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May 11, 2017

Board of Directors
Jackson County Schneck Memorial Hospital and Affiliated Organizations
411 W. Tipton Street
Seymour, IN 47274

We have reviewed the audit report prepared by Blue & Co., LLC Independent Public Accountants, for the period January 1, 2016 to December 31, 2016. In our opinion, the audit report was prepared in accordance with the guidelines established by the State Board of Accounts. Per the Report of Independent Auditors, the financial statements included in the report present fairly the financial condition of the Jackson County Schneck Memorial Hospital and Affiliated Organizations, as of December 31, 2016 and the results of its operations for the period then ended, on the basis of accounting described in the report.

The audit report is filed with this letter in our office as a matter of public record.

Paul D. Joyce
Paul D. Joyce, CPA
State Examiner



SCHNECK

Better Healthcare Begins Here

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

CONSOLIDATED FINANCIAL STATEMENTS

AND

REQUIRED SUPPLEMENTARY INFORMATION

DECEMBER 31, 2016 AND 2015

CPAs / ADVISORS



**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

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DECEMBER 31, 2016 AND 2015

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REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Jackson County Schneck Memorial Hospital
and Affiliated Organizations
Seymour, Indiana

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Jackson County Schneck Memorial Hospital (d/b/a Schneck Medical Center) and Affiliated Organizations (collectively the "Medical Center"), component units of Jackson County, which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of operations and changes in net position, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated 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 and the *Uniform Compliance Guidelines for Audits of Hospitals and State and Local Governments by Authorized Independent Public Accountants*, issued by the Indiana State Board of Accounts. 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.

Board of Trustees
Jackson County Schneck Memorial Hospital
and Affiliated Organizations
Seymour, Indiana

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Medical Center as of December 31, 2016 and 2015, and the results of its operations, its changes in net position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis, and the schedules of pension plan information on pages i-ix and 52-53, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Blue & Co., LLC

Louisville, Kentucky
April 30, 2017

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2016 AND 2015

Management's discussion and analysis of the financial performance of Jackson County Schneck Memorial Hospital (d/b/a Schneck Medical Center) (the "Hospital") and Affiliated Organizations (collectively the "Medical Center") provides an overview of the Medical Center's financial activities and performance for the years ended December 31, 2016 and 2015. This discussion and analysis should be read in conjunction with the accompanying Medical Center's consolidated financial statements.

FINANCIAL HIGHLIGHTS

The Medical Center's net position increased \$23,084,121 from 2015 to 2016. During 2016, the Medical Center's total operating revenue decreased by 3.2% to \$275,329,888 with total operating expenses increasing by 1.6% to \$255,672,055.

- The Medical Center did not raise rates in 2016.
- During the period from 2012 to 2014, the Medical Center assumed ownership of the bed licenses of fifteen long term care facilities. The Medical Center entered into management agreements with the previous owners and/or management entities to manage the day-to-day operations of the facilities. The Medical Center also leases the buildings and premises from the prior owners. The first full year of operations was 2015 with all fifteen facilities included in the Medical Center's financial results. The amount included in income from operations attributable to the nursing facilities was \$10,971,694 in 2016 and \$14,221,972 in 2015.
- The Medical Center purchased the assets of an existing Primary Care Physician Practice and began operating the practice October 1, 2016. The acquisition increased patient volume, positively impacting operating revenue.
- In an effort to increase Medicaid reimbursement to hospitals, the State of Indiana implemented a Hospital Assessment Fee program in 2012. Indiana hospitals are assessed a fee which allows the state to access Federal funds allowing it to pay Medicaid patient claims at higher rates, not to exceed Medicare reimbursement. The Medical Center incurred Hospital Assessment Fees expense of \$3,027,163 in 2016 and \$2,807,078 in 2015.

The Medical Center's net position increased \$38,659,716 from 2014 to 2015 and included income from operations of \$32,739,211 and a restatement due to the adoption of GASB 68. During 2015, the Medical Center's total operating revenue increased by 10.9% to \$284,384,819 with total operating expenses increasing by 8.8% to \$251,645,608.

- The Medical Center raised rates by 2.5% in 2015.
 - During the period from 2012 to 2014, the Medical Center assumed ownership of the bed licenses of fifteen long term care facilities. The Medical Center entered into management agreements with the previous owners and/or management entities to manage the day-to-day operations of the facilities. The Medical Center also leases the buildings and premises from the prior owners. The first full year of operations was 2015 with all fifteen facilities included in the Medical Center's financial results. The
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JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

amount included in income from operations attributable to the nursing facilities was \$14,221,972 in 2015.

- The Medical Center was notified in August 2015 of favorable resolution to an appeal regarding Transitional Corridor Payments (TOPS) dating back to 2008. As a result, the Medical Center recognized \$7,537,575 of additional income in 2015.
- In an effort to increase Medicaid reimbursement to hospitals, the State of Indiana implemented a Hospital Assessment Fee program in 2012. Indiana hospitals are assessed a fee which allows the state to access Federal funds allowing it to pay Medicaid patient claims at higher rates, not to exceed Medicare reimbursement. The Medical Center incurred Hospital Assessment Fees expense of \$2,807,078 in 2015 and \$5,011,227 in 2014.

FINANCIAL STATEMENTS

The consolidated financial statements of the Medical Center present information about the Medical Center using financial reporting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information. The consolidated balance sheets include all of the Medical Center's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to the Medical Center's creditors (liabilities). It also provides the basis for compiling rate of return, evaluating the capital structure of the Medical Center and assessing the liquidity and financial flexibility of the Medical Center. All of the current and prior year's revenues and expenses are accounted for in the consolidated statements of operations and changes in net position. This statement measures the financial results of the Medical Center's operations and presents revenues earned and expenses incurred. The consolidated statements of cash flows provide information about the Medical Center's cash flows from operating activities, capital and related financing activities, and investing activities, plus provide information on the sources and uses of cash during both the current and prior year.

FINANCIAL ANALYSIS

The consolidated balance sheets and the consolidated statements of operations and changes in net position report information about the Medical Center's activities. These two statements report the net position of the Medical Center and its changes. Increases or decreases in the Medical Center's net position are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in economic conditions, population changes (including uninsured and medically indigent individuals and families), and new or changed governmental legislation should also be considered.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2016 AND 2015

CONDENSED FINANCIAL INFORMATION

A summary of the Medical Center's consolidated balance sheets as of December 31, 2016 and 2015 is presented below:

| | 2016 | 2015 | \$ Change | % Change |
|--|-----------------------|-----------------------|----------------------|----------|
| Assets | | | | |
| Current assets | \$ 124,841,858 | \$ 122,674,381 | \$ 2,167,477 | 1.8% |
| Capital assets | 75,211,492 | 73,735,888 | 1,475,604 | 2.0% |
| Other assets | 158,742,895 | 150,311,421 | 8,431,474 | 5.6% |
| Total assets | 358,796,245 | 346,721,690 | 12,074,555 | 3.5% |
| Deferred outflows | 4,196,697 | 33,168 | 4,163,529 | 12552.8% |
| Total assets and deferred outflows | <u>\$ 362,992,942</u> | <u>\$ 346,754,858</u> | <u>\$ 16,238,084</u> | 4.7% |
| Liabilities | | | | |
| Current liabilities | \$ 33,157,045 | \$ 34,073,442 | \$ (916,397) | -2.7% |
| Long-term liabilities | 34,687,281 | 40,517,071 | (5,829,790) | -14.4% |
| Total liabilities | 67,844,326 | 74,590,513 | (6,746,187) | -9.0% |
| Deferred inflows | 386,751 | 486,601 | (99,850) | 100.0% |
| Total liabilities and deferred inflows | 68,231,077 | 75,077,114 | (6,846,037) | -9.1% |
| Net position | | | | |
| Net investment in capital assets | 47,052,542 | 39,468,755 | 7,583,787 | 19.2% |
| Restricted expendable net position | 4,784,573 | 5,275,027 | (490,454) | -9.3% |
| Restricted nonexpendable net position | 310,215 | 308,534 | 1,681 | 0.5% |
| Unrestricted | 242,614,535 | 226,625,428 | 15,989,107 | 7.1% |
| Total net position | 294,761,865 | 271,677,744 | 23,084,121 | 8.5% |
| Total liabilities and net position | <u>\$ 362,992,942</u> | <u>\$ 346,754,858</u> | <u>\$ 16,238,084</u> | 4.7% |

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2016 AND 2015

A summary of the Medical Center's consolidated balance sheets as of December 31, 2015 and 2014 is presented below:

| | 2015 | 2014* | \$ Change | % Change |
|--|-----------------------|-----------------------|----------------------|----------|
| Assets | | | | |
| Current assets | \$ 122,674,381 | \$ 108,794,430 | \$ 13,879,951 | 12.8% |
| Capital assets | 73,735,888 | 75,846,274 | (2,110,386) | -2.8% |
| Other assets | 150,311,421 | 132,042,583 | 18,268,838 | 13.8% |
| Total assets | 346,721,690 | 316,683,287 | 30,038,403 | 9.5% |
| Deferred outflows | 33,168 | 1,739,188 | (1,706,020) | -98.1% |
| Total assets and deferred outflows | <u>\$ 346,754,858</u> | <u>\$ 318,422,475</u> | <u>\$ 28,332,383</u> | 8.9% |
| Liabilities | | | | |
| Current liabilities | \$ 34,073,442 | \$ 43,070,834 | \$ (8,997,392) | -20.9% |
| Long-term liabilities | 40,517,071 | 42,333,613 | (1,816,542) | -4.3% |
| Total liabilities | 74,590,513 | 85,404,447 | (10,813,934) | -12.7% |
| Deferred inflows | 486,601 | -0- | 486,601 | 100.0% |
| Total liabilities and deferred inflows | 75,077,114 | 85,404,447 | (10,327,333) | |
| Net position | | | | |
| Net investment in capital assets | 39,468,755 | 41,668,528 | (2,199,773) | -5.3% |
| Restricted expendable net position | 5,275,027 | 5,505,037 | (230,010) | -4.2% |
| Restricted nonexpendable net position | 308,534 | 333,340 | (24,806) | -7.4% |
| Unrestricted | 226,625,428 | 185,511,123 | 41,114,305 | 22.2% |
| Total net position | 271,677,744 | 233,018,028 | 38,659,716 | 16.6% |
| Total liabilities and net position | <u>\$ 346,754,858</u> | <u>\$ 318,422,475</u> | <u>\$ 28,332,383</u> | 8.9% |

*The 2014 balance sheet was not restated as it was not practical to determine the effects of GASB 68 as no evaluation was performed as of May 1, 2014.

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

CONDENSED FINANCIAL INFORMATION

A summary of the Medical Center's consolidated statements of operations and changes in net position for the years ended December 31, 2016 and 2015 is presented below:

| | 2016 | 2015 | \$ Change | % Change |
|---|----------------|----------------|----------------|----------|
| Operating revenues | | | | |
| Net patient service revenue | \$ 272,728,401 | \$ 282,563,218 | \$ (9,834,817) | -3.5% |
| Other revenue | 2,601,487 | 1,821,601 | 779,886 | 42.8% |
| Total operating revenues | 275,329,888 | 284,384,819 | (9,054,931) | -3.2% |
| Operating expenses | | | | |
| Salaries and benefits | 142,625,989 | 137,137,726 | 5,488,263 | 4.0% |
| Supplies and drugs | 34,827,374 | 33,633,994 | 1,193,380 | 3.5% |
| Depreciation and amortization | 8,282,640 | 8,639,376 | (356,736) | -4.1% |
| Other operating expenses | 69,936,052 | 72,234,512 | (2,298,460) | -3.2% |
| Total operating expenses | 255,672,055 | 251,645,608 | 4,026,447 | 1.6% |
| Income from operations | 19,657,833 | 32,739,211 | (13,081,378) | -40.0% |
| Nonoperating revenues (expenses) | 3,426,288 | (1,165,197) | 4,591,485 | 394.1% |
| Change in net position | \$ 23,084,121 | \$ 31,574,014 | \$ (8,489,893) | -26.9% |
| Restatement due to GASB 68 | \$ -0- | \$ 7,085,702 | \$ (7,085,702) | -100.0% |
| Net position, end of year | \$ 294,761,865 | \$ 271,677,744 | \$ 23,084,121 | 8.5% |

A summary of the Medical Center's consolidated statements of operations and changes in net position for the years ended December 31, 2015 and 2014 is presented below:

| | 2015 | 2014* | \$ Change | % Change |
|---|----------------|----------------|---------------|----------|
| Operating revenues | | | | |
| Net patient service revenue | \$ 282,563,218 | \$ 253,245,775 | \$ 29,317,443 | 11.6% |
| Other revenue | 1,821,601 | 3,294,281 | (1,472,680) | -44.7% |
| Total operating revenues | 284,384,819 | 256,540,056 | 27,844,763 | 10.9% |
| Operating expenses | | | | |
| Salaries and benefits | 137,137,726 | 125,612,129 | 11,525,597 | 9.2% |
| Supplies and drugs | 33,633,994 | 30,774,044 | 2,859,950 | 9.3% |
| Depreciation and amortization | 8,639,376 | 8,789,029 | (149,653) | -1.7% |
| Other operating expenses | 72,234,512 | 66,140,993 | 6,093,519 | 9.2% |
| Total operating expenses | 251,645,608 | 231,316,195 | 20,329,413 | 8.8% |
| Income from operations | 32,739,211 | 25,223,861 | 7,515,350 | 29.8% |
| Nonoperating revenues (expenses) | (1,165,197) | 624,295 | (1,789,492) | -286.6% |
| Change in net position | \$ 31,574,014 | \$ 25,848,156 | \$ 5,725,858 | 22.2% |
| Restatement due to GASB 68 | \$ 7,085,702 | \$ -0- | \$ 7,085,702 | 100.0% |
| Net position, end of year | \$ 271,677,744 | \$ 233,018,028 | \$ 38,659,716 | 16.6% |

*The 2014 statement of operations was not restated as it was not practical to determine the effects of GASB 68 as no evaluation was performed as of May 1, 2014.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2016 AND 2015

SOURCES OF REVENUE

The Medical Center derives the majority of its revenue from charges for patient care and related services. The Medical Center is reimbursed for services from a variety of sources including the Medicare and Medicaid programs, insurance carriers, managed care plans, and patients. The Medical Center has established payment arrangements with Medicare, Medicaid, and various commercial insurance carriers. Services provided under those arrangements are paid at predetermined rates and/or reimbursable cost as defined. Provisions have been made in the consolidated financial statements for contractual adjustments representing the difference between the standard charges for services and the actual or estimated payment.

