



CONSOLIDATED FINANCIAL STATEMENTS

AND

SUPPLEMENTARY INFORMATION

DECEMBER 31, 2018 AND 2017

CPAs / ADVISORS



UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT AUDITORS

Board of Directors
Union Health System, Inc.
Terre Haute, Indiana

REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

We have audited the accompanying consolidated financial statements of Union Health System, Inc. and Subsidiaries (the System), which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

MANAGEMENT'S RESPONSIBILITY FOR THE 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; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States and Guidelines for Examination of Entities Receiving Financial Assistance from Governmental Sources, issued by the Indiana State Board of Accounts. Those standards require that we plan and perform the audits 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 System'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 System'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 Directors
Union Health System, Inc.
Terre Haute, 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 System as of December 31, 2018 and 2017, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

CHANGE IN ACCOUNTING PRINCIPLE

As discussed in Note 3 to the consolidated financial statements, effective January 1, 2018, the System adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2016-14, *Presentation of Financial Statement of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

REPORT ON SUPPLEMENTARY INFORMATION

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating balance sheets, consolidating statements of operations and changes in net assets, and consolidating statements of operations (Union Hospital, Inc. and Subsidiaries) information as listed in the accompanying table of contents is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations and changes in net assets of the individual entities, and is not a required part of the consolidated financial statements. The accompanying schedule of property and equipment of mortgagor and schedule of expenditures of federal awards, as required by Title 2 U.S. *Code of Federal Regulations (CFR) Part 200, Uniform Administrative requirements, Cost Principles, and Audit Requirements for Federal Awards*, are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Board of Directors
Union Health System, Inc.
Terre Haute, Indiana

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated April 16, 2019 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

Blue & Co., LLC

Indianapolis, Indiana
April 16, 2019

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2018 AND 2017

ASSETS	2018	Restated 2017
Current assets		
Cash and cash equivalents	\$ 71,169,772	\$ 51,095,248
Patient accounts receivable, net	55,567,042	67,525,612
Inventories	5,773,542	5,890,533
Prepaid expenses and other current assets	18,621,601	16,439,814
Total current assets	151,131,957	140,951,207
Investments limited as to use		
Funds held by trustee	7,127,367	3,939,955
Board designated	67,545,798	60,155,430
Total investments limited as to use	74,673,165	64,095,385
Property and equipment		
Land and improvements	38,280,140	37,685,526
Buildings and fixed equipment	376,979,879	369,366,453
Movable equipment	178,519,398	168,528,589
	593,779,417	575,580,568
Less allowances for depreciation	323,714,223	299,461,001
	270,065,194	276,119,567
Construction in progress	486,164	7,851,065
Total property and equipment, net	270,551,358	283,970,632
Other assets		
Due from Union Health Foundation, Inc.	3,650,489	3,187,376
Intangible assets, net and other	3,616,958	5,541,838
Investment in joint ventures	6,253,946	4,312,532
	13,521,393	13,041,746
Total assets	\$ 509,877,873	\$ 502,058,970

See accompanying notes to consolidated financial statements.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2018 AND 2017

LIABILITIES AND NET ASSETS

	2018	Restated 2017
Current liabilities		
Accounts payable and other current liabilities	\$ 32,710,278	\$ 43,030,398
Salaries, wages and related liabilities	34,949,425	30,549,746
Estimated third party settlements	1,577,262	2,142,902
Current portion of long-term debt	9,289,113	10,600,023
Total current liabilities	<u>78,526,078</u>	<u>86,323,069</u>
Long-term liabilities		
Long-term debt, less current portion	262,724,862	271,670,593
Other long-term liabilities	85,985	294,236
Total long-term liabilities	<u>262,810,847</u>	<u>271,964,829</u>
Total liabilities	341,336,925	358,287,898
Net assets		
Without donor restrictions	163,173,698	139,165,226
Noncontrolling interests in UHT, LLC	510,306	529,695
Total net assets without donor restrictions	<u>163,684,004</u>	<u>139,694,921</u>
With donor restrictions	4,856,944	4,076,151
Total net assets	<u>168,540,948</u>	<u>143,771,072</u>
Total liabilities and net assets	<u>\$ 509,877,873</u>	<u>\$ 502,058,970</u>

See accompanying notes to consolidated financial statements.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	Restated 2017
Operating revenue		
Net patient service revenue (net of contractual allowances and discounts including financial assistance provisions of \$16,728,292 and \$18,363,848 in 2018 and 2017, respectively)	\$ 552,927,027	\$ 525,204,201
Less provision for bad debts	39,090,678	28,805,557
Net patient service revenue net of provision for bad debts	513,836,349	496,398,644
Other revenue	23,747,855	15,782,339
Total operating revenue	537,584,204	512,180,983
Operating expenses		
Physician, mid-level, and other provider salaries and wages	54,445,224	54,119,056
Other salaries and wages	113,289,777	101,541,697
Employee benefits	31,578,198	38,494,094
Medical supplies and drugs	92,093,272	89,553,730
Physician services	20,908,226	19,373,250
Contract services	97,750,260	94,590,035
Rent and leases	10,227,420	11,109,134
Utilities, supplies, and other	34,511,414	34,939,887
Hospital assessment fee	21,906,132	16,853,726
Depreciation and amortization	26,347,834	21,519,114
Interest	12,939,582	13,737,220
Total operating expenses	515,997,339	495,830,943
Income from operations before pension termination	21,586,865	16,350,040
Pension termination	-0-	48,909,624
Income (loss) from operations after pension termination	21,586,865	(32,559,584)
Non-operating gains (losses)		
Investment income, net	2,227,046	5,460,047
Other	5,945,228	2,834,231
Total non-operating gains (losses)	8,172,274	8,294,278
Excess of revenue over (under) expenses	29,759,139	(24,265,306)
Other changes in net assets without donor restrictions		
Pension related changes other than net pension cost	-0-	44,826,541
Distribution to non-controlling interests	(1,450,729)	(1,505,038)
Net unrealized gain (loss) on investments	(4,324,417)	69,880
Net assets released for property and equipment	5,090	424,207
Change in net assets without donor restrictions	23,989,083	19,550,284
Net assets with donor restrictions		
Other changes in receivable from Union Health Foundation, Inc.	785,883	1,302,688
Net assets released for property and equipment	(5,090)	(424,207)
Change in net assets with donor restrictions	780,793	878,481
Change in net assets	24,769,876	20,428,765
Net assets		
Beginning of year	143,771,072	123,342,307
End of year	\$ 168,540,948	\$ 143,771,072

