Continued)**

Reimbursements are received by Goshen Health for Medicare and Medicaid beneficiaries in accordance with reimbursement agreements and related rules and regulations. Also, Goshen Health receives certain payments under the Medicaid Assessment Fee program from the state of Indiana (see Note 4). These reimbursements and payments are less than the cost of providing the related services.

Through the community health needs assessment that Goshen Health conducted, the following community health needs were identified and selected as priority areas in which Goshen Health will focus on community benefit efforts: access to primary health care, access to behavioral health care, obesity prevention, smoking cessation, and diabetes education. The costs of providing these programs and services are included in expenses in the accompanying consolidated statements of operations and changes in net assets.

**Note 3. Significant Accounting Policies**

**Principles of consolidation:** The consolidated financial statements include the accounts of Goshen Health and all majority-owned or controlled subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

**Use of estimates:** The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

**Cash and cash equivalents:** Investments in highly liquid debt instruments with a maturity of three months or less when purchased, excluding assets limited as to use, are considered by management to be cash equivalents. Goshen Health places its cash and cash equivalents with institutions of high credit quality and/or positions them such that they are insured by the Federal Deposit Insurance Corporation in order to mitigate potential concentrations of credit risk.

**Patient accounts receivable, estimated amounts due to third-party payors, and net patient service revenue:** Patient accounts receivable and net patient service revenue are reported at estimated net realizable amounts due from patients, third-party payors (e.g. Medicare, Medicaid, health maintenance organizations, and commercial insurance companies), and others at the time services are rendered. Provision is made, by a charge to contractual allowances that reduce patient service revenue, for the difference between gross charges for patient services and estimated reimbursement from these third-party payors. Certain revenue is subject to estimated retroactive revenue adjustments under reimbursement agreements with third-party payors due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period that the related services are rendered, and such amounts are adjusted in future periods as adjustments become known, or as reimbursement periods are settled and are no longer subject to such audits, reviews, and investigations. Changes in estimated amounts due to third-party payors increased patient service revenue during the year ended December 31, 2016 by approximately \$34.

**Notes to Consolidated Financial Statements**  
**(Dollars in Thousands)**

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**Note 3. Significant Accounting Policies (Continued)**

The provision for uncollectible patient accounts, for all payors, is recognized when services are provided based upon management's assessment of historical and expected net collections, taking into consideration business and economic conditions, changes and trends in health care coverage, and other collection indicators. Periodically, management assesses the adequacy of the allowance for uncollectible accounts based upon accounts receivable payor composition and aging, the significance of individual payors to outstanding accounts receivable balances, and historical write-off experience by payor category, as adjusted for collection indicators. The results of the review are then used to make any modifications to the provision for uncollectible accounts and the allowance for uncollectible accounts. In addition, Goshen Health follows established guidelines for placing certain past due patient balances with collection agencies. Patient accounts that are uncollected, including those placed with collection agencies, are initially charged against the allowance for uncollectible accounts in accordance with collection policies of Goshen Health and, in certain cases, are reclassified to charity care if deemed to otherwise meet financial assistance policies of Goshen Health.

**Inventories:** Inventories consist primarily of drugs and supplies, are stated at the lower of cost or market, and are valued using the average cost method.

**Assets limited as to use:** Assets limited as to use include the following: (i) cash and cash equivalents and designated investment assets, set aside by the Board of Directors for future capital improvements and for other purposes, over which the Board retains control and may, in certain circumstances, use for other purposes and (ii) investments required to be held in escrow under the separation agreement with IUH (see Note 7). Substantially all assets limited as to use are invested and managed by professional investment managers and are held in custody by financial institutions.

Investments in equity securities with readily determinable fair values and all investments in debt securities are classified as trading securities and are measured at fair value based on quoted market prices. Investments in hedge funds are recorded under the equity method of accounting, based on the fund's financial information. Generally, the net asset value (NAV) of these funds reflects the contributed capital, as well as an allocated share of the underlying limited partnership's realized and unrealized gains and losses.

