Indiana Orthopaedic Hospital, LLC
d/b/a OrthoIndy Hospital

Independent Auditor’s Report and Consolidated Financial Statements

December 31, 2017 and 2016

Indiana Orthopaedic Hospital, LLC
d/b/a OrthoIndy Hospital
December 31, 2017 and 2016

Contents

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Independent Auditor's Report

Board of Managers
Indiana Orthopaedic Hospital
d/b/a OrthoIndy Hospital
Indianapolis, Indiana

We have audited the accompanying consolidated financial statements of Indiana Orthopaedic Hospital, LLC d/b/a OrthoIndy Hospital, which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, members' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Indiana Orthopaedic Hospital, LLC d/b/a OrthoIndy Hospital of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

BKD, LLP

Indianapolis, Indiana
March 12, 2018

Indiana Orthopaedic Hospital, LLC
d/b/a OrthoIndy Hospital
Consolidated Balance Sheets
December 31, 2017 and 2016

Assets

	2017	2016
Current Assets		
Cash and cash equivalents	$ 8,802,979	$ 6,245,805
Patient accounts receivable, net of allowance: 2017 - $3,900,000 2016 - $5,700,000	23,841,639	19,857,335
Supplies	925,099	934,432
Prepaid expenses and other	1,608,688	2,417,224
Total current assets	35,178,405	29,454,796
Property and Equipment, at cost		
Land and land improvements	5,992,046	4,947,195
Buildings and improvements	3,114,586	2,685,216
Equipment	30,863,695	28,495,921
	39,970,327	36,128,332
Less accumulated depreciation	23,295,527	20,916,914
	16,674,800	15,211,418
Other Assets		
Other	68,862	68,862
Total assets	$ 51,922,067	$ 44,735,076

Liabilities and Members' Equity

	2017	2016
Current Liabilities		
Accounts payable	$ 7,083,147	$ 6,497,428
Accrued expenses	3,604,797	3,713,788
Current maturities of long-term obligations	762,601	924,336
Total current liabilities	11,450,545	11,135,552
Long-Term Obligations	3,203,448	3,910,858
Total liabilities	14,653,993	15,046,410
Members' Equity	37,268,074	29,688,666
Total liabilities and members' equity	$ 51,922,067	$ 44,735,076

Indiana Orthopaedic Hospital, LLC
d/b/a OrthoIndy Hospital
Consolidated Statements of Income
Years Ended December 31, 2017 and 2016

	2017	2016
Operating Revenues		
Net patient service revenue (net of contractual discounts and allowance	$ 171,174,061	$ 160,116,895
Provision for uncollectible accounts	(3,852,028)	(2,123,471)
Net patient service revenue less provision for uncollectible accounts	167,322,033	157,993,424
Other	525,912	473,937
Total operating revenues	167,847,945	158,467,361
Expenses and Losses		
Salaries and wages	27,483,757	26,902,940
Employee benefits	5,234,251	5,313,630
Purchased services and professional fees	8,254,867	7,649,701
Medical supplies and pharmaceuticals	36,035,504	34,710,126
Facility expense	11,922,638	11,498,616
Management fees	8,233,189	7,497,191
Depreciation and amortization	2,458,079	2,578,423
Interest	116,632	120,911
Provider hospital assessment fee	1,752,476	1,444,184
Other expenses	2,629,124	2,351,481
Total operating expenses	104,120,517	100,067,203
Net Income	$ 63,727,428	$ 58,400,158

Indiana Orthopaedic Hospital, LLC
d/b/a OrthoIndy Hospital
Consolidated Statements of Members' Equity
Years Ended December 31, 2017 and 2016

Balance, January 1, 2016	$ 44,031,653
Net income	58,400,158
Membership units issued	934,320
Membership units redeemed	(282,380)
Distributions to members	(73,395,085)
Balance, December 31, 2016	29,688,666
Net income	63,727,428
Membership units issued	6,571,980
Membership units redeemed	(720,000)
Distributions to members	(62,000,000)
Balance, December 31, 2017	$ 37,268,074