The Medical Center's percentages of gross revenue by payor for 2016, 2015, and 2014 are as follows:

| <u>Payor Mix</u> | <u>2016</u> | <u>2015</u> | <u>2014</u> |
|--------------------------|--------------|--------------|--------------|
| Medicare | 38 % | 39 % | 39 % |
| Medicaid | 28 | 26 | 24 |
| Blue Cross | 14 | 15 | 16 |
| SIHO* | 5 | 5 | 5 |
| Other third-party payors | 8 | 7 | 7 |
| Self-pay | 7 | 8 | 9 |
| Total | <u>100 %</u> | <u>100 %</u> | <u>100 %</u> |

*Southeastern Indiana Health Organization

OPERATING AND FINANCIAL PERFORMANCE

The Medical Center's financial performance from operations was positive in 2016, though lower in comparison to 2015. The same is true for the Medical Center's overall financial performance. A discussion of the highlights of 2016 operations and changes in activity is presented below:

Revenues

The Medical Center's net patient service revenues decreased by \$9,834,817 in 2016. Highlights of this change are as follows:

- There was no rate increase in 2016.
- Contractual adjustments as a percent of gross revenue increased in 2016 due to shifts in patient types and insurance payer mix.
- Upper Payment Limit (UPL) revenue relating to ownership of fifteen nursing home licenses decreased approximately \$6.4 million from 2015 to 2016. UPL revenue is reliant on each home's Medicaid days and per day rate.

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2016 AND 2015

- Patient volume increases were noted for births, emergency department visits, surgeries, laboratory tests, diagnostic imaging procedures, respiratory therapy, occupational therapy, and home health services. Patient volume decreases were noted in inpatient days, physical therapy, speech therapy, and hospice services.

Expenses

Total operating expenses increased by \$4,026,447 in 2016. Highlights of this change are as follows:

- Salary and benefits costs increased \$5,488,263. This was due to staffing needs, market wage adjustments for many positions, and the addition of a primary care practice and several specialty physicians.
- Purchased services expense decreased \$1,831,508 due primarily to purchased services relating to the fifteen long term care facilities.

The Medical Center's financial performance from operations improved in 2015 in comparison to 2014 and the Medical Center's overall financial performance improved from 2014 to 2015. A discussion of the highlights of 2015 operations and changes in activity is presented below:

Revenues

The Medical Center's net patient service revenues increased by \$29,317,443 in 2015. This is primarily due to additional revenue relating to ownership of the fifteen nursing home licenses, a 2.5% rate increase, and increases in laboratory volumes and emergency department visits as compared to the prior year. Highlights of revenue activity are as follows:

- An overall rate increase of 2.5% effective January 1, 2015 was implemented.
- Patient volume increases were noted for emergency department visits, laboratory tests, diagnostic imaging procedures, respiratory therapy, occupational therapy, speech therapy, home health and hospice services. Patient volume decreases were noted in births, inpatient days, surgeries, and physical therapy.

Expenses

Total operating expenses increased by \$20,329,413 in 2015. Highlights of this change are as follows:

- Salary and benefits costs increased \$11,525,597. This was due to staffing needs and wage costs due to the addition of several new physicians and labor costs relating to the fifteen long term care facilities, including four new facilities in 2014.
- Purchased services increased \$4,971,307 due to costs relating to the fifteen long term care facilities.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2016 AND 2015

FINANCIAL ANALYSIS – CASH FLOWS

The Medical Center's 2016 cash flows increased \$18,519,130 due primarily to positive cash inflows received for patient services and investment income, which exceeded cash outflows for cash paid to employees and vendors and purchases of capital assets. In addition, the Medical Center was able to increase investment activity in 2016.

The Medical Center's 2015 cash flows increased \$2,674,792 due primarily to positive cash inflows received for patient services and investment income, which exceeded cash outflows for cash paid to employees and vendors and purchases of capital assets.

Capital Assets

| | 2016 | 2015 | \$Change | %Change |
|-------------------------------|----------------------|----------------------|---------------------|-------------|
| Land and land improvements | \$ 12,436,637 | \$ 12,147,614 | \$ 289,023 | 2.4% |
| Leasehold improvements | 671,058 | 671,058 | -0- | 0.0% |
| Buildings | 87,948,639 | 86,982,502 | 966,137 | 1.1% |
| Equipment | 56,173,446 | 59,185,699 | (3,012,253) | -5.1% |
| Construction in progress | 4,522,214 | 1,147,873 | 3,374,341 | 294.0% |
| | <u>161,751,994</u> | <u>160,134,746</u> | <u>1,617,248</u> | <u>1.0%</u> |
| Less accumulated depreciation | 86,540,502 | 86,398,858 | 141,644 | 0.2% |
| Capital assets, net | <u>\$ 75,211,492</u> | <u>\$ 73,735,888</u> | <u>\$ 1,475,604</u> | <u>2.0%</u> |

Net capital assets increased in 2016 due to annual depreciation and the disposal of assets that have exhausted their useful lives being greater than capital expenditures.

| | 2015 | 2014 | \$Change | %Change |
|-------------------------------|----------------------|----------------------|-----------------------|--------------|
| Land and land improvements | \$ 12,147,614 | \$ 10,772,609 | \$ 1,375,005 | 12.8% |
| Leasehold improvements | 671,058 | 672,661 | (1,603) | -0.2% |
| Buildings | 86,982,502 | 84,989,080 | 1,993,422 | 2.3% |
| Equipment | 59,185,699 | 57,998,911 | 1,186,788 | 2.0% |
| Construction in progress | 1,147,873 | 883,098 | 264,775 | 30.0% |
| | <u>160,134,746</u> | <u>155,316,359</u> | <u>4,818,387</u> | <u>3.1%</u> |
| Less accumulated depreciation | 86,398,858 | 79,470,085 | 6,928,773 | 8.7% |
| Capital assets, net | <u>\$ 73,735,888</u> | <u>\$ 75,846,274</u> | <u>\$ (2,110,386)</u> | <u>-2.8%</u> |

Net capital assets decreased in 2015 due to annual depreciation and the disposal of assets that have exhausted their useful lives being greater than capital expenditures.

See additional information on capital assets in the notes to the consolidated financial statements in footnote number 5.

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2016 AND 2015

Long-Term Debt

At December 31, 2016, the Medical Center had long-term debt (including current portion) of \$28,158,950, which is comprised of revenue bonds outstanding.

At December 31, 2015, the Medical Center had long-term debt (including current portion) of \$34,267,133. Which is comprised of revenue bonds outstanding.

ECONOMIC FACTORS AND 2017 BUDGET

The Medical Center's Board and management considered many factors when establishing the 2017 budget. Included was the status of the economy, which takes into consideration market factors and other environmental factors such as the following items:

- Advances in medical equipment and information systems technology and the need to replace obsolete equipment
- Decreasing reimbursement from governmental and commercial insurance payors
- Increasing costs of supplies and services
- Nationwide workforce shortages in nursing and other healthcare specialist positions
- Increasing awareness and expectations from the public on the quality of services
- Increasing patient sensitivity to amount charged for services provided
- Increased competition from niche providers
- Size, composition, and needs of the Medical Center's physician medical staff

CONTACTING THE MEDICAL CENTER

This report is designed to provide our citizens, customers and creditors with a general overview of the Medical Center's finances. These consolidated financial statements include the activities of the Hospital, Jackson County Schneck Memorial Hospital Foundation (the "Foundation"), Jackson Medical Building, LLC, and Health Development Corporation and Affiliated Organization ("HDC"). Separately-issued audited financial statements are available for both HDC and the Foundation. If you have questions about this report or need additional information, contact Deborah Mann, Vice President of Fiscal Services at 812-522-0171.

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**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2016 AND 2015

| | 2016 | 2015 |
|---|----------------|----------------|
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | \$ 69,096,172 | \$ 69,337,240 |
| Investments | 8,411,773 | 8,342,972 |
| Patient accounts receivable, net of estimated uncollectibles of \$26,829,458 in 2016 and \$24,612,418 in 2015 | 28,574,485 | 28,209,592 |
| Inventories | 4,129,678 | 4,244,238 |
| Prepaid expenses and other current assets | 11,809,785 | 9,351,514 |
| Estimated third-party payor settlements | 384,109 | 687,937 |
| Physician recruitment guarantees, current portion | 110,000 | 334,584 |
| Other assets, current portion | 499,629 | 297,839 |
| Current portion of assets whose use is limited | 1,826,227 | 1,868,465 |
| Total current assets | 124,841,858 | 122,674,381 |
| Assets whose use is limited, net of amount required to meet current obligations | 145,166,964 | 133,404,741 |
| Capital assets, net | 75,211,492 | 73,735,888 |
| Net pension asset | 5,852,824 | 10,355,225 |
| Other long-term assets | | |
| Physician recruitment guarantees, net of current portion | -0- | 110,000 |
| Other assets, net of current portion | 7,723,107 | 6,441,455 |
| Total other long-term assets | 7,723,107 | 6,551,455 |
| Total assets | 358,796,245 | 346,721,690 |
| Deferred outflows | | |
| Pension deferred outflows | 4,196,697 | 33,168 |
| Total deferred outflows | 4,196,697 | 33,168 |
| Total assets and deferred outflows | \$ 362,992,942 | \$ 346,754,858 |

See accompanying notes to consolidated financial statements.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2016 AND 2015

LIABILITIES AND NET POSITION

| | 2016 | 2015 |
|--|----------------|----------------|
| Current liabilities | | |
| Accounts payable | \$ 21,208,004 | \$ 21,621,831 |
| Accrued personnel costs | 9,961,117 | 10,198,703 |
| Accrued expenses | 246,573 | 352,922 |
| Physician recruitment guarantees, current portion | 110,000 | 334,584 |
| Current portion of long-term debt | 1,631,351 | 1,565,402 |
| Total current liabilities | 33,157,045 | 34,073,442 |
| Long-term liabilities | | |
| Long-term debt, net of current portion | 26,527,599 | 32,701,731 |
| Deferred compensation liabilities | 8,159,682 | 7,705,340 |
| Physician recruitment guarantees, net of current portion | -0- | 110,000 |
| Total long-term liabilities | 34,687,281 | 40,517,071 |
| Pension deferred inflows | 386,751 | 486,601 |
| Total liabilities and deferred inflows | 68,231,077 | 75,077,114 |
| Net position | | |
| Net investment in capital assets | 47,052,542 | 39,468,755 |
| Restricted | | |
| Expendable for debt service | 3,102,106 | 3,732,156 |
| Expendable for donor-restricted purposes | 1,682,467 | 1,542,871 |
| Nonexpendable perpetual trust | 310,215 | 308,534 |
| Unrestricted | 242,614,535 | 226,625,428 |
| Total net position | 294,761,865 | 271,677,744 |
| Total liabilities and net position | \$ 362,992,942 | \$ 346,754,858 |

See accompanying notes to consolidated financial statements.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION
YEARS ENDED DECEMBER 31, 2016 AND 2015

| | 2016 | 2015 |
|---|----------------|----------------|
| Operating revenues | | |
| Net patient service revenue | \$ 272,728,401 | \$ 282,563,218 |
| Other revenue | 2,601,487 | 1,821,601 |
| Total operating revenues | 275,329,888 | 284,384,819 |
| Operating expenses | | |
| Salaries and wages | 128,852,488 | 124,178,835 |
| Employee benefits and payroll taxes | 13,773,501 | 12,958,891 |
| Professional medical fees | 1,772,448 | 1,768,900 |
| Medical supplies | 14,655,221 | 13,802,036 |
| Other supplies | 8,564,185 | 8,572,058 |
| Drugs | 11,607,968 | 11,259,900 |
| Purchased services | 29,356,940 | 31,188,448 |
| Utilities | 4,631,186 | 4,706,194 |
| Insurance | 2,981,683 | 3,567,117 |
| Depreciation and amortization | 8,282,640 | 8,639,376 |
| Rent | 19,842,007 | 19,664,451 |
| Hospital assessment fee | 3,027,163 | 2,807,078 |
| Other operating expenses | 8,324,625 | 8,532,324 |
| Total operating expenses | 255,672,055 | 251,645,608 |
| Income from operations | 19,657,833 | 32,739,211 |
| Nonoperating revenues (expenses) | 3,426,288 | (1,165,197) |
| Change in net position | 23,084,121 | 31,574,014 |
| Net position, beginning of year as previously reported | 271,677,744 | 233,018,028 |
| Restatement due to adoption of GASB 68 | -0- | 7,085,702 |
| Net position, beginning of year | 271,677,744 | 240,103,730 |
| Net position, end of year | \$ 294,761,865 | \$ 271,677,744 |

See accompanying notes to consolidated financial statements.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2016 AND 2015

| | 2016 | 2015 |
|--|----------------|----------------|
| Operating activities | | |
| Cash received for patient services | \$ 272,667,336 | \$ 275,737,251 |
| Cash paid to/for employees | (142,170,211) | (140,859,980) |
| Cash paid to vendors and suppliers | (107,819,490) | (104,488,845) |
| Other receipts, net | 2,601,487 | 1,821,601 |
| Net cash flows from operating activities | 25,279,122 | 32,210,027 |
| Noncapital financing activities | | |
| Noncapital contributions | 747,405 | 537,941 |
| Capital and related financing activities | | |
| Principal payments on long-term debt | (6,035,000) | (1,619,390) |
| Interest paid | (1,088,173) | (1,467,691) |
| Purchase of capital assets | (9,949,159) | (6,303,086) |
| Proceeds from sale of capital assets | 306,350 | -0- |
| Change in bond premiums | (73,183) | (30,411) |
| Change in deferred loss on bond refunding | -0- | 1,739,188 |
| (Gain) loss on disposal of capital assets | 79,242 | 10,543 |
| Net cash flows from capital and related financing activities | (16,759,923) | (7,670,847) |
| Investing activities | | |
| Investment income | 4,072,620 | 401,253 |
| Other nonoperating revenues (expenses) | (305,564) | (636,700) |
| Change in investments | (68,801) | 23,359 |
| Change in assets whose use is limited | 7,040,213 | (21,591,477) |
| Change in other assets | (1,485,942) | (598,764) |
| Net cash flows from investing activities | 9,252,526 | (22,402,329) |
| Net change in cash and cash equivalents | 18,519,130 | 2,674,792 |
| Cash and cash equivalents, beginning of year | 119,690,516 | 117,015,724 |
| Cash and cash equivalents, end of year | \$ 138,209,646 | \$ 119,690,516 |
| Reconciliation of cash and cash equivalents to the balance sheets | | |
| Cash and cash equivalents in current assets | \$ 69,096,172 | \$ 69,337,240 |
| Cash and cash equivalents in assets whose use is limited | 69,113,474 | 50,353,276 |
| Total cash and cash equivalents | \$ 138,209,646 | \$ 119,690,516 |

See accompanying notes to consolidated financial statements.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2016 AND 2015

| | 2016 | 2015 |
|--|---------------|---------------|
| Reconciliation of income from operations to net cash and cash equivalents from operating activities | | |
| Income from operations | \$ 19,657,833 | \$ 32,739,211 |
| Adjustments to reconcile income from operations to net cash flows from operating activities | | |
| Depreciation | 8,280,140 | 8,632,199 |
| Amortization | 2,500 | 7,177 |
| Provision for bad debts | 16,437,849 | 15,998,803 |
| Changes in operating assets and liabilities | | |
| Patient accounts receivable | (16,802,742) | (16,581,433) |
| Inventories | 114,560 | 10,825 |
| Prepaid expenses and other current assets | (2,458,271) | 4,020,675 |
| Net pension asset | 4,502,401 | (3,269,523) |
| Pension deferred outflows | (4,163,529) | (33,168) |
| Accounts payable | (606,004) | (2,580,534) |
| Accrued personnel costs | (237,586) | (714,621) |
| Accrued expenses | (106,349) | (71,305) |
| Estimated third-party payor settlements | 303,828 | (6,243,337) |
| Pension deferred inflows | (99,850) | 486,601 |
| Deferred compensation liabilities | 454,342 | (191,543) |
| Net cash flows from operating activities | \$ 25,279,122 | \$ 32,210,027 |
| Supplemental disclosures of noncash operating and capital and related financing activities | | |
| Property and equipment acquired included in accounts payable | \$ 192,177 | \$ 229,270 |

See accompanying notes to consolidated financial statements.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Jackson County Schneck Memorial Hospital (d/b/a Schneck Medical Center) (the "Hospital") is a not-for-profit, acute care hospital located in Seymour, Indiana. The Hospital is county owned and operates under the Indiana County Hospital Law, Indiana Code 16-22. The Hospital is organized for the purpose of providing healthcare services to the residents of Jackson County and the surrounding area. The Hospital's primary sources of support are from patient revenues and other ancillary income. Patient revenues include funds received from Medicare, state agencies, insurance companies, and the patients themselves.