See accompanying notes to consolidated financial statements.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
Operating activities		
Change in net assets	\$ 24,769,876	\$ 20,428,765
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation	24,320,222	20,029,052
Amortization of intangible asset	2,027,612	1,490,062
Amortization of bond issuance costs	307,285	315,968
Provision for bad debts	39,090,678	28,805,557
Distribution to non-controlling interests	1,450,729	1,505,038
(Gain) loss on property disposals	82,447	(566,343)
Net unrealized (gain) loss on investments	4,324,417	(69,880)
Changes in operating assets and liabilities		
Patient accounts receivable	(27,132,108)	(39,280,610)
Other current and noncurrent assets	(4,572,055)	(4,767,415)
Accounts payable and other current liabilities	(10,350,295)	(528,154)
Salaries, wages and related liabilities	4,399,679	(2,185,832)
Other long-term liabilities	(208,251)	(9,670,015)
Estimated third-party payor settlements	(565,640)	(2,818,072)
Net cash flows from operating activities	57,944,596	12,688,121
Investing activities		
Purchases of property and equipment	(10,965,607)	(27,316,633)
Proceeds from sale of property and equipment	12,387	1,484,637
Purchase of investments	(26,227,198)	(48,159,073)
Proceeds from sale of investments	11,325,001	54,907,017
Net cash flows from investing activities	(25,855,417)	(19,084,052)
Financing activities		
Payments on long-term debt	(10,586,209)	(8,402,317)
Proceeds from long-term debt	22,283	31,443
Distribution to non-controlling interests	(1,450,729)	(1,505,038)
Net cash flows from financing activities	(12,014,655)	(9,875,912)
Change in cash and cash equivalents	20,074,524	(16,271,843)
Cash and cash equivalents		
Beginning of year	51,095,248	67,367,091
End of year	\$ 71,169,772	\$ 51,095,248
Noncash investing activities		
Capital acquisitions included in accounts payable	\$ 30,175	\$ 31,247
Financed acquisition of medical practice service line	\$ -0-	\$ 3,330,000
Supplemental cash flow information		
Cash paid for interest	\$ 12,632,297	\$ 13,421,252

See accompanying notes to consolidated financial statements.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

1. ORGANIZATION

Nature of Operations

Union Health System, Inc. (UHS), an Indiana nonprofit corporation, is the sole member of Union Hospital, Inc. (the Corporation). UHS and the Corporation are 50% members of Union Associated Physicians Clinic, LLC (UAPC). UHS, UAPC, and the Corporation are collectively referred to as the System. The System was formed in November 2009 to provide vision and strategic direction in the formation of a regional health care system to expand and improve the delivery of health care services in order to meet the health care needs of residents in the System's service area.

The Corporation is an Indiana not-for-profit corporation, which owns and operates Union Hospital (the Hospital), a 278 staffed-beds and regional referral center hospital located in Terre Haute, Indiana. The Hospital is a full-service, acute-care hospital with medical-surgical, obstetric, pediatric, coronary care, post-coronary care, intensive care, maximum care, and medical rehabilitation units. Additionally, as the largest hospital in west central Indiana, the Hospital is a referral center for such services as its newborn intensive care unit (Level II), open heart surgery, cardiac rehabilitation clinic, radiology, non-invasive cardiology services, cardiopulmonary services, and radiation therapy. The Hospital and its related consolidated entities provide comprehensive health care services to the residents of Terre Haute and the surrounding communities, west central Indiana, and east central Illinois through its acute, specialty care facilities, and physician medical practices.

UAPC is an Indiana, not-for-profit, limited liability company, which operates a multi-specialty physician clinic and consists of approximately 115 physicians and allied health professionals.

The consolidated financial statements include the accounts of UHS, the Corporation, IPACS, Inc. (IPACS), Center for Occupational Health (COH), Union Hospital Therapy, LLC (UHT) and UAPC (collectively, the System). Union Hospital Clinton is a designated Medicare critical access hospital operating as a division of the Corporation. IPACS is a wholly owned, taxable subsidiary of the Corporation engaged in providing collection services to hospitals, hospital physicians, and other health care providers. COH provides work related injury care and other occupational medicine services and is also a wholly owned tax-exempt subsidiary of the Corporation. All material intercompany accounts and transactions have been eliminated.

During 2014, UHT was formed for the purpose of providing physical, occupational, and speech therapy, and related rehabilitation services. The Corporation ownership interest in UHT is 51%. The Corporation maintains substantial participation in the operations of UHT in addition to an economic interest in UHT's financial position. The 49% non-controlling interest is owned by Clinical Management Solutions, LLC. All material intercompany accounts and transactions have been eliminated.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

The System is also related to various organizations principally through overlapping board membership, which does not constitute control. These organizations include Union Health Foundation, Inc., Union Hospital Health Services, Inc., and Visiting Nurse Association of the Wabash Valley, Inc. The majority of all fund-raising activities are conducted by Union Health Foundation, Inc. (the Foundation).