Indiana Orthopaedic Hospital, LLC
d/b/a OrthoIndy Hospital
Consolidated Statements of Cash Flows
Years Ended December 31, 2017 and 2016

	2017	2016
Operating Activities		
Net income	$ 63,727,428	$ 58,400,158
Items not requiring cash		
Depreciation and amortization	2,458,079	2,578,423
Provision for uncollectible accounts	3,852,028	2,123,471
Changes in		
Patient accounts receivable, net	(7,836,332)	(2,759,282)
Accounts payable and accrued expenses	476,728	2,517,588
Other current and noncurrent assets	817,869	(1,457,822)
Net cash provided by operating activities	63,495,800	61,402,536
Investing Activity - purchase of property and equipment	(3,921,461)	(1,623,911)
Financing Activities		
Principal payments under long-term obligations	(869,145)	(1,204,510)
Proceeds from issuance of membership units	6,571,980	934,320
Distributions to members	(62,000,000)	(73,395,085)
Unit redemption	(720,000)	(282,380)
Net cash used in financing activities	(57,017,165)	(73,947,655)
Increase (Decrease) in Cash and Cash Equivalents	2,557,174	(14,169,030)
Cash and Cash Equivalents, Beginning of Year	6,245,805	20,414,835
Cash and Cash Equivalents, End of Year	$ 8,802,979	$ 6,245,805
Supplemental Cash Flows Information		
Interest paid	$ 116,632	$ 120,911
Capital lease obligations incurred for capital assets	-	1,582,128

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Indiana Orthopaedic Hospital, LLC d/b/a OrthoIndy Hospital primarily earns revenues by providing inpatient and outpatient musculoskeletal and related surgical services to patients in the greater Indianapolis, Indiana area.

NNS, LLC was formed for the purpose to own, manage, invest, develop, lease and otherwise deal in real property.

Principles of Consolidation

The consolidated financial statements include the accounts of Indiana Orthopaedic Hospital, LLC d/b/a OrthoIndy Hospital and NNS, LLC (collectively, the Hospital). All material inter-organizational accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2017 and 2016, cash equivalents consisted primarily of money market accounts.

At December 31, 2017, the Hospital’s cash accounts exceeded federally insured limits by approximately $12,500,000.

Investment Return

Investment return is comprised primarily of interest income earned on the operating cash accounts.

Patient Accounts Receivable

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the Hospital analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer 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 coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid, or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely).

For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Hospital 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 or provided by policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Supplies

The Hospital states supply inventories at the lower of cost, determined using the first-in, first-out (FIFO) method or market.

Property and Equipment

Property and equipment is stated at cost and is depreciated on a straight-line basis over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital:

Buildings and leasehold improvements	5-40 years
Equipment	2-20 years

Long-Lived Asset Impairment

The Hospital evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

No asset impairment was recognized during the years ended December 31, 2017 and 2016.

Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such estimated amounts are revised in future periods as adjustments become known.

Substantially all of the net patient service revenue received by the Hospital is from third-party payer sources.

Charity Care

The Hospital provides charity care to patients who are unable to pay for services. The amount of charity care is included in net patient service revenue and is not separately classified from the provision for uncollectible accounts.

Estimated Malpractice Costs

The Hospital recognizes an accrual for claim liabilities based on estimated ultimate losses and costs associated with settling claims and a receivable to reflect the estimated insurance recoveries, if any. Malpractice claims are described more fully later in these notes.

Income Taxes

The Hospital is organized as a pass-through limited liability company under the Internal Revenue Code. As such, the Hospital is not taxed at the entity level, and income is passed through to the members of the Hospital. Accordingly, the Hospital does not recognize income taxes in the accompanying consolidated financial statements. The Hospital's tax years still subject to examination by taxing authorities are years subsequent to December 31, 2014.

Note 2: Net Patient Service Revenue

The Hospital recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients who do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital records a significant provision for bad debts related to uninsured patients in the period the services are provided. This provision for bad debts is presented on the consolidated statements of income as a component of net patient service revenue.

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

Medicare. Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary.