Pursuant to the provision of long-term care, the Hospital owns the operations of fifteen long term care facilities by way of an arrangement with the managers of the facilities. These facilities provide inpatient and therapy services. Generally, gross revenues from the operation of the facilities are the property of the Hospital and the Hospital is responsible for the associated operating expenses and working capital requirements. While the management and related lease agreements are in effect, the performance of all activities of the managers shall be on behalf of the Hospital and the Hospital retains the authority for the operation of the facilities.

The Hospital has entered into lease agreements with the long-term care facilities, collectively referred to as the Lessors, to lease the facilities. Concurrently, the Hospital entered into agreements with the long-term care facilities to manage the above leased facilities, collectively referred to as the Managers. As part of the agreements, the Hospital will pay the Managers a management fee to continue managing the facilities on behalf of the Hospital in accordance with the terms of the agreements. These management fees consist of base management fees, subordinated management fees, and quarterly incentive payments. The agreements' initial terms expire at various times beginning in 2016 and beyond. The terms of these agreements may be renewed at the end of each term for an additional period of two years. All parties involved can terminate the agreement without cause with 90 days written notice. Other current assets and liabilities include certain reimbursement receivables, accrued fees and expenses, and working capital balances related to the long-term care facilities.

Health Development Corporation ("HDC") is a not-for-profit corporation located in Seymour, Indiana. HDC was organized to operate exclusively for the benefit of, to perform the functions of, and to carry out the purposes of the Hospital by recruiting physicians to the surrounding area and by providing medical education programs to the medical and Hospital staff. HDC's primary sources of revenue are from service fees charged to the Hospital.

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

HDC's consolidated financial statements at December 31, 2016 and 2015, include the accounts of Coordinated Health, LLC (the "Clinic"). The Clinic is wholly-owned by HDC and began operations in 2002. The Clinic was organized to operate exclusively for the benefit of HDC and the purposes for which HDC is organized and operated, including the promotion and support of the health of Jackson County, Indiana residents and residents of surrounding communities. Currently, the Clinic operates three healthcare facilities located in North Vernon, Salem, and Scottsburg, Indiana. The Clinic's primary source of revenue is from patient services.

The Jackson County Schneck Memorial Hospital Foundation, Inc. (d/b/a Schneck Medical Center Foundation) (the "Foundation") is a not-for-profit organization located in Seymour, Indiana. The Foundation operates for the benefit of the Hospital. The Foundation's main sources of revenue are earnings on investments, donations received, and rental income.

Jackson Medical Building, LLC ("JMB") is a limited liability company that is wholly owned by the Hospital. JMB was organized to own and operate a medical office building located on the Hospital's campus. JMB's primary source of revenue is from rental income.

The significant accounting policies followed by the Hospital, HDC, JMB, and the Foundation (collectively the "Medical Center") in the preparation of the consolidated financial statements are summarized below:

Reporting Entity and Consolidation Policy

The accompanying consolidated financial statements include the accounts of the Hospital, HDC, the Clinic, JMB, and the Foundation. The Board of County Commissioners of Jackson County appoints the governing Board of Trustees of the Hospital, and a financial benefit/burden relationship exists between the Hospital and the Jackson County government. For these reasons, the Hospital is considered a component unit of Jackson County. Similarly, due to their organized purposes, HDC, the Clinic, JMB, and the Foundation are considered blended component units of the Hospital. Intercompany transactions and balances have been eliminated in consolidation. The separate audited financial statements of HDC (including the Clinic) and the Foundation may be obtained by contacting the Hospital as follows:

Schneck Medical Center
411 W. Tipton Street
P.O. Box 2349
Seymour, IN 47274

Management's Estimates

Management uses estimates and assumptions in preparing the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, if any, and the reported revenues and expenses. Actual results could vary from the estimates that were used.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

New Accounting Standards

During 2016, the Medical Center implemented GASB Statement No. 72 *Fair Value Measurement and Application*. This statement addressed accounting and financial reporting issues related to fair value measurements. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. There was no impact to these financial statement disclosures as a result of adoption of this standard as these disclosures have been provided historically.

During 2016, the Medical Center implemented GASB Statement No. 76 *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addressed the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. There was no impact to these financial statement disclosures as a result of adoption of this standard.

Measurement Focus and Basis of Accounting

The financial statements are reported using the economic resources measurement focus and on the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Pensions

For purposes of measuring the net pension asset, deferred outflows, and deferred inflows of resources related to pensions, pension expense, information about the fiduciary net position of the Jackson County Schneck Memorial Hospital Employees' Pension Plan (the "Plan"), and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by the Plan. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Risk Management

The Medical Center is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years. The Medical Center is insured for medical malpractice claims and judgments.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

Cash and Cash Equivalents

Cash and cash equivalents as reported on the consolidated balance sheets include petty cash and other cash on hand amounts, checking accounts, and savings accounts that are readily available for use. Cash and cash equivalents as reported on the consolidated statements of cash flows include investments in highly liquid assets with maturity dates of 90 days or less when purchased.

Investments

Investments include certificates of deposit amounts maturing within one year of the dates of the consolidated balance sheets. Investments are recorded at cost, which approximates market value.

Patient Accounts Receivable and Net Patient Service Revenue

The Medical Center recognizes net patient service revenues on the accrual basis of accounting in the reporting period in which services are performed based on the current gross charge structure, less actual adjustments and estimated discounts for contractual allowances, principally for patients covered by Medicare, Medicaid, managed care, and other health plans. Gross patient service revenue is recorded in the accounting records using the established rates for the types of service provided to the patient. The Medical Center recognizes an estimated contractual allowance to reduce gross patient charges to the estimated net realizable amount for service rendered based upon previously agreed-to rates with a payor. The Medical Center utilizes the patient accounting system to calculate contractual allowances on a payor-by-payor basis based on the rates in effect for each primary third-party payor. Another factor that is considered and could further influence the level of the contractual reserves includes the status of accounts receivable balances as inpatient or outpatient. The Medical Center's management continually reviews the contractual estimation process to consider and incorporate updated laws and regulations and the frequent changes in managed care contractual terms that result from contract negotiations and renewals.

Payors include federal and state agencies, including Medicare and Medicaid, managed care health plans, commercial insurance companies, and patients. These third-party payors provide payments to the Medical Center at amounts different from its established rates based on negotiated reimbursement agreements. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and fee schedule payments. Retroactive adjustments under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Allowance for Doubtful Accounts

Accounts receivable are reduced by an allowance for doubtful accounts based on the Medical Center's evaluation of its major payor sources of revenue, the aging of the accounts, historical losses, current economic conditions, and other factors unique to the service area and the healthcare

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

industry. Management regularly reviews data about the major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party payor coverage, the Medical Center analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulty that make the realization of amounts due unlikely). For receivables associated with self-pay payments, which includes both patients without insurance and patient with deductible and copayment balances due for which third-party coverage exists for part of the bill, the Medical Center records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts. The December 31, 2016 and 2015 allowance for doubtful accounts balances were comprised of the following:

| | <u>2016</u> | <u>2015</u> |
|--|----------------------|----------------------|
| Reserve for third-party payor balances | \$ 4,898,396 | \$ 4,673,862 |
| Reserve for self-pay balances | <u>21,931,062</u> | <u>19,938,556</u> |
| Total allowance for doubtful accounts | <u>\$ 26,829,458</u> | <u>\$ 24,612,418</u> |

Inventories

Inventories consist of medical supplies, pharmaceuticals, and office supplies and are valued at the lower of cost or market, with cost being determined on the first-in, first-out (FIFO) method.

Assets Whose Use is Limited

Investments in certificates of deposit are reported in the consolidated financial statements at cost, which approximates fair value.

Assets whose use is limited include assets set aside by the respective Boards for future capital improvements, over which the Boards retain control and may at their discretion subsequently use for other purposes; assets held by trustees under indenture agreements; assets that have been restricted by donors for specific purposes; and amounts that have been set aside as part of deferred compensation plans.

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair market value in the consolidated balance sheets. Investment income

JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL AND AFFILIATED ORGANIZATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

or loss, including realized gains and losses on investments and assets whose use is limited, net change in the market value of assets whose use is limited, interest, and dividends, is included in nonoperating revenues (expenses) when earned.

Capital Assets

The Medical Center's capital assets are reported at historical cost and include expenditures for additions and repairs which substantially increase the useful lives of capital assets. Maintenance, repairs, and minor improvements are expensed as incurred. Contributed capital assets are reported at their estimated fair value at the time of their donation. All capital assets other than land and construction in progress are depreciated using the straight-line method of depreciation over their estimated useful lives based upon the American Hospital Association Guide for Estimated Useful Lives for Fixed Assets.

Costs of Borrowing

Except for capital assets acquired through gifts, contributions, or capital grants, interest costs on borrowed funds during the period of construction of capital assets are capitalized as a component of the cost of acquiring those assets. For the years ended December 31, 2016 and 2015, the Medical Center capitalized interest costs of \$108,344 and \$54,523, respectively.

Classification of Net Position

The net position of the Medical Center is classified in four components. (1) *Net investment in capital assets* consists of capital assets net of accumulated depreciation plus deferred outflows related to losses on bond refunding which are reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. (2) *Restricted expendable net position* includes assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Medical Center, including amounts deposited with trustees as required by revenue bond indentures. (3) *Restricted nonexpendable net position* includes the principal portion of permanent endowments and non-controlling interests owned by external investors. (4) *Unrestricted net position* is the remaining net position that does not meet the definition of *net investment in capital assets* or *restricted*. When both restricted and unrestricted resources are available for use, the Medical Center's policy is to use restricted resources first, then unrestricted resources as they are needed.

Consolidated Statements of Operations and Changes in Net Position

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenues and expenses. Peripheral and incidental transactions are reported as nonoperating revenues (expenses). Nonoperating revenues (expenses) which are excluded from income from operations include investment income, contributions received, restricted expenditures, and the net change in the market value of assets whose use is limited.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

Advertising and Marketing Costs

Advertising and marketing costs are charged to operations when incurred. Advertising and marketing costs charged to operations were \$914,426 and \$939,258 for the years ended December 31, 2016 and 2015, respectively.

Charity Care

The Medical Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Amounts determined to qualify as charity care are reported as reductions of net patient service revenue.

Income Taxes

The Hospital has been granted exemption from taxation as a not-for-profit organization by the Internal Revenue Service under Section 115, and in 2005 was also granted exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code for purposes of maintaining a 403b deferred compensation plan. Therefore, no provision for income taxes has been provided in the consolidated statements of operations and changes in net position. HDC and the Foundation are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. As such HDC and the Foundation are generally exempt from income taxes. However, HDC and the Foundation are required to file Federal Form 990 – Return of Organization Exempt from Income Tax which is an informational return only. The Clinic and JMB are both organized as a single-member Limited Liability Company (LLC). As of December 31, 2016, the 2012 - 2016 income tax years are still open for tax examinations for both the Clinic and JMB. HDC is the sole member of the Clinic, and the Hospital is the sole member of JMB. As such, the Clinic and JMB are not required to file separate State or Federal tax returns. For tax reporting purposes, all activities of the Clinic are required to be filed with the activities of HDC, and all activities of JMB are required to be filed with the activities of the Hospital.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by each entity comprising the Medical Center and recognize a tax liability if any Medical Center entity has taken an uncertain tax position that more likely than not would not be sustained upon examination by various federal and state taxing authorities. Management has analyzed the tax positions taken by each entity of the Medical Center, and has concluded that as of December 31, 2016 and 2015, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying consolidated financial statements. Each entity of the Medical Center is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

Grants and Contributions

From time to time, the Medical Center receives grants as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues.

Physician Recruitment Guarantees

GASB Statement No. 62 requires the Medical Center to report a liability for physician revenue guarantees on its consolidated balance sheets at fair value and amortize that liability and corresponding intangible asset over the income guarantee period. As cash payments are made to the physicians in accordance with the terms of the income guarantees, the Medical Center records a note receivable from each participating physician. These notes are either paid back to the Medical Center or are forgiven by the Medical Center in accordance with the terms of each separate income guarantee agreement. As of December 31, 2016 and 2015, the Medical Center had matching assets and liabilities relating to physician guarantees of \$110,000 and \$444,584, respectively.

Subsequent Events

The Medical Center has evaluated events or transactions occurring subsequent to the consolidated balance sheet date for recognition and disclosure in the accompanying consolidated financial statements through the date the consolidated financial statements are issued, which is April 30, 2017.

Reclassifications

Certain 2015 amounts have been reclassified to provide for consistency with reporting of 2016 information. These reclassifications had a \$1 effect on the previously reported change in net position and total net position.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

2. DEPOSITS AND INVESTMENTS

Deposits and investments are comprised of the following at December 31, 2016 and 2015:

| | 2016 | 2015 |
|--|----------------|----------------|
| Carrying amount | | |
| Cash and cash equivalents | \$ 138,209,646 | \$ 119,690,516 |
| Certificates of deposit | 17,003,892 | 17,237,930 |
| Brokered certificates of deposit | 149,288 | -0- |
| Mutual funds | 62,768,201 | 52,644,395 |
| Corporate bonds | 36,577 | 45,024 |
| Money market mutual funds | 4,692,955 | 21,844,596 |
| Perpetual trust | 310,215 | 308,534 |
| Interest receivable | 19,687 | 15,845 |
| Fixed income guaranteed option | 193,448 | 196,247 |
| Common stocks | 1,117,227 | 970,331 |
| Total | \$ 224,501,136 | \$ 212,953,418 |
| | 2016 | 2015 |
| Included in the consolidated balance sheet captions: | | |
| Cash and cash equivalents | \$ 69,096,172 | \$ 69,337,240 |
| Investments | 8,411,773 | 8,342,972 |
| Assets whose use is limited | 146,993,191 | 135,273,206 |
| Total | \$ 224,501,136 | \$ 212,953,418 |

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that, in the event of a bank failure, the Medical Center's deposits may not be returned to it. The Medical Center does not have a deposit policy for custodial credit risk. Deposits with financial institutions in the State of Indiana at year-end were entirely insured by the Federal Depository Insurance Corporation ("FDIC") or by the Indiana Public Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying institution.