Accordingly, changes in unrealized gains and losses in the fair value of investments are included in non-operating income (loss) within investment income (loss), net, in the accompanying consolidated statements of operations and changes in net assets. Goshen Health is a limited partner in certain funds that employ hedged investment strategies. These investments are accounted for using the equity method of accounting, based on the fund's financial information.

Investment income or loss (including realized gains and losses on the sale of investments, unrealized gains and losses on trading securities, and changes in the carrying value of hedge funds), is reported as nonoperating income (loss) unless the income is restricted by donor or law. The cost of securities sold is based on the specific-identification method.

Investment securities purchased and sold are reported based on the trade date. Due to the period lag between the trade and settlement date, Goshen Health reports receivables for securities sold but not settled and reports liabilities for securities purchased but not settled. These receivables and payables are settled from within the investment portfolio and are presented on a net basis within assets whose use is limited in the consolidated balance sheets.

**Notes to Consolidated Financial Statements**  
**(Dollars in Thousands)**

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**Note 3. Significant Accounting Policies (Continued)**

**Property and equipment:** Property and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the assets. Interest cost incurred on borrowed funds during the period of construction and other interest costs related to tax-exempt bonds are capitalized as a component of the cost of constructing the assets. In addition, interest earnings on unexpended borrowed funds related to tax-exempt financings offset capitalized tax-exempt interest. Repairs and maintenance costs are expensed when incurred.

Goshen Health evaluates when events or changes in circumstances have occurred that would indicate that the remaining estimated useful life of long-lived assets warrant revision or that the remaining balance of such assets may not be recoverable. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset or asset group. If undiscounted cash flows are insufficient to recover the carrying value of the long-lived asset, such asset is written down to its fair value if its carrying value exceeds fair value.

**Equity interest in unconsolidated subsidiaries:** Goshen Health has also entered into certain limited liability company agreements with third parties that provide health care-related services. Where applicable, these arrangements are accounted for using the equity method of accounting. Overall, equity interest in unconsolidated subsidiaries recorded within other assets on the consolidated balance sheets was \$723 and \$653 as of December 31, 2016 and 2015 respectively. Goshen Health reports its interest in the income of its unconsolidated subsidiaries within other nonoperating income, totaling \$155 and \$107 during the years ended December 31, 2016 and 2015 respectively.

**Derivative financial instruments:** As part of its debt management program, Goshen Health has entered into certain interest rate swap transactions (fixed-pay swaps). Derivative financial instruments are recognized as either assets or liabilities in the consolidated balance sheets at fair value. During the years ended December 31, 2016 and 2015, these fixed-pay swap agreements did not qualify for hedge accounting, and accordingly, the changes in fair value of those interest rate swap agreements are reported with nonoperating income (loss) in the consolidated statements of operations and changes in net assets. Net settlement payments on interest rate swaps are reported in non-operating income (loss) in the consolidated statements of operations and changes in net assets.

**Contributions:** Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give, including indications of an intention to give, are reported at fair value at the date the gift is received. If the gifts are received with donor stipulations that limit the use of the donated assets, the gifts are reported as either temporarily or permanently restricted. Donor-restricted contributions for which restrictions are met in the same year as received are reported as unrestricted contributions in the accompanying consolidated statements of operations and changes in net assets.

**Temporarily restricted net assets:** Temporarily restricted net assets are those assets whose use has been limited by donors to a specific time period or purpose. These net assets are generally restricted for medical supplies and equipment and patient care services.

**Income taxes:** The Internal Revenue Service has determined that Goshen Health and certain affiliated entities are tax-exempt organizations as defined in Section 501(c)(3) of the Internal Revenue Code. Certain subsidiaries of Goshen Health are taxable entities, the tax expense and liabilities of which are not material to the consolidated financial statements.