Medicaid. Inpatient acute care services and substantially all outpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates. Approximately 29% of the Hospital's receivables are due from a single commercial insurance carrier for the years ended December 31, 2017 and 2016.

Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the year ended December 31, was approximately:

	2017	2016
Medicaid	$ 2,162,969	$ 1,695,489
Medicare	31,967,590	30,853,115
Other third-party payers and self-pay	137,043,502	127,568,291
Total	$ 171,174,061	$ 160,116,895

Note 3: Limited Liability Company

The Hospital is organized as an Indiana limited liability company and is owned by four classes of units and members, referred to as Classes A, B, C and D.

Effective January 1, 2013, the Hospital's individual Class A and Class B members, which are more fully described below, entered into an agreement with Orthopaedics-Indianapolis, Inc. (OI). The terms of the agreements provided that the Class A and Class B members exchanged their units of the Hospital for additional shares of OI, thereby, resulting in OI becoming the majority member in the Hospital. In connection with this agreement, the Hospital amended its Operating Agreement permitting the exchange of units and permitting OI to become a Class A member of the Hospital. The Hospital's Amended and Restated Operating Agreement also permits a new entity, APM Holdings, LLC, to become a Class A member; total Class A shares represent approximately 78.42%, which was $28,656,145 and $23,281,852 at December 31, 2017 and 2016, respectively. The previous Class D member will continue to own 20% as a Class C member (a new Class of units) and an irrevocable trust established by the Hospital will own approximately 1.58% as a Class D member. The Class C member's equity was $7,453,615 and $5,937,733 at December 31, 2017 and 2016, while the Class D member's equity was $588,836 and $469,081 at December 31, 2017 and 2016, respectively. Founding members of the Hospital will continue to hold a founding member's interest approximating 3% in the Hospital as Class B members as set forth in the Amended and Restated Operating Agreement. Total Class B members' equity was $569,478 at December 31, 2017. Classes A and B vote their respective ownership interest. The Class D member does not have a vote.

The Class C member owns 20% of the Hospital's outstanding units, and is entitled to a single vote equal to 20% interest in all of the Hospital's issues other than issues related to the issuance or redemption of Class A units or any of the Hospital's solely owned subsidiaries. Effective May 1, 2016, the Class C member acquired from Class A members a 20% profits interest attributed to the South Campus for $17,300,000. The purchase of the profits interest of the South Campus required the Hospital amended and restated Operating Agreement to prospectively provide for the change in pro-rata profit distribution. In connection with the purchase of the profits interest and the associated Amended and Restated Operating Agreement, the Hospital has certain call rights that provides the Hospital the right to repurchase the profit interest in the South Side Campus. Under the terms of the Class C units, for any reason, the Class C member may elect to require the Hospital to purchase the Class C units. Additionally, voting Class A members may elect to call the outstanding units. Such transactions will be based upon the then fair market value, as defined in the operating agreement.

NNS, LLC (Company) was organized as a limited liability company and was formed in October 2008. Indiana Orthopaedic Hospital, LLC d/b/a OrthoIndy Hospital is the sole member of NNS, LLC with complete authority, power and discretion to manage and control the business affairs and properties of the Company, to make all decisions regarding those matters and to perform any and all other acts or activities customary or incident to the management of NNS, LLC's business. The Hospital holds 100 units of the Company.

Note 4: Medical Malpractice Coverage and Claims

Medical Malpractice Claims

The Hospital is a qualified health care provider under the Indiana Medical Malpractice Act and is fully insured under a claims-made policy on a fixed premium basis. The Indiana Medical Malpractice Act limits a qualified provider's liability for an occurrence to the amount of required insurance. The Indiana patient compensation fund is liable for the excess up to an overall damage cap. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claim experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

Note 5: Line of Credit

The Hospital is a party to a $5,000,000 line of credit agreement and a $2,000,000 equipment purchase line agreement, as of December 31, 2017 and 2016. The line of credit agreement expires August 1, 2018, and the equipment purchase line expires August 5, 2018. Interest on the line of credit and equipment purchase line varies with the bank's prime rate. At December 31, 2017, the interest rate was 3.00% and 3.50% on the line of credit and the equipment purchase line, respectively. At December 31, 2017 and 2016, there was nothing drawn on the equipment purchase line or the line of credit.