Investments are carried at fair value or cost which approximates fair value. Net realized gains and losses on security transactions are determined on the specific identification cost basis. As of December 31, 2016 and 2015, the Medical Center had the following investments and maturities,

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all of which were held in the Medical Center's name by custodial banks or investment companies that are agents of the Medical Center:

| December 31, 2016 | | | | | |
|-------------------------|----------------------------------|---------------|-----------|-----------------|--------|
| Carrying Amount | Investment Maturities (in years) | | | | |
| | Less than 1 | 1 - 5 | 6 - 10 | More than 10 | |
| Certificates of deposit | \$ 17,153,180 | \$ 17,153,180 | \$ -0- | \$ -0- | \$ -0- |
| Corporate bonds | 36,577 | 16,486 | 20,091 | -0- | -0- |
| Total | \$ 17,189,757 | \$ 17,169,666 | \$ 20,091 | \$ -0- | \$ -0- |

| December 31, 2015 | | | | | |
|-------------------------|----------------------------------|---------------|-----------|-----------------|--------|
| Carrying Amount | Investment Maturities (in years) | | | | |
| | Less than 1 | 1 - 5 | 6 - 10 | More than 10 | |
| Certificates of deposit | \$ 17,237,930 | \$ 17,237,930 | \$ -0- | \$ -0- | \$ -0- |
| Corporate bonds | 45,024 | 4,040 | 40,984 | -0- | -0- |
| Total | \$ 17,282,954 | \$ 17,241,970 | \$ 40,984 | \$ -0- | \$ -0- |

Interest Rate Risk

Interest risk rate is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates.

The Medical Center does have formal investment policies that limit investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates. The Hospital's current investment policy limits investments with maturities of two years or longer to no more than 60 percent of total investments. The Foundation's investment policy prohibits the purchase of fixed income securities with original maturities of more than 10 years, unless the securities are part of a fund portfolio which has an average maturity of not greater than 10 years.

Credit Risk – Investments

Credit risk is the risk that, in the event of a failure of a financial institution, the Medical Center would not be able to recover deposits, the value of its investments, or collateral securities that are in the possession of an outside party.

Statutes authorize the Medical Center to invest in interest-bearing deposit accounts, passbook savings accounts, certificates of deposit, money market deposit accounts, repurchase agreements, mutual funds, pooled fund investments, and securities backed by the full faith and

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credit of the United States Treasury. The statutes require that repurchase agreements be fully collateralized by U.S. Government or U.S. Government Agency obligations.

| Investment Type | Credit Rating Moody's | Fair Value 2016 | Fair Value 2015 |
|-----------------|--------------------------|--------------------|--------------------|
| Corporate bonds | A1 | \$ 2,084 | \$ 2,320 |
| Corporate bonds | A2 | 4,216 | 11,840 |
| Corporate bonds | A3 | 10,337 | 8,515 |
| Corporate bonds | Aaa | 2,059 | 2,165 |
| Corporate bonds | Aa2 | 4,195 | 4,040 |
| Corporate bonds | Ba1 | 4,314 | -0- |
| Corporate bonds | Baa1 | 3,145 | 4,360 |
| Corporate bonds | Baa2 | 4,197 | 5,269 |
| Corporate bonds | Baa3 | 2,030 | 6,515 |
| | | <u>\$ 36,577</u> | <u>\$ 45,024</u> |

Concentration of Credit Risk

The Hospital places no limit on the amount it may invest in any one issuer. The Foundation limits investments in securities of a single issuer to 10 percent of the portfolio's total market value. This limitation does not include U.S. Government Securities. The Medical Center maintains its investments, which at times may exceed federally insured limits. The Medical Center has not experienced any losses in such accounts. The Medical Center believes that it is not exposed to any significant credit risk on investments.

Fair Value Measurements and Disclosures

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active market for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Medical Center has the ability to access.
- Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation

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or other means. If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2016 and 2015.

- *Brokered Certificates of Deposit*: Determined by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the credit-worthiness of the issuer.
 - *Mutual funds*: Valued at the daily closing price as reported by the fund. Mutual funds held by the Medical Center are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value and to transact at that price. The mutual funds held by the Medical Center are deemed to be actively traded.
 - *Corporate bonds*: Valued using pricing models maximizing the use of observable inputs for similar securities. This includes basing value on yields currently available on comparable securities of issuers with similar credit ratings.
 - *Perpetual trust*: Valued at fair value as reported by the trustee, which represents the Medical Center's *pro rata* interest in the net position of the trust, substantially all of which are valued on a mark-to-market basis.
 - *Fixed income guaranteed option*: Guaranteed investment contracts are valued at fair value by the insurance company by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the creditworthiness of the issuer. Since the participants transact at contract value, fair value is determined annually for financial statement reporting purposes only. In determining the reasonableness of the methodology the Finance Committee evaluates a variety of factors including review of existing contracts, economic conditions, industry and market developments, and overall credit ratings. Certain unobservable inputs are assessed through review of contract terms (for example, duration or payout date) while others are substantiated utilizing available market data (for example, swap curve rate).
 - *Common stocks*: Valued at the closing price reported on the active market on which the individual securities are traded.
-

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- *Deferred compensation:* Value based on the underlying investments.
- *Money market mutual funds:* Generally transact subscription and redemption activity at a \$1 stable net asset value (NAV) however, on a daily basis the funds are valued at their daily NAV calculated using the amortized cost of the securities held in the fund.

The following table set forth by level, within the hierarchy, the Medical Center's assets measured at fair value on a recurring basis as of December 31, 2016 are as follows:

| | Level 1 | Level 2 | Level 3 | Total |
|-------------------|-----------|----------|---------|-----------|
| <u>Assets</u> | | | | |
| Corporate bonds | | | | |
| Financial | \$ -0- | \$ 7,287 | \$ -0- | \$ 7,287 |
| Healthcare | -0- | 8,340 | -0- | 8,340 |
| Basic materials | -0- | 6,148 | -0- | 6,148 |
| Consumer goods | -0- | 3,144 | -0- | 3,144 |
| Services | -0- | 11,658 | -0- | 11,658 |
| | -0- | 36,577 | -0- | 36,577 |
| Common stocks | | | | |
| Basic materials | 130,286 | -0- | -0- | 130,286 |
| Consumer goods | 157,946 | -0- | -0- | 157,946 |
| Consumer services | 125,169 | -0- | -0- | 125,169 |
| Financials | 227,608 | -0- | -0- | 227,608 |
| Healthcare | 155,850 | -0- | -0- | 155,850 |
| Industrials | 97,660 | -0- | -0- | 97,660 |
| Utilities | 2,681 | -0- | -0- | 2,681 |
| Technology | 220,027 | -0- | -0- | 220,027 |
| | 1,117,227 | -0- | -0- | 1,117,227 |

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| | | | | |
|-----------------------------------|---------------|----------------|------------|----------------|
| Mutual funds | | | | |
| Large cap value | 4,827,613 | -0- | -0- | 4,827,613 |
| Large cap blend | 11,530,359 | -0- | -0- | 11,530,359 |
| Large cap growth | 7,152,454 | -0- | -0- | 7,152,454 |
| Mid cap value | 28,440 | -0- | -0- | 28,440 |
| Mid cap growth | 3,416,481 | -0- | -0- | 3,416,481 |
| Mid cap blend | 9,062,963 | -0- | -0- | 9,062,963 |
| Small cap growth | 1,752,573 | -0- | -0- | 1,752,573 |
| Small cap blend | 239,299 | -0- | -0- | 239,299 |
| Small cap value | 655,369 | -0- | -0- | 655,369 |
| Foreign small growth | 2,305,354 | -0- | -0- | 2,305,354 |
| Foreign large value | 1,614,594 | -0- | -0- | 1,614,594 |
| Foreign large blend | 4,790,071 | -0- | -0- | 4,790,071 |
| Foreign large growth | 1,843,433 | -0- | -0- | 1,843,433 |
| World stock | 3,985,343 | -0- | -0- | 3,985,343 |
| Diversified emerging markets | 1,587,300 | -0- | -0- | 1,587,300 |
| Intermediate term bond | 3,850,872 | -0- | -0- | 3,850,872 |
| Short term bond | 223,403 | -0- | -0- | 223,403 |
| Real estate | 24,313 | -0- | -0- | 24,313 |
| High yield bond | 337,795 | -0- | -0- | 337,795 |
| Intermediate government | 3,183,199 | -0- | -0- | 3,183,199 |
| Long government | 5,346 | -0- | -0- | 5,346 |
| Bank loan | 9,443 | -0- | -0- | 9,443 |
| Preferred stock | 13,443 | -0- | -0- | 13,443 |
| Inflation protected bond | 328,741 | -0- | -0- | 328,741 |
| | 62,768,201 | -0- | -0- | 62,768,201 |
| Brokered certificates of deposit | -0- | 149,288 | -0- | 149,288 |
| Money market mutual funds | -0- | 4,692,955 | -0- | 4,692,955 |
| Perpetual trust, held by trustee | -0- | -0- | 310,215 | 310,215 |
| Fixed income guaranteed option | -0- | 193,448 | -0- | 193,448 |
| Total assets at fair value | \$ 63,885,428 | \$ 5,072,268 | \$ 310,215 | 69,267,911 |
| Cash and cash equivalents | | | | 138,209,646 |
| Certificates of deposit | | | | 17,003,892 |
| Interest receivable | | | | 19,687 |
| Total deposits and investments | | | | \$ 224,501,136 |
| <u>Liabilities</u> | | | | |
| Deferred compensation liabilities | \$ -0- | \$ (8,159,682) | \$ -0- | \$ (8,159,682) |

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The following table set forth by level, within the hierarchy, the Medical Center's asset measured at fair value on a recurring basis as of December 31, 2015 are as follows:

| | Level 1 | Level 2 | Level 3 | Total |
|---------------------------|------------|------------|---------|------------|
| <u>Assets</u> | | | | |
| Corporate bonds | | | | |
| Financial | \$ -0- | \$ 12,759 | \$ -0- | \$ 12,759 |
| Energy | -0- | 4,195 | -0- | 4,195 |
| Healthcare | -0- | 3,175 | -0- | 3,175 |
| Basic materials | -0- | 2,040 | -0- | 2,040 |
| Consumer goods | -0- | 8,664 | -0- | 8,664 |
| Services | -0- | 14,191 | -0- | 14,191 |
| | -0- | 45,024 | -0- | 45,024 |
| Common stocks | | | | |
| Basic materials | 68,792 | -0- | -0- | 68,792 |
| Consumer goods | 110,427 | -0- | -0- | 110,427 |
| Natural resources | 12,606 | -0- | -0- | 12,606 |
| Consumer services | 144,474 | -0- | -0- | 144,474 |
| Financials | 238,127 | -0- | -0- | 238,127 |
| Healthcare | 156,639 | -0- | -0- | 156,639 |
| Industrials | 76,846 | -0- | -0- | 76,846 |
| Utilities | 13,189 | -0- | -0- | 13,189 |
| Technology | 149,231 | -0- | -0- | 149,231 |
| | 970,331 | -0- | -0- | 970,331 |
| Mutual funds | | | | |
| Large cap value | 6,745,662 | -0- | -0- | 6,745,662 |
| Large cap blend | 9,133,009 | -0- | -0- | 9,133,009 |
| Large cap growth | 7,667,711 | -0- | -0- | 7,667,711 |
| Mid cap growth | 2,495,638 | -0- | -0- | 2,495,638 |
| Mid cap blend | 5,138,246 | -0- | -0- | 5,138,246 |
| Small cap blend | 954,577 | -0- | -0- | 954,577 |
| Foreign small growth | 1,981,118 | -0- | -0- | 1,981,118 |
| Foreign large value | 192,264 | -0- | -0- | 192,264 |
| Foreign large blend | 7,057,186 | -0- | -0- | 7,057,186 |
| World stock | 4,993,311 | -0- | -0- | 4,993,311 |
| Intermediate term bond | 1,254,641 | -0- | -0- | 1,254,641 |
| Short term bond | 1,263,741 | -0- | -0- | 1,263,741 |
| Real Estate | 2,074,243 | -0- | -0- | 2,074,243 |
| High yield bond | 757,162 | -0- | -0- | 757,162 |
| Emerging markets | 935,886 | -0- | -0- | 935,886 |
| | 52,644,395 | -0- | -0- | 52,644,395 |
| Money market mutual funds | -0- | 21,844,596 | -0- | 21,844,596 |

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| | | | | |
|----------------------------------|----------------------|----------------------|-------------------|-----------------------|
| Perpetual trust, held by trustee | -0- | -0- | 308,534 | 308,534 |
| Fixed income guaranteed option | -0- | 196,247 | -0- | 196,247 |
| Total assets at fair value | <u>\$ 53,614,726</u> | <u>\$ 22,085,867</u> | <u>\$ 308,534</u> | 76,009,127 |
| Cash and cash equivalents | | | | 119,690,516 |
| Certificates of deposit | | | | 17,237,930 |
| Interest receivable | | | | 15,845 |
| Total deposits and investments | | | | <u>\$ 212,953,418</u> |

Liabilities

| | | | | |
|-----------------------------------|---------------|-----------------------|---------------|-----------------------|
| Deferred compensation liabilities | <u>\$ -0-</u> | <u>\$ (7,705,340)</u> | <u>\$ -0-</u> | <u>\$ (7,705,340)</u> |
|-----------------------------------|---------------|-----------------------|---------------|-----------------------|

The Medical Center's policy is to recognize transfers between levels as of the end of the reporting period. There were no significant transfers between levels 1, 2, and 3 during 2016 and 2015.