Accordingly, unrestricted gifts and bequests received without donor restrictions directly by the System are recorded as nonoperating gains, and restricted gifts and bequests received by the Foundation for the benefit of the Corporation are recorded by the Corporation as net assets with donor restrictions until expended by the System for their intended purpose.

2. SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

All significant intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of the consolidated 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, including the allowance for estimated uncollectible accounts and estimated third-party payor settlements, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period and could differ from actual results.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with a maturity of three months or less when purchased, excluding investments limited as to use. The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents approximate fair value.

Patient Accounts Receivable, Estimated Third Party Settlements, and Net Patient Service Revenue

Patient accounts receivable and net patient service revenue are reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered. Net patient service revenue includes estimated retroactive adjustments under reimbursement agreements with certain third-party payors (principally for the Medicare program). Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered, adjusted in future periods as final settlements are determined, and are included with estimated receivables from third-party payors.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

A reconciliation of the amount of services provided to patients at established rates to net patient service revenue as presented in the consolidated statements of operations and changes in net assets follows:

	2018	2017
Inpatient revenue	\$ 506,447,541	\$ 517,272,164
Outpatient revenue	992,290,657	910,455,690
Physician revenue	128,040,613	128,986,555
Gross patient revenue	1,626,778,811	1,556,714,409
Financial assistance revenue foregone	16,728,292	18,363,848
Contractual adjustments	1,057,123,492	1,013,146,360
Total adjustments	1,073,851,784	1,031,510,208
Net patient service revenue	552,927,027	525,204,201
Less provision for bad debts	39,090,678	28,805,557
	\$ 513,836,349	\$ 496,398,644

A summary of gross patient service revenue at established rates by payor source for 2018 and 2017, respectively, is as follows:

	2018	2017
Medicare	51%	50%
Medicaid	18%	19%
Managed care and commercial insurance	28%	28%
Self-pay and other	3%	3%
	100%	100%

There is a single insurance and managed care provider that constituted 17% of patient service revenue at established rates for the years ended December 31, 2018 and 2017.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the System analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources 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 System 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 payor has not yet paid, or for payors 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 System 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.

During 2018, the System's allowance for uncollectible accounts for patient and physician services increased approximately \$6,300,000 from approximately \$24,200,000 in 2017 to approximately \$30,500,000. This increase is due to revenue growth and a continued shift in accounts receivable payor mix. During 2017, the System's allowance for uncollectible accounts for patient and physician services increased approximately \$6,000,000 from approximately \$18,200,000 to approximately \$24,200,000. As of December 31, 2018 and 2017, respectively, the allowance for uncollectible accounts of \$30,500,000 and \$24,200,000 was comprised of approximately \$15,500,000 and \$11,000,000 reserved for self-pay balances and approximately \$15,000,000 and \$13,200,000 reserved for third-party payor balances.

The System grants credit to patients, substantially all of whom are local residents of the communities served. The System does not generally require credit or other collateral or other security in extending credit to patients; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies (e.g., Medicare, Medicaid, health maintenance organizations, and commercial insurance policies). The System has not changed its financial assistance or uninsured discount policies during 2018 or 2017.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

At December 31, 2018 and 2017, gross accounts receivable from patients and third party were comprised of the following:

	2018	2017
Medicare	31%	33%
Medicaid	19%	21%
Managed care and commercial insurance	36%	33%
Self-pay and other	14%	13%
	<u>100%</u>	<u>100%</u>

The allowance for doubtful accounts is based on management's assessment of historical and expected net collections considering business and economic conditions, trends in health care coverage, and other collection indicators. Periodically throughout the year, management assesses the adequacy for uncollectible receivables based upon the payor composition and aging of receivables as of the reporting date with consideration of the historical write-off experience by payor category. The results of these reviews are then used to make any modifications to the provision for uncollectible receivables to establish an appropriate allowance for uncollectible receivables. After satisfaction of amounts due from insurance, the System follows established guidelines for placing past-due patient accounts with collection agencies.

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

Medicare: Physician services, inpatient acute care services, and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Critical access hospital services are reimbursed based on cost reimbursement methodologies. Cost reimbursable services are reimbursed at a tentative rate with final settlement determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary.

Medicaid: Reimbursement for services rendered to Medicaid program beneficiaries are at prospectively determined rates per discharge for inpatient hospital services. Other services are reimbursed based on a combination of cost reimbursement methodologies and prospectively determined rates.

Other: Reimbursement for services to certain patients is received from commercial insurance carriers, health maintenance organizations, preferred provider organizations, and other payors, based on prospectively determined rates per discharge or discount of charges for inpatient hospital services and discount of charges for outpatient services.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimated settlements could change by a material amount in the near term.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Management believes that adequate provisions have been made for any adjustments, which may result from such final settlements. Differences between prior estimates and subsequent actual settlements are immaterial to these financial statements for 2018 and 2017.

Financial Assistance and Community Benefit

Patients are provided care regardless of their ability to pay in accordance with financial assistance policies of the System. These policies define financial assistance services as those services for which no or reduced payment is anticipated and are based on federal poverty income levels and certain other factors. Because collection of amounts determined to qualify as financial assistance is not pursued, such amounts are not reported as revenue.

Of the System's total expenses reported, an estimated \$5,855,000 and \$7,228,000 arose from providing services to patients requiring financial assistance during the years ended December 31, 2018 and 2017, respectively. The estimated costs of providing patient assistance services are based on a calculation, which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to patients requiring financial assistance. The ratio of cost to charges is calculated based on the System's total expenses divided by gross patient service revenue.