Note 6: Long-Term Obligations

	2017	2016
Capital lease obligations (A)	$ 1,060,760	$ 1,362,650
Capital lease obligations (B)	67,826	146,615
Capital lease obligations (C)	173,674	237,289
Capital lease obligations (D)	-	64,053
Capital lease obligations (E)	-	43,445
Note payable to bank (F)	477,539	662,392
Note payable to bank (G)	2,186,250	2,318,750
Total long-term obligations	3,966,049	4,835,194
Less current maturities	762,601	924,336
	$ 3,203,448	$ 3,910,858

(A) Capital lease obligation payable in monthly installments of $28,880 with an interest rate of 3.64%. The lease is governed by a master lease agreement from a leasing company and is secured by the leased equipment. The lease was amended on March 30, 2016 and is scheduled to expire in 2021.

(B) Capital lease obligation payable in monthly installments of $11,330 with an interest rate of .78%. The lease is governed by a master lease agreement from a leasing company and is secured by the leased equipment. The lease is scheduled to expire at the beginning of 2018.

(C) Capital lease obligation payable in monthly installments of $5,524 with an interest rate of 1.28%. The lease is governed by a master lease agreement from a leasing company and is secured by the leased equipment. The lease is scheduled to expire in 2020.

(D) Capital lease obligation payable in monthly installments of $6,475 with an interest rate of 3.55%. The lease is governed by a master lease agreement from a leasing company is secured by the leased equipment. At December 31, 2017, the lease was paid in full.

(E) Capital lease obligation payable in monthly installments of $10,981 with an interest rate of 2.50%. The lease is governed by a master lease agreement from a leasing company is secured by the leased equipment. At December 31, 2017, the lease was paid in full.

(F) A promissory note payable in 60 monthly installments of $15,404 plus variable rate interest of prime less one-half percent. At December 31, 2017, this rate was 2.75%. The loan is secured by the Hospital's assets. The loan was originally a draw on the Hospital's equipment purchase line in early 2015, and it converted into a promissory note in August 2015. The promissory note matures in July 2020.

(G) During 2014, the Hospital refinanced two of its promissory notes. The new promissory note in the name of NNS, LLC is payable in monthly installments of $11,042 and matures in June 2019. Interest is payable monthly at a rate of LIBOR plus 1.25%. At December 31, 2017, this rate was 2.49%. The loan is secured by certain real estate.

Property and equipment include the following property under capital lease arrangements:

	2017	2016
Equipment	$ 2,976,070	$ 2,976,070
Less accumulated depreciation	1,782,111	1,149,064
	$ 1,193,959	$ 1,827,006

Aggregate annual payments on capital lease obligations and long-term debt at December 31, 2017, are:

	Long-Term Debt (Excluding Capital Lease Obligations)	Capital Lease Obligations
2018	$ 317,354	$ 480,664
2019	2,238,604	412,846
2020	107,831	390,745
2021	-	86,553
	$ 2,663,789	1,370,808
Less amount representing interest		68,548
Present value of future minimum lease payments		1,302,260
Less current maturities		445,247
Noncurrent portion		$ 857,013

Note 7: Operating Leases

Noncancellable operating leases for the primary Hospital facility, several other facilities in the greater Indianapolis area and certain diagnostic equipment expire through 2025. The facility leases generally contain renewal options for periods ranging from five to ten years and require the Hospital to pay all executory costs (property taxes, maintenance and insurance). The leases are secured by certain assets, as defined in the lease agreements.

Future minimum lease payments at December 31, 2017, were:

2018	$ 8,104,092
2019	8,194,649
2020	8,347,674
2021	8,392,622
2022	8,539,749
Later years	22,970,382
Future minimum lease payments	$ 64,549,168

Total lease expense was $7,669,312 and $7,435,992 for 2017 and 2016, respectively.