The following summary sets forth a summary of changes in the fair values of the Medical Center's Level 3 assets for the years ended December 31, 2016 and 2015:

| | 2016 | 2015 |
|--------------------------------|------------------------------------|------------------------------------|
| | Perpetual Trust Held by Trustee | Perpetual Trust Held by Trustee |
| | <u> </u> | <u> </u> |
| Balance, beginning of the year | \$ 308,534 | \$ 333,340 |
| Purchase of investments | -0- | -0- |
| Redemption | -0- | -0- |
| Change in investment value | 1,681 | (24,806) |
| Balance, end of year | <u>\$ 310,215</u> | <u>\$ 308,534</u> |

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3. PATIENT ACCOUNTS RECEIVABLE

Patient accounts receivable reported as current assets at December 31, 2016 and 2015, consist of the following:

| | 2016 | 2015 |
|--|---------------|---------------|
| Medicare | \$ 20,763,583 | \$ 18,517,929 |
| Medicaid | 15,461,994 | 13,703,492 |
| Blue Cross | 6,420,287 | 6,686,905 |
| Other insurance carriers | 12,912,219 | 13,178,419 |
| Patients | 23,952,148 | 22,077,541 |
| Total patient accounts receivable | 79,510,231 | 74,164,286 |
| Less allowance for contractals | 24,106,288 | 21,342,276 |
| Less allowance for uncollectible amounts | 26,829,458 | 24,612,418 |
| Patient accounts receivable, net | \$ 28,574,485 | \$ 28,209,592 |

4. ASSETS WHOSE USE IS LIMITED

Assets whose use is limited that are required for obligations classified as current liabilities are reported in current assets. Assets whose use is limited are reported at market value and include the following at December 31, 2016 and 2015:

Investment Summary by Type

| | 2016 | % | 2015 | % |
|---|----------------|---------|----------------|---------|
| Cash and cash equivalents | \$ 69,113,474 | 47.0 % | \$ 50,353,276 | 37.2 % |
| Money market funds | 4,692,955 | 3.2 | 21,844,596 | 16.2 |
| Interest receivable | 19,687 | 0.0 | 15,845 | 0.0 |
| Certificates of deposit | 9,003,892 | 6.1 | 9,237,930 | 6.8 |
| Brokered certificates of deposit | 149,288 | 0.1 | -0- | 0.0 |
| Corporate bonds | 36,577 | 0.0 | 45,024 | 0.0 |
| Common stocks | 911,340 | 0.6 | 616,375 | 0.5 |
| Fixed income guaranteed option | 193,448 | 0.1 | 196,247 | 0.1 |
| Mutual funds | 62,562,315 | 42.6 | 52,655,379 | 38.9 |
| Perpetual trust, held by trustee | 310,215 | 0.3 | 308,534 | 0.2 |
| Total assets whose use is limited | \$ 146,993,191 | 100.0 % | \$ 135,273,206 | 100.0 % |
| Less amount required for current obligations | 1,826,227 | | 1,868,465 | |
| Assets whose use is limited, net of amount required to meet current obligations | \$ 145,166,964 | | \$ 133,404,741 | |

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Investment Summary by Fund

| | | | | |
|-----------------------------|-----------------------|----------------|-----------------------|----------------|
| Board-Designated Funds | \$ 133,738,721 | 91.0 % | \$ 121,984,305 | 90.2 % |
| Trustee-Held Funds | 3,102,106 | 2.0 | 3,732,156 | 2.7 |
| Donor-Restricted Funds | 1,992,682 | 1.4 | 1,851,405 | 1.4 |
| Deferred Compensation Funds | 8,159,682 | 5.6 | 7,705,340 | 5.7 |
| | <hr/> | | <hr/> | |
| Total | <u>\$ 146,993,191</u> | <u>100.0 %</u> | <u>\$ 135,273,206</u> | <u>100.0 %</u> |

Board-Designated Funds

The Hospital's Board of Trustees approved the funding of depreciation expense to meet the capital asset replacement needs of the facility. Depreciation is funded totally with expenditures for capital items reducing the funded depreciation balance. Board-designated funds also include amounts intended for specific purposes, as established by the Hospital's, HDC's, and Foundation's separate Boards. All income earned by the board-designated accounts is left to accumulate as additions to the funds. Board-designated funds remain under the control of the separate Boards, which may at their discretion later use for other purposes. Therefore, all board-designated funds are included in unrestricted net position.

Trustee-Held Funds

The trustee-held funds are restricted for the payments of principal and interest related to certain long-term debt agreements.

Donor-Restricted Funds

Donor-restricted funds represent donations that have been restricted by donors for specific purposes.

Deferred Compensation Funds

The deferred compensation funds represent assets that have accumulated under the Medical Center's deferred compensation plan. The Medical Center simply maintains the funds for the participants until they are withdrawn. The Medical Center records a liability equal to the deferred compensation assets.

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5. CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2016 and 2015, was as follows:

| | 2016 | | | |
|-----------------------------------|----------------------|-----------------------|---------------------------|----------------------|
| | Beginning Balance | Additions | Retirements/ Transfers | Ending Balance |
| Land | \$ 7,764,361 | \$ 20,754 | \$ 369,686 | \$ 8,154,801 |
| Land improvements | 4,383,253 | 5,400 | (106,817) | 4,281,836 |
| Leasehold improvements | 671,058 | -0- | -0- | 671,058 |
| Buildings | 86,982,502 | 314,647 | 651,490 | 87,948,639 |
| Fixed equipment | 6,456,282 | 127,142 | (1,190,278) | 5,393,146 |
| Movable equipment | 52,729,417 | 3,189,632 | (5,138,749) | 50,780,300 |
| Construction in progress | <u>1,147,873</u> | <u>6,483,761</u> | <u>(3,109,420)</u> | <u>4,522,214</u> |
| Total historical cost | 160,134,746 | 10,141,336 | (8,524,088) | 161,751,994 |
| Less accumulated depreciation for | | | | |
| Land improvements | (2,435,984) | (223,911) | 116,973 | (2,542,922) |
| Leasehold improvements | (595,347) | -0- | (53,747) | (649,094) |
| Buildings | (37,307,302) | (3,879,502) | 1,565,528 | (39,621,276) |
| Fixed equipment | (5,159,228) | (202,389) | 1,193,473 | (4,168,144) |
| Movable equipment | <u>(40,900,997)</u> | <u>(3,974,338)</u> | <u>5,316,269</u> | <u>(39,559,066)</u> |
| Total accumulated depreciation | <u>(86,398,858)</u> | <u>(8,280,140)</u> | <u>8,138,496</u> | <u>(86,540,502)</u> |
| Capital assets, net | <u>\$ 73,735,888</u> | <u>\$ 1,861,196</u> | <u>\$ (385,592)</u> | <u>\$ 75,211,492</u> |
| | 2015 | | | |
| | Beginning Balance | Additions | Retirements/ Transfers | Ending Balance |
| Land | \$ 6,732,518 | \$ -0- | \$ 1,031,843 | \$ 7,764,361 |
| Land improvements | 4,040,091 | 298,427 | 44,735 | 4,383,253 |
| Leasehold improvements | 672,661 | -0- | (1,603) | 671,058 |
| Buildings | 84,989,080 | 302,619 | 1,690,803 | 86,982,502 |
| Fixed equipment | 6,422,491 | 14,530 | 19,261 | 6,456,282 |
| Movable equipment | 51,576,420 | 1,996,631 | (843,634) | 52,729,417 |
| Construction in progress | <u>883,098</u> | <u>3,920,149</u> | <u>(3,655,374)</u> | <u>1,147,873</u> |
| Total historical cost | 155,316,359 | 6,532,356 | (1,713,969) | 160,134,746 |
| Less accumulated depreciation for | | | | |
| Land improvements | (2,204,150) | (239,968) | 8,134 | (2,435,984) |
| Leasehold improvements | (542,603) | (58,475) | 5,731 | (595,347) |
| Buildings | (33,566,068) | (3,733,214) | (8,020) | (37,307,302) |
| Fixed equipment | (4,955,367) | (203,861) | -0- | (5,159,228) |
| Movable equipment | <u>(38,201,897)</u> | <u>(4,396,681)</u> | <u>1,697,581</u> | <u>(40,900,997)</u> |
| Total accumulated depreciation | <u>(79,470,085)</u> | <u>(8,632,199)</u> | <u>1,703,426</u> | <u>(86,398,858)</u> |
| Capital assets, net | <u>\$ 75,846,274</u> | <u>\$ (2,099,843)</u> | <u>\$ (10,543)</u> | <u>\$ 73,735,888</u> |

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Long-Lived Asset Impairment

The Medical Center evaluates the recoverability of the carrying value of long-lived assets on an ongoing basis and recognizes any impairment in the year of determination. It is reasonably possible that relevant conditions could change in the near term and necessitate a change in management's estimate of the recoverability of these assets. No asset impairment was recognized during the years ended December 31, 2016 and 2015.

6. OTHER ASSETS

At December 31, 2016 and 2015, other assets consist of the following:

| | 2016 | 2015 |
|--|--------------|--------------|
| Physician notes receivable | \$ 1,195,124 | \$ 1,206,204 |
| Notes receivable | 19,115 | -0- |
| Investment in managed care company | 3,679,293 | 3,279,463 |
| Investment in RCG Columbus, LLC | 974,900 | 974,900 |
| Investment in captive insurance company | 335,311 | 335,311 |
| Captive insurance company subscriber savings | 872,403 | 872,403 |
| Investment in Inspire Health Partners | 63,770 | 61,587 |
| Goodwill | 1,075,000 | -0- |
| Other | 7,820 | 9,426 |
| Total other assets | 8,222,736 | 6,739,294 |
| Other assets, current portion | (499,629) | (297,839) |
| Other assets, net of current portion | \$ 7,723,107 | \$ 6,441,455 |

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Physician notes receivable are in varying amounts maturing through 2021. If the physicians meet the period of service requirement, the Medical Center will forgive these notes. If the physicians do not meet the period-of-service requirement, the notes are immediately due in full. Interest rates are prime rate + 1 percent (4.75 percent at December 31, 2016).

The Medical Center is a partial owner of a healthcare managed care company. The Medical Center owns 250 shares out of 1,000 for 25 percent ownership and accounts for its investment using the equity method.

The Medical Center made a \$974,900 contribution to purchase a 12.25 percent ownership interest in RCG Columbus, LLC ("RCG"). RCG provides renal care to patients. The Medical Center's investment in RCG is being accounted for under the cost method.

The Medical Center is a 12.5 percent owner of Indiana Healthcare Reciprocal Risk Retention Group (the "Captive"), a risk retention company created to purchase professional liability and general liability insurance for its members. The Medical Center accounts for this investment using the cost method. In addition, the Captive retains a subscriber savings account for each of its members based upon the premiums paid in and the resulting claims paid out, plus other factors. Members are paid the balance of their subscriber savings account once they leave the Captive in accordance with the terms of the Captive agreement.

The Medical Center is a 50 percent owner of Inspire Health Partners ("Inspire"), which is a clinically integrated network of physicians and healthcare providers who work together to coordinate patient care. Inspire is a collaboration between various hospitals, physicians, and the Medical Center to offer a community-based provider network that ensures patients get the right care, at the right time, in the right setting, in the most cost-effective manner. The Medical Center does not have majority voting rights or control over Inspire. The Medical Center accounts for this investment using the equity method.

The Medical Center purchased certain assets of a physician practice resulting in a recognition of goodwill in the amount of \$1,075,000.

Separate financial statements related to the joint ventures described above may be obtained by contacting Medical Center management.

7. COMPENSATED ABSENCES

The Medical Center provides a paid time off (PTO) policy to employees for vacation, sick time, personal days, and holidays. Upon employment, full and part-time employees who are budgeted, scheduled, and work at least 37.5 hours per pay period accrue PTO from the date of hire. After completion of 6 months of service as a benefit eligible employee, PTO may be used with pay for the total amount accrued.

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The rate at which full-time employees earn PTO and the maximum number of hours that may be banked are as follows:

| <u>Employee Type</u> | <u>Length of Service</u> | <u>PTO earned for each hour paid</u> | <u>Maximum PTO bank</u> |
|----------------------|--------------------------|--|-----------------------------|
| Non-exempt | 0 - 2 years | 0.0885 | 368 hours |
| Non-exempt | 2 - 10 years | 0.1077 | 448 hours |
| Non-exempt | 10 or more years | 0.1270 | 528 hours |
| Exempt | 0 - 2 years | 0.0885 | 368 hours |
| Exempt | 2 - 5 years | 0.1077 | 448 hours |
| Exempt | 5 or more years | 0.1270 | 528 hours |
| Vice Presidents | Upon hire | 0.1462 | 608 hours |

PTO days are accrued when incurred. The PTO accrual at December 31, 2016 and 2015 was \$4,509,795 and \$4,141,657, respectively and is reported in accrued personnel costs on the consolidated financial statements.

8. EMPLOYEE HEALTH BENEFIT PLAN

The Medical Center operates a self-funded health plan covering substantially all employees. The Medical Center has an annual stop loss limit on the plan of \$100,000 per insured per year and an aggregate stop loss limit of approximately \$8,500,000. Claim expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. Claims liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amounts of pay out, and other economic and social factors. The accrued liability for claims liabilities is recorded in accrued personnel costs on the consolidated balance sheets.

Changes in the balance of claims liabilities during the years ended December 31, 2016 and 2015, were as follows:

| | <u>2016</u> | <u>2015</u> |
|--|---------------------|---------------------|
| Accrued liability, beginning of year | \$ 1,203,381 | \$ 1,265,626 |
| Incurred claims, changes in estimates, and fees/premiums | 7,972,548 | 8,460,134 |
| Claim payments | <u>(8,089,651)</u> | <u>(8,522,379)</u> |
| Accrued liability, end of year | <u>\$ 1,086,278</u> | <u>\$ 1,203,381</u> |

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9. DEFINED BENEFIT PENSION PLAN

Plan Description

The Medical Center sponsors a single-employer, defined benefit pension plan established to provide retirement, termination/severance, disability, and survivor benefits for Medical Center employees. The Plan was established on May 1, 1975 and was last restated effective May 1, 2013. Benefit provisions are established or may be amended at any time by the action of the Plan's Board of Trustees. The Medical Center functions as the plan administrator of the defined benefit pension plan, as authorized by IC 16-22-3-11. A publicly available financial report that includes the defined benefit pension plan's financial statements and required supplementary information may be obtained by contacting:

Schneck Medical Center
P.O. Box 2349
Seymour, IN 47274
Ph. (812) 522-0118

Benefits Provided

The Plan provides that the monthly retirement benefit shall be a pension payable for the member's lifetime equal to one percent (1.00%) of the member's monthly plan compensation, plus sixty-five hundredths of one percent (0.65%) in excess of covered compensation. This sum is then multiplied by the years of benefit service up to thirty (30) years to arrive at the benefit amount. Benefit service is not credited prior to May 1, 1970. The accrued benefit shall not be less than the benefit accrued as of April 30, 1990.

Employees became eligible members of the Plan after one year of service and age twenty-one. Participants are fully vested after 5 years of service. Participation and the accrual of benefits for additional years of service for active participants was frozen as of July 1, 2010.

The employee normal retirement date is age 65 if the employee's date of participation is prior to May 1, 1990, or the later of age 65 or 5 years of service if the employee's date of participation is on or after May 1, 1990. The employee early retirement date can occur once an employee has attained age 55 and has 10 years of service. A reduced early retirement benefit is available to members with at least ten years of vesting service any time after attainment of age 55, with a reduction factor determined by the date of severance from employment.

For participants who severed employment prior to May 1, 2002, the accrued benefit is reduced one-one hundred eightieth (1/180) for each completed month of the first five years and one-three hundred sixtieth (1/360) for each completed month of the next five years by which the date of commencement precedes the normal retirement date. For participants who severed

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employment on or after May 1, 2002, the accrued benefit is reduced three percent for each year by which the date of commencement precedes the normal retirement date.