The System also provides programs and services to address the needs of the communities it serves, generally at no, or low, cost to those being served. Specific community needs being addressed by the System include, among others, low-weight births and infant mortality, high incidence of, and deaths from, certain diseases and chronic illnesses, underserved populations, adequacy of the supply of physicians and other health care providers, and certain behavioral risk factors. The System's programs and services include, among others, services to low-income women in need of prenatal care, health screenings for underserved women, wellness and injury prevention programs, chronic disease management assistance, educational programs, rural health care access and availability initiatives, transportation services for elderly and low-income patients, and access to support groups for critically and chronically ill patients and their families. Assistance is also provided to senior citizens, other patients, and their families for the submission of forms for insurance, financial counseling, and application to the Medicare and Medicaid programs for health service coverage. The System periodically reviews, modifies, and reports on its community health assessment and plan of action for the communities served.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Hospital Assessment Fee (HAF) Program

The purpose of the HAF Program is to fund the state share of enhanced Medicaid payments and Medicaid Disproportionate Share (DSH) payments for Indiana inpatient providers. Previously, the state share was funded by governmental 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 patients and result in increased Medicaid rates.

During the years ended December 31, 2018 and 2017, the System recognized HAF Program expense of approximately \$21,900,000 and \$16,900,000, respectively, which resulted in increased Medicaid reimbursement. The HAF Program expense is included in the consolidated statements of operations and changes in net assets as an operating expense. The Medicaid rate increases under the HAF Program are included in net patient service revenue in the consolidated statements of operations and changes in net assets.

Inventories

Inventories, consisting primarily of medical supplies and pharmaceuticals, are stated at the lower of cost or market and principally valued using the average cost method.

Investments Limited as to Use

Investments limited as to use are stated at fair value. The fair value of assets is based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. The cost of securities sold is based on the specific identification method. Dividends and interest income, realized gains and losses on sales of investments, and investment expenses are recorded as investment income within non-operating gains (losses) in the consolidated statements of operations and changes in net assets. Unrealized gains (losses) and temporary appreciation (temporary losses) of investments are reported as other changes in net assets without donor restrictions in the consolidated statements of operations and changes in net assets.

Investments are generally commingled for investment purposes and consist of short-term investments (principally money market deposit accounts), U.S. government obligations, mutual funds, corporate obligations, common stocks, and commingled funds.

Investments limited as to use include investments set aside by the Board of Directors for future capital improvements and retirement of debt over which the Board of Directors retains control and may, at its discretion, subsequently use for other purposes; and investments held by trustees under bond indenture agreements; and donor-restricted funds. Amounts that are required for obligations classified as current liabilities, and other amounts previously paid from operating cash that are to be reimbursed by the applicable funds, are reported in current assets.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Property and Equipment

Property and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the assets. The estimated useful lives are as follows: land improvements 3 to 30 years, buildings 5 to 40 years, and equipment 3 to 25 years. The System's policy is to designate certain available net assets without donor restrictions for expansion and renovation.

Equipment under capital lease obligations is amortized on the straight-line method over the lease term or the estimated useful life of the equipment, whichever period is shorter. Such amortization is included with depreciation and amortization in the consolidated statements of operations and changes in net assets. Interest cost incurred on borrowed funds during the period of construction and other interest costs are capitalized as a component of the cost of constructing the assets. Repair and maintenance costs are expensed when incurred.

The System periodically evaluates whether circumstances have occurred that would indicate whether the remaining estimated useful life of long-lived assets may warrant revision or that the remaining balance of such assets may not be recoverable. When factors indicate that such assets should be evaluated for possible impairment, an estimate is made of the undiscounted cash flows over the remaining life of the assets in measuring whether the asset is recoverable in accordance with accounting standards.

Intangible Assets

Intangible assets arising from the purchase of physician practices (primarily non-compete provisions) and service lines are carried at cost. Amortization is computed using the straight-line method based on the assets' estimated useful lives. During 2018 and 2017, the System purchased targeted service lines for approximately \$-0- and \$3,300,000, respectively. As of December 31, 2018 and 2017, intangible assets approximated \$2,737,000 and \$4,764,000, respectively, and recorded within intangible assets, net and other on the consolidated balance sheets. The System expects future amortization as follows:

Year Ending December 31,	
2019	\$ 1,241,808
2020	832,500
2021	662,382
	<u>\$ 2,736,690</u>

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Unamortized Debt Issuance Costs

Costs incurred in connection with the issuance of long-term debt are amortized using the bonds outstanding method, which approximates the amortization under the effective interest rate method, and are included in interest expense in the accompanying consolidated statements of operations and changes in net assets. The unamortized debt issuance costs are included in the consolidated balance sheets as a reduction in related long-term debt.

Medical Malpractice Insurance

The System has a self-insurance plan for professional liability insurance. A third-party claims administrator has been retained to process all benefit claims. Claims are processed and presented for payment upon occurrence. The System makes periodic deposits into a trust fund for the proper administration and protection of the fund.

The Indiana Medical Malpractice Act, IC 34-18 (the Act) provides a maximum recovery of \$1,650,000 for an occurrence of malpractice until June 30, 2019, and \$1,800,000 thereafter. The Act requires the System to maintain medical malpractice liability insurance in the amount of at least \$400,000 per occurrence and \$12,000,000 in the annual aggregate until June 30, 2019. Starting July 1, 2019, the Act will require the System to maintain medical malpractice liability insurance in the amount of at least \$500,000 per occurrence and \$15,000,000 in the annual aggregate. The Act also requires the System to pay a surcharge to the State Patient's Compensation Fund (Fund). The Fund is used to pay medical malpractice claims in excess of per occurrence and the annual aggregate amounts as noted above, under certain terms and conditions. No accrual for possible losses attributable to incidents that may have occurred but that have not been identified has been made because the amount, if any, is not reasonably estimable. The Fund is on a claims-made basis and as long as this coverage is continuous or replaced with equivalent insurance, claims based on occurrences during its term but reported subsequently will be insured.