Note 8: Related Party Transactions

The Hospital and Orthopaedics-Indianapolis, Inc. (OI) are related parties through OI's ownership of the Hospital. OI provides certain management, administrative and payroll related services for the Hospital. Amounts paid to OI for these services were $1,135,286 and $1,148,245 for the years ended December 31, 2017 and 2016, respectively. Reimbursed expenses from OI amounted to $581,539 and $1,190,632 for the years ended December 31, 2017 and 2016. Amounts due from and to OI, are reported in the accompanying consolidated balance sheets as other current assets or liabilities. Amounts due to OI was $677,937 and $167,536 at December 31, 2017 and 2016, respectively.

OrthoIndy Enterprises, LLC (OE) is a related party through common ownership. The Hospital entered into a management service agreement with the Hospital to provide management services, including certain management, administrative and payroll related services for an initial period of five years, renewing automatically for one-year terms unless terminated by either party. Amounts paid to OE for these services were $8,542,708 and $7,902,659 for the years ended December 31, 2017 and 2016, respectively. Reimbursed expenses from OE amounted to $30,462 for the years ended December 31, 2017 and 2016. Amounts due from and to OE are reported in the accompanying consolidated balance sheets as other current assets or liabilities.

The Hospital subleases certain facilities from OI on the west and south sides of Indianapolis. The west and south side leases expire in 2023 and 2025, respectively, and provide annual rental payments of approximately $2,500,000. Lease expense recognized in 2017 and 2016 approximated $2,500,000 and $2,463,000, respectively.

NNS, LLC, a consolidated entity of the Hospital, owns certain property the Hospital rents for its use. The intercompany rent has been eliminated in the consolidated financial statements.

Note 9: Pension Plan

In March 2007, the Hospital joined the retirement benefit plan of OI. The plan provides for a matching component for up to 6% of the employees' salary and also allows a discretionary profit-sharing contribution from the Hospital. Substantially all of the Hospital's full-time employees are covered by the plan. Pension expense in 2017 and 2016 was $1,411,115 and $1,398,580, respectively.

Note 10: Commitments and Contingencies

Litigation

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Hospital's commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Hospital evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of ultimate expected loss, if any, for each of these matters. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

Self-Insurance of Employee Health Claims

The Hospital pools its share of health insurance claims with OI, a related party. Any such accrual is included in the related party accrual described in Note 8.

Note 11: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Allowance for Net Patient Service Revenue Adjustments

Estimates of allowances for adjustments included in net patient service revenue are described in Notes 1 and 2.

Malpractice Claims

Estimates related to the accrual for medical malpractice claims are described in Notes 1 and 4.

Admitting Physicians

The Hospital is served by a group of admitting and surgical physicians that comprise nearly 100% of the Hospital's net patient service revenue. The physician group is a related party of the Hospital through ownership as described in Note 8.

Note 12: Subsequent Events

Subsequent events have been evaluated through March 12, 2018, which is the date the consolidated financial statements were available to be issued.

Note 13: Future Change in Accounting Principle

Accounting for Leases

The Financial Accounting Standards Board amended its standard related to the accounting for leases. Under the new standard, lessees will now be required to recognize substantially all leases on the balance sheet as both a right-of-use asset and a liability. The standard has two types of leases for income statement recognition purposes: operating leases and finance leases. Operating leases will result in the recognition of a single lease expense on a straight-line basis over the lease term similar to the treatment for operating leases under existing standards. Finance leases will result in an accelerated expense similar to the accounting for capital leases under existing standards. The determination of lease classification as operating or finance will be done in a manner similar to existing standards. The new standard also contains amended guidance regarding the identification of embedded leases in service contracts and the identification of lease and nonlease components in an arrangement. The new standard is effective for annual periods beginning after December 15, 2019, and any interim periods within annual reporting periods that begin after December 15, 2019. The Hospital is evaluating the impact the standard will have on the consolidated financial statements; however, the standard is expected to have a material impact on the consolidated financial statements due to the recognition of additional assets and liabilities for operating leases.