A terminated participant is eligible for termination benefits after five or more years of service with an hour of service after May 1, 2000. A disabled participant is eligible for disability retirement after five or more years of service with an hour of service after May 1, 2000.

The employee's death benefit is payable to a surviving spouse after the satisfaction of early retirements and prior to actual or normal retirement. If a participant's death occurs while an employee on or after satisfaction of early retirement requirements and prior to the earlier of their termination of employment or late retirement, their surviving spouse, if any, will be entitled to a fifty percent survivor benefit. If a participant's death occurs on or after their actual retirement while an employee, but prior to the commencement of their retirement benefit their beneficiary will be entitled to the benefit if any, payable on account of the participant's death, assuming their retirement benefit had commenced the day before their death.

Funding Policy

No contributions from active plan members are required or permitted. The Internal Revenue Service has determined that the plan is a government plan which is not subject to Employee Retirement Income Security Act (ERISA) minimum funding requirements.

Employees Covered by Benefit Terms

At April 30, 2016, the following employees were covered by the benefit terms:

| | <u>2016</u> |
|---|-------------------|
| Inactive plan members or beneficiaries currently receiving benefits | 238 |
| Inactive plan members or beneficiaries entitled to but not yet receiving benefits | 136 |
| Active plan members | <u>439</u> |
| Total | <u><u>813</u></u> |

Contributions

The annual required contributions for the year ended April 30, 2016 and estimated liabilities as of April 30, 2016 were determined as part of the actuarial valuations using the Entry Age actuarial cost method. The Medical Center intends to contribute to the Plan each year such amounts as may be required to operate the Plan on a sound actuarial basis.

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Net Pension (Asset) Liability

The total pension liability was measured as of April 30, 2016, and the total pension liability used to calculate the net pension (asset) liability was determined by an actuarial valuation as of that date.

Actuarial Assumptions

The total pension liability in the April 30, 2016 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | 2016 |
|---------------------------|---------------------------------|
| Inflation | 2.50% |
| Salary increases | Not applicable (Plan is frozen) |
| Investment rate of return | 8% |

Mortality rates were based on the 2016 IRS Annuitant/Non-Annuitant Mortality Tables (sex-distinct) with no future mortality improvement.

The actuarial value of assets was determined using the Market Value method and the trust information furnished by PNC Institutional Investments as of April 30, 2016.

The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

| Asset Class | Target Allocation | Long-Term Expected Real Rate of Return |
|-------------------------------|----------------------|---|
| Cash | -0- % | 0.0% |
| Fixed income securities | 10 | 2.0% |
| Domestic and foreign equities | 90 | 6.0% |
| Total | 100 % | |

Discount Rate

The discount rate used to measure the total pension liability was 8 percent as of April 30, 2016, and is equal to the long-term expected return on plan investments. The projection cash flows used to determine the discount rate assumed that employer contributions would be made at the actuarially calculated rate computed to prevent the deterioration in the actuarial status of the trust. The future contribution assumption was based upon the review of recent Medical Center contribution history compared to the corresponding actuarially determined contributions. Based

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on this assumption, the Plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members.

Sensitivity of the Net Pension (Asset) Liability

The following presents the net pension (asset) liability of the Plan, calculated using the discount rate of 8 percent, as well as what the Plan's net pension (asset) liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7 percent) or 1-percentage-point higher (9 percent) than the current rate:

| | 1 % Decrease (7.0%) | Current Discount Rate (8.0%) | 1% Increase (9.0%) |
|-------------------------------|------------------------|---------------------------------|-----------------------|
| Net pension (asset) liability | \$ (2,802,720) | \$ (5,852,824) | \$ (8,412,271) |

Detailed information about the Plan's fiduciary net position is available in a separately issued actuarial valuation report.

Changes in the Net Pension (Asset) Liability

The change in the net pension (asset) liability during the 2016 Plan year was as follows:

| | Total Pension Liability (a) | Plan Fiduciary Net Position (b) | Net Pension (Asset) Liability (a) - (b) |
|--|-----------------------------------|---------------------------------------|---|
| Balances at 4/30/2015 | \$ 26,869,569 | \$ 37,224,794 | \$ (10,355,225) |
| Changes of the year: | | | |
| Service cost | -0- | -0- | -0- |
| Interest | 2,077,981 | -0- | 2,077,981 |
| Difference between expected and actual experience | 216,064 | -0- | 216,064 |
| Change in assumptions | 39,514 | -0- | 39,514 |
| Benefit payments | (1,654,220) | (1,654,220) | -0- |
| Employer contributions | -0- | -0- | -0- |
| Net investment income | -0- | (2,126,387) | 2,126,387 |
| Administrative expenses | -0- | (42,455) | 42,455 |
| Other | -0- | -0- | -0- |
| Net changes | 679,339 | (3,823,062) | 4,502,401 |
| Balances at 4/30/2016 | \$ 27,548,908 | \$ 33,401,732 | \$ (5,852,824) |

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Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended December 31, 2016, the Medical Center recognized pension expense (gain) of \$239,022. At December 31, 2016, the Medical Center reported deferred outflows of resources and deferred inflows of resources related to pension from the following sources:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|-------------------------------------|-----------------------------------|----------------------------------|
| Balance, 4/30/2015 | \$ 33,168 | \$ (486,601) |
| Changes in assumptions | 28,469 | -0- |
| Liability experience gains (losses) | 184,572 | 38,347 |
| Investment gains (losses) | 3,950,488 | 61,503 |
| | \$ 4,196,697 | \$ (386,751) |

Amounts reported as deferred outflows of resources and deferred inflows of resources related to pension will be recognized in pension expense as follows:

| Year ended April 30: | Amount |
|----------------------|-------------|
| 2017 | \$ 930,309 |
| 2018 | 930,309 |
| 2019 | 930,308 |
| 2020 | 991,812 |
| 2021 | 4,190 |
| Thereafter | 23,018 |
| | \$3,809,946 |

10. LONG-TERM DEBT

At December 31, 2016 and 2015, the Medical Center was obligated for long-term debt agreements as follows:

| | 2016 | 2015 |
|---|--------------|---------------|
| Indiana Financing Authority Series 2010 Revenue Bonds dated December 2010, payable in annual principal installments commencing February 2011 through February 2022, in amounts ranging from \$325,000 to \$1,765,000. Serial fixed interest rates ranging from 3.0% to 5.0%. Secured by gross revenues. | \$ 9,530,000 | \$ 10,915,000 |

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Indiana Health and Educational Facility Financing Authority ("IHEFFA") Series 2006A Revenue Bonds dated May 2006, payable in annual principal installments commencing February 2023 through February 2030, in amounts ranging from \$465,000 to \$670,000. Fixed interest rate of 5.125%. Secured by gross revenues.

-0- 4,500,000

IHEFFA Series 2006B Revenue Bonds dated May 2006, payable in annual principal installments commencing February 2007 through February 2036 in amounts ranging from \$150,000 to \$950,000. In May 2013, bonds were converted to long-maturity and issued to Capital One Public Funding, LLC and Jackson County Bank who will hold the bonds through February 2023 at which time a balloon payment is due for all remaining unpaid principal and interest. In February 2023, Capital One and Jackson County Bank may exercise a put option on the bonds, or refinance the remaining principal with the Medical Center. Fixed interest rate of 2.8% on \$18,795,000. Secured by gross revenues.

| | | |
|--|----------------------|----------------------|
| | <u>18,495,000</u> | <u>18,645,000</u> |
| | 28,025,000 | 34,060,000 |
| Unamortized bond premium | 133,950 | 207,133 |
| Less current portion | <u>(1,631,351)</u> | <u>(1,565,402)</u> |
| Long-term debt, net of current portion | <u>\$ 26,527,599</u> | <u>\$ 32,701,731</u> |

Long-term debt activity for the years ended December 31, 2016 and 2015 was as follows:

| | 2016 | | | | |
|-----------------------------|----------------------|---------------|-----------------------|----------------------|---------------------|
| | Beginning Balance | Increases | Decreases | Ending Balance | Current Portion |
| Revenue bonds, series 2006A | \$ 4,500,000 | \$ -0- | \$ (4,500,000) | \$ -0- | \$ -0- |
| Revenue bonds, series 2006B | 18,645,000 | -0- | (150,000) | 18,495,000 | 150,000 |
| Revenue bonds, series 2010 | 10,915,000 | -0- | (1,385,000) | 9,530,000 | 1,455,000 |
| Bond premiums | 207,133 | -0- | (73,183) | 133,950 | 26,351 |
| Total long-term debt | <u>\$ 34,267,133</u> | <u>\$ -0-</u> | <u>\$ (6,108,183)</u> | <u>\$ 28,158,950</u> | <u>\$ 1,631,351</u> |

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| | 2015 | | | | |
|-----------------------------|----------------------|---------------|-----------------------|----------------------|---------------------|
| | Beginning Balance | Increases | Decreases | Ending Balance | Current Portion |
| Revenue bonds, series 2006A | \$ 4,500,000 | \$ -0- | \$ -0- | \$ 4,500,000 | \$ -0- |
| Revenue bonds, series 2006B | 18,795,000 | -0- | (150,000) | 18,645,000 | 150,000 |
| Revenue bonds, series 2010 | 12,245,000 | -0- | (1,330,000) | 10,915,000 | 1,385,000 |
| JMB note payable to bank | 139,390 | -0- | (139,390) | \$ -0- | \$ -0- |
| Bond premiums | 237,544 | -0- | (30,411) | 207,133 | 30,402 |
| Total long-term debt | \$ 35,916,934 | \$ -0- | \$ (1,649,801) | \$ 34,267,133 | \$ 1,565,402 |

Debt service requirements on long-term debt at December 31, 2016 are based on the interest rate modes in effect and are as follows:

| <u>Year Ending December 31,</u> | <u>Principal</u> | <u>Interest</u> |
|---------------------------------|----------------------|---------------------|
| 2017 | \$ 1,631,351 | \$ 989,635 |
| 2018 | 1,701,351 | 912,685 |
| 2019 | 1,781,351 | 832,235 |
| 2020 | 1,856,351 | 750,810 |
| 2021 | 1,941,351 | 664,310 |
| 2022 - 2026 | 19,247,195 | 650,470 |
| Total | <u>\$ 28,158,950</u> | <u>\$ 4,800,145</u> |

The Medical Center's debt agreements contain various restrictive covenants, including covenants related to days cash on hand ratio, debt service coverage ratio, debt to capitalization ratio, and audited financial statement submission requirements. Management believes the Medical Center was in compliance with all restrictive covenants during 2016 and 2015.

11. DEFERRED COMPENSATION PLAN

The Medical Center offers its employees deferred compensation plans in accordance with Internal Revenue Code Sections 457 and 403(b). The plans, available to all Medical Center employees, permit them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All amounts of compensation deferred under the plans, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) solely the property and rights of the Medical Center (without being restricted to the provisions of benefits under the plans), subject only to the claims of the Medical Center's general creditors. Participants' rights under the plans are equal to those of general creditors of the Medical Center in an amount equal to the fair market value of the deferred account for each participant. The Medical Center believes that it is unlikely that it will use the assets

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to satisfy the claims of general creditors in the future. The deferred compensation assets and related liabilities under these plans are reported in the consolidated balance sheets as assets whose use is limited and deferred compensation liabilities, respectively. The amounts recognized as both deferred compensation assets and liabilities were \$8,159,682 and \$7,705,340 for the years ended December 31, 2016 and 2015, respectively.

In 2010, the Medical Center amended its 403(b) defined contribution plan to allow for employer discretionary and matching contributions. For the years ended December 31, 2016 and 2015, the Medical Center recognized \$1,357,718 and \$1,310,661, respectively, in expense related to the 403(b) plan.

12. DONOR-RESTRICTED AND NONEXPENDABLE RESTRICTED NET POSITION

Donor-restricted net position amounts are donor-restricted for a specific use or by the passage of time. Nonexpendable restricted net position amounts include a perpetual trust. Donor-restricted and nonexpendable restricted net position amounts include the following at December 31, 2016 and 2015:

| | 2016 | 2015 |
|--|--------------|--------------|
| Donor-restricted net position | | |
| Dr. Bud Fund | \$ 501,609 | \$ 472,946 |
| Medical Technology Fund | 125,698 | 127,759 |
| Women's Center Fund | 2,950 | 2,475 |
| Cancer Fund | 447,624 | 365,141 |
| Hospice Fund | 325,168 | 295,134 |
| EPIC Fund | 278,034 | 276,523 |
| Employee Humanitarian Fund | 1,384 | 2,893 |
| Total donor-restricted net position | \$ 1,682,467 | \$ 1,542,871 |
| Nonexpendable restricted net position | | |
| Perpetual trust, held by trustee | \$ 310,215 | \$ 308,534 |

Dr. Bud Fund

The Dr. Bud Fund was established to provide scholarships to area students seeking to pursue careers in healthcare. Scholarships are awarded based on the recommendations of the Dr. Bud Fund Scholarship Committee.

Medical Technology Fund

The Medical Technology Fund was established to address the rapid changes in medical technology and related increased costs to replace outdated equipment. The assets of the fund are used to purchase medical equipment.

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Cancer Fund

The Cancer Fund was established to provide support for the detection/prevention of cancer.

Hospice Fund

The Hospice Fund was established to support Hospice program and patient needs.

EPIC Fund

The EPIC (Employee Partners Invested in Caring) Fund was established to receive financial support from its members for special projects and programs recommended by those members.

Perpetual Trust, Held by Trustee

The perpetual trust, held by trustee represents a donation that is held in a separate trust account. The donation is to be held in perpetuity. The Medical Center has no control over the investment strategy of the trust, and will not receive any payments from the trust's principal. However, the Medical Center is entitled to receive 20 percent of the trust's net income each year. All of the Medical Center's portion of income earned by this trust is unrestricted and may be used at the Medical Center's Board of Trustee's discretion.