**Notes to Consolidated Financial Statements**  
**(Dollars in Thousands)**

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**Note 3. Significant Accounting Policies (Continued)**

Goshen Health and its tax-exempt affiliated entities each file a Form 990 (Return of Organization Exempt from Income Tax) annually. When these returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would ultimately be sustained. Examples of tax positions common to health systems include such matters as the tax-exempt status of each entity, the continued tax-exempt status of bonds, the nature, characterization and taxability of joint venture income, and various positions relating to potential sources of unrelated business taxable income (reported on Form 990T). As of December 31, 2016 and 2015, there are no unrecognized tax benefits resulting from uncertain tax positions.

Forms 990 and 990T filed by Goshen Health and its tax-exempt affiliated entities are subject to examination by the Internal Revenue Service up to three years from the extended due date of each return. Forms 990 and 990T filed by Goshen Health and its tax-exempt affiliated entities are no longer subject to examination for tax year 2013 and prior.

**Operating and performance indicators:** The activities of Goshen Health are primarily related to providing health care services and, accordingly, expense information by functional classification is not used as a basis for measuring performance. Furthermore, since substantially all resources are derived from providing health care services, similar to that if provided by a business enterprise, the following indicators are considered important in evaluating how well management has discharged its stewardship responsibilities:

**Operating indicator (operating income):** Includes all unrestricted revenue, gains, donor contributions to offset operating expenses, other support, and expenses directly related to the recurring and ongoing health care operations during the reporting period. The operating indicator excludes investment income or losses on assets limited as to use (including changes in unrealized gains and losses on trading securities), changes in the fair value of interest rate swaps, gains and losses related to equity interests in unconsolidated subsidiaries, and other gains and losses deemed by management not to be directly related to providing health care services.

**Performance indicator (excess of revenues over expenses):** Includes operating income and nonoperating income (loss). The performance indicator excludes certain changes in contributions for capital expenditures and net assets released from restricted funds.

**Newly adopted accounting pronouncement:** In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-1, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This guidance changes how entities account for equity investments that do not result in consolidation and are not accounted for under the equity method of accounting. Entities will be required to measure these investments at fair value at the end of each reporting period and recognize changes in fair value in net income (excess of revenue over expenses). This guidance also changes certain disclosure requirements and other aspects of current U.S. GAAP. The guidance is effective for Goshen Health's December 31, 2019 consolidated financial statements. Goshen Health elected to early adopt the amendment that no longer requires disclosure of the fair market value of financial instruments that are not measured at fair value and, as such, these disclosures are not included herein. Goshen Health is currently evaluating the impact of the adoption of the remaining provisions of ASU 2016-01 on the consolidated financial statements.

Notes to Consolidated Financial Statements  
(Dollars in Thousands)

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**Note 3. Significant Accounting Policies (Continued)**

**New accounting pronouncements not yet adopted:** In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. The guidance will be effective for Goshen Health's December 31, 2018 consolidated financial statements. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that period. Goshen Health has not yet selected a transition method and is currently evaluating the effect of the new standard on the consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases—(Topic 842)*, which supersedes the leasing guidance in *Topic 840, Leases*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the statement of operations. The new standard is effective for Goshen Health's December 31, 2019 consolidated financial statements. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. Goshen Health is currently evaluating the effect of the new standard on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. Key elements of the ASU include a reduction in the number of net asset categories from three to two, conforming requirements on releases of capital restrictions, several new requirements related to expense presentation and disclosure (including investment expenses), and new required disclosures communicating information useful in assessing liquidity. The ASU will be effective for Goshen Health's December 31, 2018 consolidated financial statements. Early adoption is permitted. Retrospective application is required for many provisions of this guidance. Goshen Health is currently evaluating the effect of the new standard on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 provides guidance on how certain cash receipts and cash payments should be presented and classified in the statement of cash flows with the objective of reducing existing diversity in practice with respect to these items. The new standard will be effective for Goshen Health's December 31, 2019 consolidated financial statements. Early adoption is permitted. ASU 2016-15 requires a retrospective transition method. However, if it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. Goshen Health is currently evaluating the effect of the new standard on the consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. ASU 2016-18 applies to all entities that have restricted cash or restricted cash equivalents and are required to present a statement of cash flows. Its provisions require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. As a result, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The new standard will be effective for Goshen Health's December 31, 2019 consolidated financial statements. Early adoption is permitted. ASU 2016-18 requires a retrospective transition method. Goshen Health is currently evaluating the effect of the new standard on the consolidated financial statements.