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 System's claim experience, an accrual for estimated malpractice claims costs was approximately \$1,497,000 as of December 31, 2018 and 2017. It is reasonably possible that this estimate could change materially in the near term.

The System also provides medical malpractice insurance for its employed physicians who practice in the state of Illinois with limits of \$1,000,000 per occurrence and \$3,000,000 in the aggregate.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Malpractice insurance coverage provided through the Compensation Fund and the captive insurance company is provided on a claims-made basis. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term but reported subsequently will be uninsured.

Pension Plans

A noncontributory, defined-benefit pension plan covers substantially all employees. Plan benefits are based on years of service and the employee's compensation. During 2010, the Corporation froze the defined benefit plan and initiated a discretionary match component to the 403b defined contribution plan. UAPC has established an employer match, safe harbor 401k and profit sharing plan for certain employees based on eligibility requirements including annual hours of service and designated plan entry dates. See Note 11 for additional details on the System's pension plans.

Net Assets and Financial Statement Presentation

The System is required to report information regarding its financial position and activities according to two classes of net assets (net assets without donor restrictions and net assets with donor restrictions) based upon the existence or absence of donor imposed restrictions.

Net assets without donor restrictions represent the part of the net assets of the System that is not restricted by donor-imposed stipulations. Net assets with donor restrictions are those assets whose use by the System has been limited by donors primarily for a specified time period or purpose. When a donor restriction expires or is met, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statements of operations and changes in net assets as net assets released for property and equipment. Property and equipment donated to the Hospital are recorded as additions to net assets with donor restrictions at their fair value at the date of receipt and as a transfer to net assets without donor restrictions when the assets are placed in service. Net assets with donor restrictions include approximately \$3,650,000 and \$3,187,000 of funds held by the Foundation for the benefit of the System at December 31, 2018 and 2017, respectively. These amounts represent planned contributions of property and equipment received on behalf of the System by the Foundation and other amounts the Foundation has granted to the System and are included within Due from Union Health Foundation Inc. on the consolidated balance sheets. Other miscellaneous funds are held as net assets with donor restrictions in the approximate amounts of \$1,207,000 and \$889,000 as of December 31, 2018 and 2017, respectively, and held for future capital improvements.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Health Insurance

The System's employee health care insurance is provided through a combination of self-insurance and purchased re-insurance coverage from a commercial carrier. The System maintains an estimated liability for the amount of claims incurred but not reported. Substantially all employees are covered for major medical benefits. For the Corporation, the specific annual attachment point for an individual is \$325,000 with no policy period maximum. There is no aggregate limit on claims for the Corporation. For UAPC, the specific annual attachment point for an individual is \$300,000 with no lifetime maximum on claims. The maximum annual aggregate reimbursement under the policy is \$1,000,000 per year.

Income Taxes

UHS and the Corporation are organized as not-for-profit corporations under Section 501(c) (3) of the United States Internal Revenue Code. Effective January 1, 2018, UAPC was granted exemption from income taxes under Section 501(c) (3) as a not-for-profit limited liability company. Prior to receiving this exemption, UAPC was a limited liability company, whereby net taxable income is taxed directly to the members of the limited liability company. As such, UHS, the Corporation, and UAPC are generally exempt from income taxes. However, these entities are required to file Federal Form 990 – Return of Organization Exempt from Income Tax, which is an informational return only.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by UHS, the Corporation, and UAPC, and recognize a tax liability if UHS, the Corporation, and UAPC have taken an uncertain 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 UHS, the Corporation, and UAPC, and has concluded that as of December 31, 2018 and 2017, 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. UHS, the Corporation, and UAPC are subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. Filings are current through 2017. The impact of the subsidiaries tax consequences is immaterial to these consolidated financial statements.

Operating Indicator

The System's operating indicator, income (loss) from operations after pension termination, includes all unrestricted net income, gains and support, and expenses from System operations directly related to recurring and ongoing health care operations during the reporting period. The operating indicator excludes net investment income and gains and losses deemed by management not to be directly related to providing health care services.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Performance Indicator

The System's performance indicator, excess of revenues over (under) expenses, includes all changes in net assets without donor restrictions other than net unrealized gain (loss) and temporary gains (losses) on investments, investment returns restricted by donors, changes in pension plan funded status, distributions to non-controlling owners, and contributions of property and equipment.

Going Concern Evaluation

Management evaluates whether there are conditions or events that raise substantial doubt about the entity's ability to continue as a going concern for a period of one year from the date the consolidated financial statements are available to be issued.

Reclassifications

Certain amounts from the 2017 consolidated financial statements have been reclassified to conform to the current year presentation. The reclassifications did not impact previously reported net assets or changes in net assets.

Subsequent Events

The System has evaluated events or transactions occurring subsequent to the balance sheet date for recognition and disclosure in the accompanying consolidated financial statements through the date the consolidated financial statements are available to be issued which is April 16, 2019.

Recently Issued Accounting Standards

On May 28, 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The core principle of this new guidance is that "an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services". On August 12, 2015, the FASB further amended this guidance and issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606)*, which deferred the effective date for all entities by one year. These new standards, which the System is not required to adopt until its year ending December 31, 2019, deal with the timing of reporting revenues from contracts with customers, and disclosures related thereto.