13. NET PATIENT SERVICE REVENUE

For the years ended December 31, 2016 and 2015, net patient service revenue was as follows:

| | 2016 | 2015 |
|---------------------------------------|----------------|----------------|
| Gross patient service revenue | | |
| Inpatient services | \$ 68,028,360 | \$ 74,126,948 |
| Outpatient services | 262,919,879 | 248,239,549 |
| Long-term care services | 168,563,360 | 167,929,927 |
| Total gross patient service revenue | 499,511,599 | 490,296,424 |
| Deductions from revenue | | |
| Contractual allowances | (234,047,804) | (219,974,533) |
| Charity care | (1,869,476) | (2,588,685) |
| Bad debts | (16,437,849) | (15,998,803) |
| Medicaid DSH payments recognized | 3,453,828 | 2,302,552 |
| Nursing homes UPL payments recognized | 22,118,103 | 28,526,263 |
| Total deductions from revenue | (226,783,198) | (207,733,206) |
| Total net patient service revenue | \$ 272,728,401 | \$ 282,563,218 |

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The Medical Center grants credit without collateral to its patients, most of whom are local residents and insured under third-party payor agreements. The mix of gross revenues and receivables from patients and third-party payors at December 31, 2016 and 2015, was as follows:

| | 2016 | | 2015 | |
|--------------------------|----------|-------------|----------|-------------|
| | Revenues | Receivables | Revenues | Receivables |
| Medicare | 38 % | 26 % | 39 % | 25 % |
| Medicaid | 28 | 19 | 26 | 18 |
| Blue Cross | 14 | 8 | 15 | 9 |
| SIHO* | 5 | 3 | 5 | 5 |
| Other third-party payors | 8 | 13 | 7 | 13 |
| Patients | 7 | 31 | 8 | 30 |
| | 100 % | 100 % | 100 % | 100 % |

*Southeastern Indiana Health Organization

The Medical Center has agreements with third-party payors that provide for payments at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

- **Medicare**. The Medical Center is a provider of services to patients entitled to coverage under Title XVIII (Medicare) of the Health Insurance Act. The Medical Center is reimbursed for Medicare inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG) and Medicare outpatient services based on a fixed price per clinical unit of service. Differences between the total program billed charges and the payments received are reflected as deductions from revenue. At the Hospital's year end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients. The difference between computed reimbursement and interim reimbursement is reflected as a receivable from or payable to the third-party program. The Hospital's classification of patients under the Medicare program and the appropriateness of their admissions are subject to an independent review by a peer review organization under contract with the Hospital.
- **Medicaid**. The Medical Center is a provider of services to patients entitled to coverage under Title XIX (Medicaid) of the Health Insurance Act. The Medical Center is reimbursed for Medicaid inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG) and Medicaid outpatient services based on a fixed price per clinical unit of service. Differences between the total program billed charges and the payments received are reflected as deductions from revenue. There is no cost settlement for either of the inpatient or outpatient programs.
- **Charity Care**. The Medical Center provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Because the Medical Center does not collect amounts deemed to be charity care, they are not reported as revenue. The estimated costs of providing charity services are based on a calculation which

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applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the Medical Center's total operating expenses divided by gross patient service revenue. For the years ended December 31, 2016 and 2015, the Hospital incurred estimated costs of \$955,537 and \$1,323,599, respectively.

- **Other.** The Medical Center has also entered into preferred provider agreements with certain commercial insurance carriers. The basis for payment to the Medical Center under these agreements includes discounts from established charges, fee schedules, as well as inpatient DRG reimbursement methodologies.

Laws and regulations governing the Medicare and Medicaid programs 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 determination of compliance with such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

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 limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigation and/or allegations concerning possible violations of fraud and abuse statutes and/or regulations by health care providers.

The Centers for Medicare and Medicaid Services ("CMS") has been granted authority to suspend payments, in whole or in part, to Medicare providers if CMS possess reliable information on overpayment, fraud, or if willful misrepresentation exists. If CMS suspects payments are being made as the result of fraud or misrepresentation exists, CMS may suspend payment at any time without providing prior notice to the Medical Center. The initial suspensions period if limited to 180 days. However, the payment suspension period can be extended indefinitely if the matter is under investigation by the United States Department of Health, Human Services Office of Inspector General, or the United States Department of Justice. Therefore, the Medical Center is unable to predict if or when it may be subject to a suspension of payments by the Medicare and/or Medicaid programs, the possible length of the suspension period, or the potential cash flow impact of a payment suspension. Any such suspension would adversely impact the Medical Center's financial position, results of operations, and cash flows. The Medical Center believes that it is in compliance with all applicable laws and regulations.

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14. ELECTRONIC HEALTH RECORDS (EHR) INCENTIVE PAYMENTS

The Medical Center receives EHR incentive payments under the Medicare and Medicaid programs. To qualify for EHR incentive payments, the Medical Center must meet "meaningful use" criteria that become more stringent over time. The Medical Center periodically submits and attests to its use of certified EHR technology, satisfaction of meaningful use objectives, and various patient data. These submissions generally include performance measures for each annual EHR reporting period (Federal fiscal year ending on September 30th). The related EHR incentive payments are paid out over a four year transition schedule and are based upon data that is captured in the Medical Center's cost reports. The payment calculation is based upon an initial amount as adjusted for discharges, program utilization using inpatient days multiplied by a factor of total charges excluding charity care to total charges, and a transitional factor that ranges from 100% in first payment year and thereby decreasing by 25% each payment year until it is completely phased out in the fifth year.

The Medical Center recognizes EHR incentive payments as grant income when there is reasonable assurance that the Medical Center will comply with the conditions of the meaningful use objectives and any other specific grant requirements. In addition, the financial statement effects of the grants must be both recognizable and measurable. During 2016 and 2015, the Medical Center recognized approximately \$610,734 and \$61,659, respectively, in EHR incentive payments as grant income using the cliff recognition method. Under the cliff recognition method, the Medical Center records income at the end of EHR reporting period in which compliance is achieved. EHR incentive income is included in other revenue on the consolidated statements of operations and changes in net position. EHR incentive income is recognized based on management's estimate and amounts are subject to change, with such changes impacting operations in the period the changes occur.

Receipt of these funds is subject to the fulfillment of certain obligations by the Medical Center as prescribed by the program, subject to future audits and may be subject to repayment upon a determination of noncompliance.

15. HOSPITAL ASSESSMENT FEE

The purpose of the Hospital Assessment Fee ("HAF") Program is to fund the State share of enhanced Medicaid payments and Medicaid Disproportionate Share ("DSH") payments for Indiana hospitals as reflected in the hospital assessment fee reported in the consolidated statements of operations and changes in net position. Previously, the State share was funded by government entities through intergovernmental transfers. The Medicaid enhanced payments relate to both fee for service and managed care claims. The Medicaid enhanced payments are designed to follow the patient and result in increased Medicaid rates. The Medical Center recognized HAF program expense of \$3,027,163 and \$2,807,078 at December 31, 2016 and 2015, respectively. For the years ended December 31, 2016 and 2015, the Medical Center recognized revenue in net patient service revenue totaling \$ 3,453,828 and \$2,302,552, respectively, relating to the DSH adjustments.

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16. NONOPERATING REVENUES (EXPENSES)

For the years ended December 31, 2016 and 2015, nonoperating revenues (expenses) were as follows:

| | 2016 | 2015 |
|---|--------------|----------------|
| Investment income (loss) | \$ 4,070,939 | \$ 426,059 |
| Interest expense | (1,049,118) | (1,438,464) |
| Gain (loss) on disposal of capital assets | (79,242) | (10,543) |
| Donations | (170,844) | (242,206) |
| Contributions and grants | 747,405 | 537,941 |
| Change in perpetual trust | 1,681 | (24,806) |
| Inspire, gain (loss) | (47,817) | (228,384) |
| Miscellaneous | (46,716) | (184,794) |
| Total nonoperating revenues (expenses) | \$ 3,426,288 | \$ (1,165,197) |

GASB requires interest expense to be reported as nonoperating expense while FASB requires interest expense to be reported as an operating expense.

17. PROFESSIONAL LIABILITY INSURANCE

The Indiana Medical Malpractice Act, IC 34-18, provides a maximum recovery of \$250,000 for an occurrence of malpractice and \$1,250,000 for an injury or death of a patient due to an act of malpractice. The Act requires physicians to maintain medical malpractice liability insurance in the minimum amount of \$250,000 per occurrence and \$750,000 in the annual aggregate and hospitals to maintain medical malpractice liability insurance in the minimum amount of \$250,000 per occurrence and \$5,000,000 for hospitals with fewer than 100 occupied beds. The Act also requires the Medical Center to pay a surcharge to the State Patient's Compensation Fund. This fund may be used to pay medical malpractice claims in excess of the annual aggregate amount noted above, under certain terms and conditions.

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The Medical Center maintains professional liability insurance through a multiprovider reciprocal risk retention group (the "Group"), in which premiums are accrued based on the Group's experience to date. This provides protection from liability in amounts not to exceed as follows:

| | 2016 | 2015 |
|--|---------------|---------------|
| Medical Center per occurrence | \$ 250,000 | \$ 250,000 |
| Medical Center aggregate | \$ 5,000,000 | \$ 5,000,000 |
| Group umbrella aggregate | \$ 10,000,000 | \$ 10,000,000 |
| Group first additional umbrella aggregate | 10,000,000 | 10,000,000 |
| Group second additional umbrella aggregate | 10,000,000 | 10,000,000 |
| Total Group umbrella aggregate | \$ 30,000,000 | \$ 30,000,000 |

Liabilities for incurred but not reported losses at December 31, 2016 and 2015 are not determinable; however, in management's opinion, such liabilities, if any, will not have a material effect on the Medical Center's financial position and its malpractice and general liability insurance is adequate to cover losses, if any. Should the policies not be renewed or replaced with appropriate insurance coverage, claims based upon occurrences during these terms, but reported subsequently, will be uninsured. The Medical Center intends to continue carrying such insurance.

18. RELATED PARTY TRANSACTIONS

Jackson County Bank

The Medical Center's President and Chief Executive Officer serves as a member of the Board of Directors for Jackson County Bank ("JCB"). At December 31, 2016 and 2015, and for the years then ended, the Medical Center had the following related party transactions with JCB:

| | 2016 | 2015 |
|------------------|---------------|---------------|
| Deposits | \$ 51,043,449 | \$ 45,537,071 |
| Bonds payable | \$ 2,925,000 | \$ 2,950,000 |
| Interest income | \$ 120,833 | \$ 104,218 |
| Interest expense | \$ 82,017 | \$ 82,717 |

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Southeastern Indiana Health Organization (SIHO)

The Medical Center is a 25 percent owner of the SIHO insurance company. At December 31, 2016 and 2015, and for the years then ended, the Medical Center had the following related party transactions with SIHO:

| | <u>2016</u> | <u>2015</u> |
|-----------------------------|---------------|---------------|
| Patient accounts receivable | \$ 2,647,580 | \$ 3,521,983 |
| Gross patient revenue | \$ 25,607,060 | \$ 25,757,297 |
| Operating expenses | \$ 10,403,935 | \$ 9,810,638 |

19. CONCENTRATIONS OF CREDIT RISK

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

20. OPERATING LEASES

The Medical Center leases certain building space and equipment under noncancelable operating leases expiring in various years through 2020. Minimum future rental payments under these noncancelable operating leases, as of December 31, 2016, are as follows:

| Year Ending December 31, | <u>Amount</u> |
|--------------------------|---------------------|
| 2017 | \$ 353,532 |
| 2018 | 324,372 |
| 2019 | 259,464 |
| 2020 | <u>87,543</u> |
| Total minimum payments | <u>\$ 1,024,911</u> |

The Medical Center incurred \$19,842,007 and \$19,664,451 in total rent expense for the years ended December 31, 2016 and 2015, respectively, under cancelable and noncancelable operating leases.

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21. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Medical Center in estimating the fair value of its financial instruments:

Cash and Cash Equivalents

The carrying amount reported in the consolidated balance sheets for cash and cash equivalents approximates its fair value based on the short maturities of those items.

Investments

The carrying amount reported in the consolidated balance sheets for investments approximates its fair value based on the short maturities of those items.

Assets Whose Use is Limited

These assets are reported in the consolidated balance sheets at fair value. The fair value amounts are based on quoted market prices, if available, or are estimated using quoted market prices for similar securities.

Accounts Payable, Accrued Personnel Costs, and Accrued Expenses

The carrying amounts reported in the consolidated balance sheets for accounts payable, accrued personnel costs, and accrued expenses approximate their fair value based on the short maturities of those items.

Estimated Third-Party Payor Settlements

The carrying amount reported in the consolidated balance sheets for estimated third-party payor settlements approximates its fair value because they are expected to be settled in the near future.

Long-Term Debt

The carrying amounts reported in the consolidated balance sheets for long-term debt at December 31, 2016 and 2015 is \$28,158,950 and \$34,267,133, respectively. The fair value of long-term debt at December 31, 2016 and 2015 is approximately \$28,107,546 and \$34,713,350, respectively. Fair value for fixed interest rate debt was calculated using the 30 year United States of America Treasury incremental bond borrowing rate at December 31, 2016.

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Deferred Compensation Liabilities and Deferred Costs

The carrying amounts reported in the consolidated balance sheets for deferred compensation liabilities and deferred costs approximate their fair value. The fair value amounts are based on quoted market prices, if available, or are estimated using quoted market prices for similar securities.

22. CONTINGENCIES

The Medical Center is susceptible to a variety of legal proceedings and claims by others against the Medical Center in a variety of matters arising out of the conduct of the Medical Center's business. The ultimate resolution of such claims would not, in the opinion of management, have a material adverse effect on the financial statements.

There may be unknown incidents arising from services provided to patients. However, because the annual insurance policy only covers claims that have been asserted and incidents reported to the insurance carrier, these unknown incidents are not yet covered by insurance. Management intends to maintain the current claims-made insurance coverage to cover any unknown incidents that may be asserted.

Current Economic Conditions

The current economic situation continues to present hospitals with unprecedented circumstances and challenges, which in some cases have results in large declines in the fair value of investments and other assets, large declines in contributions, constraints on liquidity, and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to the Medical Center.

Current economic conditions and employer benefit trends have made it difficult for certain patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed/underemployed, services provided to self-pay and other payers may significantly impact net patient service revenue. Further, the effect of economic conditions on the state may have an adverse effect on cash flows related to the Medicaid program.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statement could change rapidly, resulting in material future adjustments in asset values and allowances for accounts receivable that could negatively impact the Medical Center's ability to improve its financial position and results of operations.

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HIPAA

Management continues to implement policies, procedures, and a compliance-monitoring organizational structure to enforce and monitor compliance with the Health Insurance Portability and Accountability Act of 1996 ("HIPAA") and other government statutes and regulations. The Medical Center's compliance with such laws and regulations is subject to future government review and interpretations, as well as regulatory actions which are unknown or unasserted at this time.

Health Care Reform Legislation

In March 2010, Congress adopted comprehensive health care insurance legislation, the Patient Care Protection and Affordable Care Act and the Health Care and Education Reconciliation Act (collectively, the "Health Care Reform Legislation" or "HCRL"). The HCRL, among other matters, is designed to expand access to health care coverage to substantially all citizens through a combination of public program expansion and private industry health insurance. Provisions of the HCRL become effective at various dates over the next several years and a number of additional steps are required to implement these requirements.

Starting in 2014, the legislation required the establishment of health insurance exchanges, which provide individuals without employer provided health care coverage the opportunity to purchase insurance. Some employers currently offering insurance to employees have opted to have employees seek insurance coverage through the insurance exchanges. In some cases, reimbursement rates paid by insurers participating in the insurance exchanges may be substantially different than rates paid under current health insurance products. Another significant component of the HCRL is the expansion of the Medicaid program to a wide range of newly eligible individuals. In anticipation of this expansion, payments under certain existing programs, such as Medicare disproportionate share, substantially decreased. Each state's participation in an expanded Medicaid program is optional. The State of Indiana is currently participating in the expansion of the Medicaid program.