**Reclassifications:** Certain prior-year amounts have been reclassified to conform to the current-year presentation, with no effect on operating income, excess of revenues over expenses or net assets.

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**Note 3. Significant Accounting Policies (Continued)**

**Subsequent events:** Management has evaluated subsequent events and transactions through March 22, 2017, the date that these consolidated financial statements were issued. During this period, there were no subsequent events requiring recognition or disclosure in the consolidated financial statements.

**Note 4. Patient Service Revenue and Accounts Receivable**

Patient service revenue, net of contractual allowances and discounts and before the provision for uncollectible accounts, was received from the following major payor sources during the years ended December 31, 2016 and 2015:

	2016	2015
Managed care programs	60%	57%
Medicare	21	23
Medicaid	7	8
Self-pay patients	7	10
Other third-party payors	5	2
	<u>100%</u>	<u>100%</u>

A single managed care provider represented 30% and 27% of net patient service revenue for the years ended December 31, 2016 and 2015 respectively.

During 2012, the Indiana General Assembly approved a hospital assessment fee program (Medicaid Assessment Fee (MAF)). Under this program, the Office of Medicaid Policy and Planning collects a fee from eligible hospitals. The fee is used in part to increase reimbursement to eligible hospitals for services provided in both fee-for-service and managed care programs, as the state's share of Medicaid Disproportionate Share (DSH) payments. The program was effective retroactively from July 1, 2011, and continued through June 30, 2013. Subsequently, the Indiana General Assembly and the Centers for Medicare and Medicaid Services (CMS) approved the extension of the MAF program for another four years.

For the years ended December 31, 2016 and 2015, increased reimbursement related to the MAF program was recorded within net patient service revenue on the consolidated statements of operations and changes in net assets totaling \$7,116 and \$6,782 respectively. During the years ended December 31, 2016 and 2015, an assessment fee was recognized of \$5,131 and \$3,915 respectively, which is reported as hospital assessment fee expense on the consolidated statements of operations and changes in net assets.

Laws and regulations governing Medicare, Medicaid, and other governmental programs are extremely complex, subject to interpretations, and sometimes provide for retroactive adjustments. As a result, there is a reasonable possibility that recorded estimated settlements could change by a material amount in the near term. Goshen Health believes it is in compliance with applicable laws and regulations governing Medicare, Medicaid, and other governmental programs and that adequate provisions have been recorded for any adjustments that may result from final settlements. However, any adjustments to the currently estimated settlements will be recorded in future periods.

For the delivery of health care services Goshen Health does not require collateral or other security from its patients, substantially all of whom are residents of the state of Indiana. However, assignment of benefit payments payable under patients' health insurance programs and plans (e.g. Medicare, Medicaid, health maintenance organizations, and commercial insurance policies) is routinely obtained, consistent with industry practice.



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**Note 4. Patient Service Revenue and Accounts Receivable (Continued)**

The composition of net patient accounts receivable as of December 31, 2016 and 2015, is as follows:

	2016	2015
Managed care	55%	54%
Medicare	19	20
Patients	11	10
Other third-party payors	8	7
Medicaid	7	9
	<u>100%</u>	<u>100%</u>

A single managed care payor represented 26% and 23% of net patient accounts receivables at December 31, 2016 and 2015 respectively.

The allowance for uncollectible accounts for self-pay patients, including self-pay discounts, and charity care, was 81% of self-pay accounts receivable as of both December 31, 2016 and 2015.