On February 25, 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. This new standard, which the System is not required to adopt until its fiscal year ending December 31, 2020, is intended to improve financial reporting about leasing transactions by requiring entities that lease assets to recognize on their balance sheet the assets and liabilities for the rights and obligations created by those leases, and to provide additional disclosures regarding the leases. Leases with terms (as defined in the ASU) of twelve months or less are not required to be reflected on an entity's balance sheet.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

On June 21, 2018, FASB issued ASU 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The amendments in this ASU clarify and improve current guidance about whether a transfer of assets (or the reduction, settlement, or cancellation of liabilities) is a contribution or an exchange transaction. The amendments clarify how an entity determines whether a resource provider is participating in an exchange transaction by evaluating whether the resource provider is receiving commensurate value in return for the resources transferred. Additionally, the amendments in this ASU require that an entity determine whether a contribution is conditional on the basis of whether an agreement includes a barrier that must be overcome and either a right of return of assets transferred or a right of release of a promisor's obligation to transfer assets. Finally, ASU 2018-08 amends the "simultaneous release accounting policy" to allow a not-for-profit entity to recognize a restricted contribution directly in unrestricted net assets/net assets without donor restrictions if the restriction is met in the same period that revenue is recognized. The System will be required to adopt this new standard in the year ending December 31, 2019.

The System is presently evaluating the effects that these ASUs will have on its future financial statements, including related disclosures.

3. CHANGE IN ACCOUNTING PRINCIPLE

Effective January 1, 2018, the System adopted FASB ASU No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. The ASU simplifies and improves how a not-for-profit organization classifies its net assets, as well as information it presents in the financial statements and notes about its liquidity, financial performance and cash flows. The System has adjusted the presentation of its 2018 financial statements herein and retrospectively restated the prior year financial statements. In addition to changes in terminology used to describe categories of net assets throughout the financial statements, new disclosures were added regarding net assets with donor restrictions (Note 8), liquidity and availability of resources (Note 14), board-designated net assets (Note 15), and disclosures related to the functional allocation of expenses were expanded (Note 16).

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

The impact of the adoption of ASU No. 2016-14 on the System's net assets is as follows:

Consolidated Balance Sheet	Previously Reported 12/31/17	Adjustment	Restated 12/31/17
Net assets			
Unrestricted net assets	\$ 139,694,921	\$ (139,694,921)	\$ -0-
Temporarily restricted net assets	4,076,151	(4,076,151)	-0-
Without donor restrictions	-0-	139,694,921	139,694,921
With donor restrictions	-0-	4,076,151	4,076,151
Total net assets	<u>\$ 143,771,072</u>	<u>\$ -0-</u>	<u>\$ 143,771,072</u>

Consolidated Statement of Operations and Changes in Net Assets	Previously Reported 12/31/17	Adjustment	Restated 12/31/17
Change in unrestricted net assets	\$ 19,550,284	\$ (19,550,284)	\$ -0-
Change in temporarily restricted net assets	878,481	(878,481)	-0-
Change in net assets without donor restrictions	-0-	\$ 19,550,284	19,550,284
Change in net assets with donor restrictions	-0-	878,481	878,481
Total change in net assets	<u>\$ 20,428,765</u>	<u>\$ -0-</u>	<u>\$ 20,428,765</u>

There was no significant impact to the consolidated statement of cash flows as a result of adopting this ASU.

4. AFFILIATED ENTITY AND RELATED PARTY TRANSACTIONS

The System contracts with AP&S Clinic for management services, which are provided to UAPC and the Corporation. Management expenses totaled approximately \$23,525,000 and \$28,938,000 for the years ended December 31, 2018 and 2017, respectively, and are included in contract services in the consolidated statements of operations and changes in net assets. Effective July 31, 2018, AP&S Clinic transferred its operations and staffing to UAPC. At December 31, 2018 a net receivable is owed from the AP&S Clinic to the System in the amount of approximately \$120,000. At December 31, 2017, a net payable is owed from the System to AP&S Clinic in the amount of approximately \$4,402,000. Balances as of 2018 and 2017 are reflected in accounts payable and other current liabilities in the consolidated balance sheets.

UAPC paid approximately \$3,023,000 and \$2,947,000 during 2018 and 2017, respectively, in rental expense to AP&S II, a related real estate entity. UAPC entered into a capital lease arrangement during 2013 with AP&S III, a related real estate entity where total payments from UAPC to AP&S III during the years ended December 31, 2018 and 2017 totaled approximately \$1,900,000, respectively. This capital lease is included within capital leases and other in Note 9.

UAPC is related to AP&S Clinic, AP&S II, and AP&S III as some physicians employed by UAPC have ownership interests in AP&S Clinic, AP&S II, and AP&S III.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

The Corporation provided management and other services for the Foundation and other related organizations for the years ended December 31, 2018 and 2017. These amounts are immaterial to the financial statements as a whole.

The Corporation received approximately \$282,000 and \$419,000 in contributions from the Foundation for the years ended December 31, 2018 and 2017, respectively. These amounts are recorded within other revenue in the consolidated statements of operations and changes in net assets.

UAPC participates in a joint venture, Oncology Services Group, LLC (OSG). The Corporation contracts with OSG to provide staffing related to oncology and chemotherapy. These expenses totaled approximately \$3,000,000 and \$2,823,000 for the years ended December 31, 2018 and 2017, respectively, and are included in contract services in the consolidated statements of operations and changes in net assets. At December 31, 2018 and 2017, the Corporation had a payable in the amount of \$80,000 and \$343,000, respectively, reflected in accounts payable and other current liabilities in the consolidated balance sheets.