Due to the complexity of the HCRL, reconciliation and implementation of the legislation continues to be under consideration by lawmakers, and it is not certain as to what changes may be made in the future regarding health care policies. Changes to existing Medicaid coverage and payments are also expected to occur as a result of this legislation. While the full impact of HCRL is not yet fully known, changes to policies regarding reimbursement, universal health insurance, and managed competition may materially impact the Medical Center's operations. Additional, it is possible the Medical Center will experience payment delays and other operational challenges during implementation.

Currently, the new administration is reviewing options to develop and pass legislation for a new health care bill. It is unknown what impact new legislation could have on the Medical Center.

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23. COMMITMENTS

As of December 31, 2016, the Medical Center has construction and renovation project commitments as follows:

| Project | Expected Date of Completion | Estimated Total Cost of Project | Costs Incurred as of December 31, 2016 |
|--------------------------|--------------------------------|------------------------------------|---|
| Power plant expansion | 2017 | \$ 1,250,000 | \$ 1,351,356 |
| Rehab elevator 11 | 2017 | 2,100,000 | 1,322,727 |
| Data center | 2017 | 1,500,000 | 5,149 |
| MM/Sterile/CDS expansion | 2018 | 2,400,000 | 102,512 |
| PACS - Radiology | 2017 | 1,045,000 | 162,674 |
| All other projects | 2017 | 1,615,714 | 1,577,796 |
| | | <u>\$ 9,910,714</u> | <u>\$ 4,522,214</u> |

24. CONDENSED FINANCIAL INFORMATION

The Medical Center includes three blended component units in its reporting entity. Condensed component unit information for all of its blended as of and for the year ended December 31, 2016 is as follows:

| | HDC | Foundation | JMB | Total |
|------------------------------------|---------------------|---------------------|---------------------|---------------------|
| Balance sheet | | | | |
| Assets | | | | |
| Current assets | \$ 1,516,741 | \$ 607,278 | \$ 896,112 | \$ 3,020,131 |
| Assets whose use is limited | -0- | 1,682,467 | -0- | 1,682,467 |
| Capital assets, net | 423,645 | -0- | 3,347,715 | 3,771,360 |
| Other assets | 227,258 | -0- | -0- | 227,258 |
| Total assets | 2,167,644 | 2,289,745 | 4,243,827 | 8,701,216 |
| Deferred outflows | -0- | -0- | -0- | -0- |
| Total assets and deferred outflows | <u>\$ 2,167,644</u> | <u>\$ 2,289,745</u> | <u>\$ 4,243,827</u> | <u>\$ 8,701,216</u> |
| Liabilities | | | | |
| Current liabilities | \$ 1,176,326 | \$ 10,000 | \$ 1,114 | \$ 1,187,440 |
| Long-term liabilities | -0- | -0- | -0- | -0- |
| Total liabilities | 1,176,326 | 10,000 | 1,114 | 1,187,440 |
| Net position | | | | |
| Net investment in capital assets | 423,645 | -0- | 3,347,715 | 3,771,360 |
| Restricted expendable | -0- | 1,682,467 | -0- | 1,682,467 |
| Restricted nonexpendable | -0- | -0- | -0- | -0- |
| Unrestricted | 567,673 | 597,278 | 894,998 | 2,059,949 |
| Total net position | <u>991,318</u> | <u>2,279,745</u> | <u>4,242,713</u> | <u>7,513,776</u> |
| Total liabilities and net position | <u>\$ 2,167,644</u> | <u>\$ 2,289,745</u> | <u>\$ 4,243,827</u> | <u>\$ 8,701,216</u> |

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| | HDC | Foundation | JMB | Total |
|--|-------------------|---------------------|---------------------|---------------------|
| Statement of operations and changes in net position | | | | |
| Operating revenues | | | | |
| Net patient service revenue | \$ 1,811,848 | \$ -0- | \$ -0- | \$ 1,811,848 |
| Other operating revenue | 1,850,897 | -0- | 769,828 | 2,620,725 |
| Total operating revenues | 3,662,745 | -0- | 769,828 | 4,432,573 |
| Operating expenses | | | | |
| Depreciation and amortization | 130,367 | 12,318 | 188,084 | 330,769 |
| Other operating expenses | 4,347,589 | 51,856 | 377,226 | 4,776,671 |
| Total operating expenses | 4,477,956 | 64,174 | 565,310 | 5,107,440 |
| Income (loss) from operations | (815,211) | (64,174) | 204,518 | (674,867) |
| Non-operating gains (losses) | (560) | (440,974) | - | (441,534) |
| Change in net position | (815,771) | (505,148) | 204,518 | (1,116,401) |
| Net position - beginning of year | 1,807,089 | 2,784,893 | 4,038,195 | 8,630,177 |
| Net position - end of year | <u>\$ 991,318</u> | <u>\$ 2,279,745</u> | <u>\$ 4,242,713</u> | <u>\$ 7,513,776</u> |

| | HDC | Foundation | JMB | Total |
|--|-------------------|-------------------|-------------------|---------------------|
| Statement of cash flows | | | | |
| Cash provided by | | | | |
| Operating activities | \$ (485,916) | \$ 142,701 | \$ 406,262 | \$ 63,047 |
| Noncapital financing activities | -0- | -0- | -0- | -0- |
| Capital and related financing activities | 280,606 | -0- | -0- | 280,606 |
| Investing activities | (51,350) | (167,937) | -0- | (219,287) |
| Total | (256,660) | (25,236) | 406,262 | 124,366 |
| Cash - beginning of year | 1,077,137 | 217,101 | 479,267 | 1,773,505 |
| Cash - end of year | <u>\$ 820,477</u> | <u>\$ 191,865</u> | <u>\$ 885,529</u> | <u>\$ 1,897,871</u> |

Condensed component unit information for all of its blended components as of and for the year ended December 31, 2015 is as follows:

| | HDC | Foundation | JMB | Total |
|------------------------------------|---------------------|---------------------|---------------------|----------------------|
| Balance sheet | | | | |
| Assets | | | | |
| Current assets | \$ 2,043,319 | \$ 576,641 | \$ 503,511 | \$ 3,123,471 |
| Assets whose use is limited | -0- | 1,542,871 | -0- | 1,542,871 |
| Capital assets, net | 868,339 | 685,381 | 3,535,798 | 5,089,518 |
| Other assets | 556,911 | -0- | -0- | 556,911 |
| Total assets | 3,468,569 | 2,804,893 | 4,039,309 | 10,312,771 |
| Deferred outflows | -0- | -0- | -0- | -0- |
| Total assets and deferred outflows | <u>\$ 3,468,569</u> | <u>\$ 2,804,893</u> | <u>\$ 4,039,309</u> | <u>\$ 10,312,771</u> |
| Liabilities | | | | |
| Current liabilities | \$ 1,551,480 | \$ 20,000 | \$ 1,114 | \$ 1,572,594 |
| Long-term liabilities | 110,000 | -0- | -0- | 110,000 |
| Total liabilities | 1,661,480 | 20,000 | 1,114 | 1,682,594 |
| Net position | | | | |
| Net investment in capital assets | 868,339 | 685,381 | 3,535,798 | 5,089,518 |
| Restricted expendable | -0- | 1,542,871 | -0- | 1,542,871 |
| Restricted nonexpendable | -0- | -0- | -0- | -0- |
| Unrestricted | 938,750 | 556,641 | 502,397 | 1,997,788 |
| Total net position | 1,807,089 | 2,784,893 | 4,038,195 | 8,630,177 |
| Total liabilities and net position | <u>\$ 3,468,569</u> | <u>\$ 2,804,893</u> | <u>\$ 4,039,309</u> | <u>\$ 10,312,771</u> |

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| | HDC | Foundation | JMB | Total |
|--|--------------|--------------|--------------|--------------|
| Statement of operations and changes in net position | | | | |
| Operating revenues | | | | |
| Net patient service revenue | \$ 1,858,779 | \$ -0- | \$ -0- | \$ 1,858,779 |
| Other operating revenue | 2,027,298 | -0- | 767,353 | 2,794,651 |
| Total operating revenues | 3,886,077 | -0- | 767,353 | 4,653,430 |
| Operating expenses | | | | |
| Depreciation and amortization | 141,725 | 18,477 | 175,261 | 335,463 |
| Other operating expenses | 3,918,520 | 51,670 | 328,731 | 4,298,921 |
| Total operating expenses | 4,060,245 | 70,147 | 503,992 | 4,634,384 |
| Income (loss) from operations | (174,168) | (70,147) | 263,361 | 19,046 |
| Non-operating gains (losses) | 49,462 | 19,228 | 5,783 | 74,473 |
| Change in net position | (124,706) | (50,919) | 269,144 | 93,519 |
| Net position - beginning of year | 1,931,795 | 2,835,812 | 3,769,051 | 8,536,658 |
| Net position - end of year | \$ 1,807,089 | \$ 2,784,893 | \$ 4,038,195 | \$ 8,630,177 |
| | HDC | Foundation | JMB | Total |
| Statement of cash flows | | | | |
| Cash provided by | | | | |
| Operating activities | \$ (245,775) | \$ (9,894) | \$ 406,003 | \$ 150,334 |
| Noncapital financing activities | -0- | -0- | -0- | -0- |
| Capital and related financing activities | (58,054) | -0- | (553,272) | (611,326) |
| Investing activities | (105,178) | (9,258) | -0- | (114,436) |
| Total | (409,007) | (19,152) | (147,269) | (575,428) |
| Cash - beginning of year | 1,486,144 | 236,253 | 626,536 | 2,348,933 |
| Cash - end of year | \$ 1,077,137 | \$ 217,101 | \$ 479,267 | \$ 1,773,505 |

25. RECENT GASB PRONOUNCEMENTS

Management has not currently determined what effects, if any, the implementation of the following recently enacted statements may have on its future financial statements:

GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, issued June 2015, will be effective for periods beginning after June 15, 2016. The objective of this Statement is to improve the usefulness of information about pensions included in the general purpose external financial reports of statement and local governments for making decisions and assessing accountability. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2016 AND 2015

GASB Statement No. 80, *Blending Requirements for Certain Component Units – an amendment of GASB Statement No. 14*, issued January 2016, will be effective for periods beginning after June 15, 2016. The objective of this Statement is to improve financial reporting by clarifying the financial statement presentation requirements for certain component units. This Statement amends the blending requirements established in paragraph 53 of Statement No. 14, *The Financial Reporting Entity, as amended*. The Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units*.

GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, issued March 2016, will be effective for periods beginning after June 15, 2016. The objective of this Statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. Split-interest agreements are a type of giving agreement used by donors to provide resources to two or more beneficiaries, including governments. Split-interest agreements can be created through trusts – or other legally enforceable agreements with characteristics that are equivalent to split-interest agreements – in which a donor transfers resources to an intermediary to hold and administer for the benefit of a government and at least one other beneficiary. Examples of these types of agreements include charitable lead trusts, charitable remainder trusts, and life-interests in real estate. This Statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement. Furthermore, this Statement requires that a government recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party, if the government controls the present service capacity of the beneficial interests. This Statement requires that a government recognize revenue when the resources become applicable to the reporting period.

GASB Statement No. 82, *Pension Issues-An Amendment of GASB Statements No. 67, No. 68, and No. 73*, issued March 2016, will be effective for periods beginning after June 15, 2016. The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this Statement address issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in the Actuarial Standard of Practice for financial reporting purposes, and, (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

REQUIRED SUPPLEMENTARY INFORMATION

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REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2016

**SCHEDULE OF CHANGES IN THE MEDICAL CENTER'S NET PENSION (ASSET) LIABILITY
AND RELATED RATIOS**

| | 2016 | 2015 | 2014 |
|---|-----------------------|------------------------|---------------|
| Total pension liability | | | |
| Service cost | \$ -0- | \$ -0- | \$ -0- |
| Interest | 2,077,981 | 2,056,704 | -0- |
| Difference between expected and actual experience | 216,064 | (278,935) | -0- |
| Change in assumptions | 39,514 | 38,454 | -0- |
| Benefit payments | (1,654,220) | (1,430,850) | -0- |
| Net change in total pension liability | 679,339 | 385,373 | -0- |
| Total pension liability - beginning | 26,869,569 | 26,484,196 | -0- |
| Total pension liability - ending (a) | <u>\$ 27,548,908</u> | <u>\$ 26,869,569</u> | <u>\$ -0-</u> |
| Plan fiduciary net position | | | |
| Employer contributions | \$ -0- | \$ -0- | \$ -0- |
| Net transfers into (out of) trust | -0- | -0- | -0- |
| Net investment income | (2,126,387) | 3,223,583 | -0- |
| Benefit payments | (1,654,220) | (1,430,850) | -0- |
| Administrative expenses | (42,455) | (67,884) | -0- |
| Other | -0- | (37,011) | -0- |
| Net change in plan fiduciary net position | (3,823,062) | 1,687,838 | -0- |
| Plan fiduciary net position - beginning | 37,224,794 | 35,536,956 | -0- |
| Plan fiduciary net position - ending (b) | <u>\$ 33,401,732</u> | <u>\$ 37,224,794</u> | <u>\$ -0-</u> |
| Medical Center net pension (asset) liability - ending (a) - (b) | <u>\$ (5,852,824)</u> | <u>\$ (10,355,225)</u> | <u>\$ -0-</u> |
| Plan fiduciary net position as a percentage of the total net pension liability | 121.25% | 138.54% | 0.00% |
| Covered-employee payroll | N/A | N/A | N/A |
| Medical Center net pension (asset) liability as a percentage of covered-employee payroll | N/A | N/A | N/A |

*The schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, the Medical Center will present information for those years for which information is available.

**JACKSON COUNTY SCHNECK MEMORIAL HOSPITAL
AND AFFILIATED ORGANIZATIONS**

REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2016

SCHEDULE OF MEDICAL CENTER CONTRIBUTIONS

| | Actuarially determined contribution | Employer contributions | Contribution deficiency (excess) | Covered employee payroll | Contributions as a % of covered employee payroll |
|-----------|---|---------------------------|--|-----------------------------|--|
| 4/30/2016 | \$ -0- | \$ -0- | \$ -0- | N/A | N/A |
| 4/30/2015 | -0- | -0- | -0- | N/A | N/A |
| 4/30/2014 | -0- | -0- | -0- | N/A | N/A |
| 4/30/2013 | -0- | -0- | -0- | N/A | N/A |
| 4/30/2012 | -0- | -0- | -0- | N/A | N/A |
| 4/30/2011 | -0- | -0- | -0- | N/A | N/A |

Notes to Schedule

Valuation date: Actuarially determined contribution rates are calculated as of May 1, one year prior to the end of the fiscal year in which contributions are reported.

Methods and assumptions used to determine most current contribution rate above:

| | |
|-------------------------------|--|
| Actuarial cost method | Entry Age |
| Amortization method | Level dollar, open |
| Remaining amortization method | 30 years |
| Asset valuation method | Market value |
| Inflation | 2.50% |
| Salary increases | Not applicable (Plan is frozen) |
| Investment rate of return | 8.00% |
| Retirement age | 65 |
| Mortality | 2016 IRS Annuitant/Non-Annuitant Mortality Tables (sex-distinct) with no mortality improvement |