**Note 5. Assets Limited as to Use**

As of December 31, 2016 and 2015, assets whose use is limited consisted of the following:

	2016	2015
Board-designated investments	\$ 183,070	\$ 174,018
Investments held in escrow under Separation Agreement with IUH (See Note 7)	18,000	-
	<u>\$ 201,070</u>	<u>\$ 174,018</u>

Assets limited as to use are invested in accordance with Board approved policies. The estimated fair value of the assets limited as to use is determined using market information and other appropriate valuation methodologies. The methods and assumptions used to estimate the fair value of assets limited as to use are as follows: (i) cash and cash equivalents: the carrying amounts reported in the consolidated balance sheets approximate fair value; (ii) marketable securities: the fair values are based on quoted market prices or, if quoted market prices are not available, quoted market prices of comparable instruments and other observable inputs; and (iii) other investments, including alternative investments (such as hedge funds): accounted for using the equity method of accounting based upon the net asset values as determined by third-party administrators of each fund in consultation with and approval of the fund investment managers.

Goshen Health is a limited partner in funds that employ hedged investment strategies and funds that employ investment strategies that require long holding periods to create value, both of which are designed to reduce overall portfolio volatility. In the case of hedged strategies, redemptions generally may be made quarterly with written notice required 15 days prior to the end of the applicable quarter; however, some funds employ aggregate redemption caps that restrict redemptions. These investments are accounted for using the equity method of accounting, based on the fund's financial information.

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**Note 5. Assets Limited as to Use (Continued)**

Alternative investments include certain other risks that may not exist with other investments that are more widely traded. These include reliance on the skill of the fund managers, who often employ complex strategies utilizing various financial instruments, including futures contracts, foreign currency contracts, structured notes, and interest rate, total return, and credit default swaps. Additionally, alternative investments may provide limited information on a fund's underlying assets and have restrictive liquidity provisions. Management believes that Goshen Health, in consultation with its investment consultant, has the capacity to analyze and interpret the risks associated with alternative investments and, with this understanding, has determined that these investments represent a prudent approach for use in its portfolio management.

As of December 31, 2016 and 2015, assets limited as to use consisted of the following:

	2016	2015
Cash and cash equivalents	\$ 18,880	\$ 3,946
Marketable securities:		
Fixed income securities	16,231	25,227
Structured notes	4,018	-
Global equities	18,946	18,571
Domestic equities	-	2,600
Mutual funds	142,772	123,429
	<u>200,847</u>	<u>173,773</u>
Alternative investments	223	245
	<u>\$ 201,070</u>	<u>\$ 174,018</u>

The composition and presentation of investment income (loss) reported in the accompanying consolidated statements of operations and changes in net assets for the years ended December 31, 2016 and 2015 are as follows:

	2016	2015
Interest and dividend income	\$ 4,483	\$ 3,518
Investment management and administration fees	(649)	(591)
Realized (losses) gains on sales of investments, net	(2,887)	1,514
Unrealized gains (losses) on investments	11,137	(8,516)
Realized losses on alternative investments	-	(76)
	<u>\$ 12,084</u>	<u>\$ (4,151)</u>

**Note 6. Property and Equipment**

The cost of property and equipment in service as of December 31, 2016 and 2015 is summarized as follows:

	2016	2015
Land and improvements	\$ 8,435	\$ 9,498
Buildings and improvements	108,725	100,118
Equipment	137,495	126,281
	<u>\$ 254,655</u>	<u>\$ 235,897</u>

**Goshen Health System, Inc. and Subsidiaries  
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**Note 6. Property and Equipment (Continued)**

Property and equipment is depreciated on a straight-line basis beginning in the month when placed in service. Useful lives of each category of assets are based on the estimated useful time frame that the particular assets are expected to be in service, generally in accordance with guidelines established by the American Hospital Association. Asset lives range as follows:

	<u>Years</u>
Land improvements	20-30
Buildings and improvements	15-40
Equipment, including software developed for internal use	3-10