UAPC participates in a joint venture, Ambulatory Surgery Management Services, LLC (ASMS II). The System contracts with ASMS II to provide staffing related to ambulatory surgery. These expenses totaled approximately \$6,377,000 and \$6,387,000 for the years ended December 31, 2018 and 2017, respectively, and are included in contract services in the consolidated statements of operations and changes in net assets. At December 31, 2018 and 2017, the System had a receivable in the approximate amount of \$104,000 reflected in prepaid expenses and other current assets and a payable in the approximate amount of \$551,000 reflected in accounts payable and other current liabilities in the consolidated balance sheets, respectively.

UAPC participates in a joint venture, Cardiovascular Management, LLC (CVM). The Corporation contracts with CVM to provide equipment, supplies and staffing related to certain cardiology services. These expenses totaled approximately \$27,229,000 and \$17,241,000 for the years ended December 31, 2018 and 2017, respectively, and are included in contract services in the consolidated statements of operations and changes in net assets. At December 31, 2018 and 2017, the Corporation had a payable in the approximate amounts of \$2,601,000 and \$1,874,000, respectively, reflected in accounts payable and other current liabilities in the consolidated balance sheets.

At December 31, 2018 and 2017, the Corporation had a payable to CVM in the amount of \$3,494,000 and \$1,319,000, respectively, reflected in accounts payable and other current liabilities in the consolidated balance sheets for quality incentive bonuses accrued for its physicians.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

5. CONSTRUCTION-IN-PROGRESS

A summary of the construction-in-progress projects at December 31, 2018 and 2017 is as follows:

	2018	2017
Non-Invasive Cardio Project	\$ -0-	\$ 4,363,588
Nuclear Med Project	-0-	2,048,296
Chiller Phase III	313,332	-0-
Clinical Decision Unit	45,618	-0-
Other renovations and upgrades	127,214	1,439,181
	\$ 486,164	\$ 7,851,065

At December 31, 2018, the System has outstanding commitments related to property and equipment of approximately \$2,040,000.

6. INVESTMENTS

The Corporation does not engage in trading activities for investment purposes. The composition of investments, at fair value, is set forth in the following table:

	2018	2017
Money market deposit accounts	\$ 7,093,826	\$ 956,640
US Government obligations	10,161,701	7,459,170
Mutual funds	34,869,579	32,415,132
Common stocks	8,720,823	8,613,379
Corporate obligations	4,499,832	3,616,499
Commingled funds	9,327,404	11,034,565
	\$ 74,673,165	\$ 64,095,385

Investment income, net included in the consolidated statements of operations and changes in net assets is primarily comprised of interest, dividends, realized gains and losses on sale of investments, and investment expenses.

	2018	2017
Investment income included within non-operating gains (losses)		
Investment income, net	\$ 2,227,046	\$ 5,460,047
Other changes in net assets:		
Unrealized gain (loss) on investments	(4,324,417)	69,880
	\$ (2,097,371)	\$ 5,529,927

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

The following schedule summarizes the fair value of securities included in investments for board designated and held by trustee that have gross unrealized losses (the amount by which historical cost exceeds the fair value) as of December 31, 2018 and 2017. The schedule further segregates the securities that have been in a gross unrealized position as of December 31, 2018 and 2017, for less than twelve months and those for twelve months or more. The gross unrealized losses of less than twelve months are a reflection of the normal fluctuations of the market and are therefore considered temporary. The gross unrealized losses of twelve months or longer are reflective of current market fluctuations. The majority of the decline is attributable to several securities which industry experts expect recovery in the short-term future.

The decline in value is determined by management to be temporary, and unrealized losses have not been reclassified to realized losses as of December 31, 2018 and 2017:

Description of securities	December 31, 2018					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Common stocks	\$ 4,076,941	\$ 821,326	\$ 920,249	\$ 369,590	\$ 4,997,190	\$ 1,190,916
Mutual funds	14,113,277	817,525	15,164,933	1,208,633	29,278,210	2,026,158
US Government obligations	760,700	6,717	3,948,236	64,668	4,708,936	71,385
Corporate obligations	1,377,344	37,367	2,660,879	94,037	4,038,223	131,404
Total temporarily impaired securities	<u>\$ 20,328,262</u>	<u>\$ 1,682,935</u>	<u>\$ 22,694,297</u>	<u>\$ 1,736,928</u>	<u>\$ 43,022,559</u>	<u>\$ 3,419,863</u>

Description of securities	December 31, 2017					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Common stocks	\$ 1,608,039	\$ 140,256	\$ -0-	\$ -0-	\$ 1,608,039	\$ 140,256
Mutual funds	137,625	1,310	17,107,301	572,105	17,244,926	573,415
US Government obligations	6,429,444	54,384	-0-	-0-	6,429,444	54,384
Corporate obligations	3,568,220	30,732	-0-	-0-	3,568,220	30,732
Total temporarily impaired securities	<u>\$ 11,743,328</u>	<u>\$ 226,682</u>	<u>\$ 17,107,301</u>	<u>\$ 572,105</u>	<u>\$ 28,850,629</u>	<u>\$ 798,787</u>

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

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 markets 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 System has the ability to access.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

- 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 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 as of December 31, 2018 and 2017.