Construction-in-progress for assets currently under development is anticipated to extend through 2017 and includes commitments for the construction, refurbishment, and replacement of facilities and equipment. A summary of the construction-in-progress as of December 31, 2016 and 2015 is as follows:

	<u>2016</u>	<u>2015</u>
Miscellaneous projects	\$ 2,793	\$ 912
Medical equipment	1,714	505
IT projects	2,571	1,014
MOB buildings	91	2,387
Surgery Center	-	2,115
Building improvements	200	2,121
	<u>\$ 7,369</u>	<u>\$ 9,054</u>

Firm commitments for construction-in-progress totaled \$6,438 at December 31, 2016.

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**Note 7. Long-Term Debt**

Long-term debt at December 31, 2016 and 2015 consists of the following:

	2016	2015
<b>Loans from Indiana University Health:</b>		
Note payable to IU Health under Separation Agreement, payable in annual installments through 2026	\$ 15,976	\$ -
Loan payable in varying principal installments, including interest at 6.05%, repaid in December 2016	-	1,134
Loan payable in varying principal installments, including interest at 0.31%, repaid in December 2016	-	8,681
Loan payable in varying principal installments, including interest at 5.54%, repaid in December 2016	-	18,614
<b>Loans from Key Bank:</b>		
Mortgage obligations (interest rates ranging from 1.66% to 1.69%)	1,469	2,838
Line of credit, including interest at LIBOR plus 1.5% (3.17% at December 31, 2016)	28,086	-
	<u>45,531</u>	<u>31,267</u>
Less current portion	(183)	(2,660)
	<u>\$ 45,348</u>	<u>\$ 28,607</u>

From November 1, 2000 through December 31, 2016, Goshen Health System, Inc. and Goshen Hospital Association, Inc. were designated as Obligated Group Affiliates pursuant to the terms of the Indiana University Health, Inc. (IUH) Master Trust Indenture. As part of the Separation Agreement executed in December 2016 with IUH, Goshen Health repaid all of the then-existing loans from IUH and, effective December 31, 2016, Goshen Health System, Inc. and Goshen Hospital Association, Inc. were deemed to have been withdrawn as Obligated Group Affiliates.

The IUH loans were repaid with amounts drawn on a \$35,000 unsecured line of credit with Key Bank, which requires monthly interest payments until it expires December 29, 2019, at which time any outstanding draws on the line of credit must be repaid in full.

As a condition of the Separation Agreement with IUH, Goshen Health agreed to pay IUH a separation payment of \$20,000. Of this amount, \$2,000 was paid in December 2016, with required annual payments of \$2,000 beginning in January 2018. Goshen Health has recognized a liability of \$15,976 at December 31, 2016 for the present value of these future annual payments, discounted at 2.45%. The Separation Agreement includes certain restrictions on IUH's activities within Goshen Health's service area through December 31, 2026. Violations of these restrictions that remain uncured for more than ninety days will result in termination of Goshen Health's obligation to repay any remaining amounts due to IUH under the Separation Agreement.

The Separation Agreement required Goshen Health to place into escrow \$18,000 to be used to fund these future payments.

In June 2014, Goshen Health modified the terms of a mortgage obligation with Key Bank, extending the due date of a balloon payment from June 2014 to June 2019.

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**Note 7. Long-Term Debt (Continued)**

The scheduled maturities and mandatory redemptions of long-term debt as of December 31, 2016 are as follows:

Year ending December 31:		
2017	\$	183
2018		2,189
2019		31,184
2020		2,000
2021		2,000
Thereafter		<u>10,000</u>
		47,556
Unamortized discount		<u>(2,025)</u>
	\$	<u>45,531</u>

Total interest paid on long-term debt for the years ended December 31, 2016 and 2015 was \$1,187 and \$1,215 respectively. No interest was capitalized in either 2016 or 2015.

**Note 8. Fair Value Measurement**

The accounting guidance for the application of fair value provides, among other matters, for the following: defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establishes a framework for measuring fair value; establishes a three-level hierarchy for fair value measurements based upon the observability of inputs to the valuation of an asset or liability as of the measurement date; requires consideration of non-performance risk when valuing liabilities; and expands disclosures about instruments measured at fair value. The three level hierarchy is based upon the nature of valuation techniques and whether such techniques are based upon observable or unobservable inputs, as defined.

Observable inputs are intended to reflect market data obtained from independent sources, while unobservable inputs may reflect market assumptions made by management or measurements made by financial specialists generally associated with the financial asset or liability. These two types of inputs create the following fair value hierarchy:

- Level 1** Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the reporting date.
- Level 2** Pricing inputs other than quoted prices included in Level 1 that are either directly observable or that can be derived or supported from observable data as of the reporting date.
- Level 3** Pricing inputs include those that are significant to the fair value of the financial asset or financial liability and are not observable from objective sources. In evaluating the significance of inputs, management generally classifies assets or liabilities as Level 3 when their fair value is determined using unobservable inputs that individually, or in the aggregate, represent more than 10% of the fair value of the assets or liabilities. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

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**Note 8. Fair Value Measurement (Continued)**

The fair value of financial assets and liabilities measured at fair value on a recurring basis was determined using the following inputs at December 31, 2016 and 2015:

	December 31, 2016			
	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Cash and cash equivalents	\$ 18,880	\$ -	\$ -	\$ 18,880
Marketable securities:				
Fixed income securities	-	16,231	-	16,231
Mutual funds	142,772	-	-	142,772
Global equities	18,946	-	-	18,946
Structured notes	-	4,018	-	4,018
	<u>\$ 180,598</u>	<u>\$ 20,249</u>	<u>\$ -</u>	<u>\$ 200,847</u>
<b>Liabilities</b>				
Interest rate swaps	\$ -	\$ 87	\$ -	\$ 87
	December 31, 2015			
	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Cash and cash equivalents	\$ 3,946	\$ -	\$ -	\$ 3,946
Marketable securities:				
Fixed income securities	-	25,227	-	25,227
Mutual funds	123,429	-	-	123,429
Domestic equities	2,600	-	-	2,600
Global equities	18,571	-	-	18,571
	<u>\$ 148,546</u>	<u>\$ 25,227</u>	<u>\$ -</u>	<u>\$ 173,773</u>
<b>Liabilities</b>				
Interest rate swaps	\$ -	\$ 252	\$ -	\$ 252

The fair value of cash and cash equivalents, which consist mainly of funds invested in money market funds, is based on quoted market prices and classified as Level 1. The fair value of Level 1 trading securities is based on quoted market prices from an active exchange. The fair value of Level 2 trading securities is based on third-party market quotes in an inactive market or similar securities in an active market and other observable inputs. The fair value of interest rate swaps is based upon forward interest rate curves, as adjusted for credit valuation.

Cash and cash equivalents not held in money market funds aggregated \$3,154 and \$16,403 as of December 31, 2016 and 2015 respectively, and are not included in the tables. Goshen Health's \$223 and \$245 of alternative investments as of December 31, 2016 and 2015 respectively, are not included in the tables because they are accounted for using the equity method of accounting (see Note 5).

Transfers are generally recorded at the end of the reporting period. There were no material transfers between Level 1 and Level 2.

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**Note 9. Commitments and Contingencies**

Goshen Health is from time to time subject to various legal proceedings and claims arising in the ordinary course of business. Goshen Health's management does not expect that the outcome in any of its currently ongoing legal proceedings or the outcome of any other claims, individually or collectively, will have a material adverse effect on Goshen Health's financial condition, results of operations, or cash flow.

**Leases:** Buildings, medical and office equipment are leased under non-cancelable operating leases. Future minimum lease payments as of December 31, 2016, are as follows:

Year ending December 31:	
2017	\$ 1,907
2018	1,468
2019	1,338
2020	1,095
2021	302
	<u>\$ 6,110</u>

Rent and lease expense, included in supplies, drugs, purchased services, and other expenses in the accompanying consolidated statements of operations and changes in net assets, amounted to \$2,662 and \$2,677 for the years ended December 31, 2016 and 2015 respectively.

**Note 10. Malpractice Insurance**

Goshen Health's medical malpractice coverage is provided through a pooled risk sharing arrangement with the Suburban Health Organization Risk Retention Group, LLC. The program of medical malpractice coverage considers limitations in claims and damages prescribed by the Indiana Medical Malpractice Act (Act), which limits the amount of individual claims to \$1,250 and annual aggregate claims of \$7,500, of which up to \$1,000 would be paid by the State of Indiana Patient Compensation Fund (Fund) and \$250 by Goshen Health for each occurrence of malpractice. The Act also requires that health care providers meet certain requirements, including making funding payments to the Fund and maintaining certain insurance levels. Goshen Health has met these requirements and is a qualified provider under the Act, retaining risk of \$250 per occurrence and \$7,500 in the annual aggregate.

**Note 11. Retirement Plans**

Retirement benefits are provided to substantially all Colleagues of Goshen Health through defined-contribution plans. Contributions, which are included in benefits expense, to the defined-contribution plans are based on compensation of qualified Colleagues and amounted to \$6,242 and \$5,202 for the years ended December 31, 2016 and 2015 respectively (net of forfeitures of \$129 in each of 2016 and 2015).

**Note 12. Related Party Transactions**

Through December 21, 2015, Goshen Health utilized various centralized programs and overhead services of Indiana University Health or its other sponsored organization, including risk management, treasury, debt management, executive management support, administrative services, and information technology services. The charges allocated to Goshen Health for these services represent both allocations of common costs and specifically identified expenses that are incurred by Indiana University Health of behalf of Goshen Health. Allocations were based on relevant metrics, such as Goshen Health's pro rata share of revenues, certain costs, or debt to the consolidated totals of Indiana University Health. The charges allocated to Goshen Health were approximately \$3,333 for the year ended December 31, 2015, and were included in operating expenses in the accompanying consolidated statement of operations and changes in net assets.

**Note 13. Health Care Legislation and Regulation**

Under Indiana law (IC 12-15-16 (1-3)), health care providers qualifying as State of Indiana Medicaid Acute Disproportionate Share and Medicaid Safety Net Hospitals (DSH providers) are eligible to receive Indiana Medicaid Disproportionate Share (state DSH) payments. The amount of these additional state DSH funds is dependent on regulatory approval by agencies of the federal and state governments and is determined by the level, extent, and cost of uncompensated care (as defined) and various other factors. State DSH payments are paid according to the fiscal year of the state, which ends on June 30 of each year, and are based on the cost of uncompensated care provided by the DSH providers during their respective fiscal year ended during the state fiscal year.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, participation requirements, reimbursement for patient services, Medicare and Medicaid fraud and abuse, and security, privacy, and standards of health information. Government activity has continued with respect to investigations and allegations concerning possible violations so fraud and abuse statutes and non-compliance with regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, significant repayments for patient services previously billed, and disruptions or delays in processing administrative transactions, including the adjudication of claims and payment. In the opinion of management, there are no known regulatory inquiries that are expected to have a material adverse effect on the financial statements of Goshen Health; however, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or un-asserted at this time.

The ACA and its associated legislation are designed, in part, to expand access to coverage to substantively all U.S. citizens through a combination of states' expansion of their Medicaid programs and the health insurance marketplace. For Indiana, CMS approved the Health Indiana Plan (HIP) 2.0, which was Indiana's response to expanding its Medicaid program. Changes to existing Medicare and Medicaid coverage and payments have also occurred as a result of this legislation. A body of regulations is generally required for legislative acts such as the ACA, which are often adopted over a period of years.