- *Common stocks*: Valued at the closing price reported on the active market on which the individual securities are traded.
- *Mutual funds*: Valued at the daily closing price as reported by the fund. Mutual funds held by the System 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 (NAV) and to transact at that price. The mutual funds held by the System are deemed to be actively traded.
- *US Government obligations*: Valued based upon the active market on which the individual securities are traded.
- *Corporate obligations*: 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.
- *Commingled funds*: Valued at the NAV of units as reported by the fund. The NAV, as provided by the investment manager, is used as a practical expedient to estimate fair value. The NAV is based on the fair value of the underlying investments held by the fund less its liabilities. Due to the nature of the investments held by the fund, changes in market conditions and the economic environment may significantly impact the NAV of the fund and, consequently, the fair value of the System's interests in the funds. Although a secondary market exists for these investments, it is not active and individual transactions are typically not observable. When transactions do occur in this limited secondary market, they may occur at discounts to the reported NAV. It is therefore reasonably possible that if the System were to sell these investments in the secondary market, a buyer may require a discount to the reported NAV, and the discount could be significant.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

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- *Money market mutual funds:* Valued based at the subscription and redemption activity at a \$1 stable NAV. However, on a daily basis the funds are valued at their daily NAV calculated using the amortized cost of the securities.

Assets measured at fair value on a recurring basis as of December 31, 2018 and 2017 are as follows:

	December 31, 2018			
	Total	Level 1	Level 2	Level 3
Investments limited as to use				
Common stocks				
Communications	\$ 275,480	\$ 275,480	\$ -0-	\$ -0-
Consumer	1,304,494	1,304,494	-0-	-0-
Energy	1,205,351	1,205,351	-0-	-0-
Financial	1,566,347	1,566,347	-0-	-0-
Healthcare	1,326,892	1,326,892	-0-	-0-
Industrials	1,059,871	1,059,871	-0-	-0-
Information technology	1,242,461	1,242,461	-0-	-0-
Materials	739,927	739,927	-0-	-0-
Total common stocks	<u>8,720,823</u>	<u>8,720,823</u>	<u>-0-</u>	<u>-0-</u>
Mutual funds				
Fixed income funds	15,164,933	15,164,933	-0-	-0-
Large cap funds	13,757,111	13,757,111	-0-	-0-
International funds	5,892,050	5,892,050	-0-	-0-
Index funds	55,485	55,485	-0-	-0-
Total mutual funds	<u>34,869,579</u>	<u>34,869,579</u>	<u>-0-</u>	<u>-0-</u>
US Government obligations	10,161,701	10,161,701	-0-	-0-
Corporate obligations				
Mid yield	4,499,832	-0-	4,499,832	-0-
Total corporate obligations	<u>4,499,832</u>	<u>-0-</u>	<u>4,499,832</u>	<u>-0-</u>
	<u>58,251,935</u>	<u>\$ 53,752,103</u>	<u>\$ 4,499,832</u>	<u>\$ -0-</u>
Money market deposit accounts	7,093,826			
Commingled funds *	9,327,404			
Total investments limited as to use	<u>\$ 74,673,165</u>			

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

	December 31, 2017			
	Total	Level 1	Level 2	Level 3
Investments limited as to use				
Common stocks				
Consumer	\$ 1,350,247	\$ 1,350,247	\$ -0-	\$ -0-
Energy	1,099,678	1,099,678	-0-	-0-
Financial	1,986,968	1,986,968	-0-	-0-
Healthcare	1,142,671	1,142,671	-0-	-0-
Industrials	1,166,448	1,166,448	-0-	-0-
Information technology	931,798	931,798	-0-	-0-
Materials	935,569	935,569	-0-	-0-
Total common stocks	<u>8,613,379</u>	<u>8,613,379</u>	<u>-0-</u>	<u>-0-</u>
Mutual funds				
Fixed income funds	17,244,926	17,244,926	-0-	-0-
Large cap funds	10,938,356	10,938,356	-0-	-0-
International funds	4,198,617	4,198,617	-0-	-0-
Index funds	33,233	33,233	-0-	-0-
Total mutual funds	<u>32,415,132</u>	<u>32,415,132</u>	<u>-0-</u>	<u>-0-</u>
US Government obligations	7,459,170	7,459,170	-0-	-0-
Corporate obligations				
Mid yield	3,616,499	-0-	3,616,499	-0-
Total corporate obligations	<u>3,616,499</u>	<u>-0-</u>	<u>3,616,499</u>	<u>-0-</u>
	<u>52,104,180</u>	<u>\$ 48,487,681</u>	<u>\$ 3,616,499</u>	<u>\$ -0-</u>
Money market deposit accounts	956,640			
Commingled funds *	11,034,565			
Total investments limited as to use	<u>\$ 64,095,385</u>			

* In accordance with Subtopic 820-10, certain investments that were measured at net asset value per share (or its equivalent) have not been classified in the fair value hierarchy. The fair value amounts present in this table are intended to permit reconciliation of the fair value hierarchy to the line items presented at fair value in the consolidated balance sheets.

The System's policy is to recognize transfers between levels as of the end of the reporting period. There were no transfers during 2018 and 2017.

The System holds investments, which are exposed to various risks such as interest rate, market, and credit. Due to the level of risk associated with these securities and the level of uncertainty related to changes in the value, it is at least reasonably possible that changes in the various risk factors will occur in the near term that could materially affect the amounts reported in the accompanying consolidated financial statements.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Fair Value of Investments in Entities that Use Net Asset Value

The following table summarizes investments measured at fair value based on net asset value (NAVs) per share as of December 31, 2018 and 2017.

December 31, 2018	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Commingled funds	9,327,404	None	Daily	Daily
	\$ 9,327,404			
December 31, 2017	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Commingled funds	11,034,565	None	Daily	Daily
	\$ 11,034,565			

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

Long-term debt: The fair value of the Corporation's long-term debt for the mortgage payable insured by the United States Department of Housing and Urban Development (HUD) and fixed rate service line loans, and variable rate debt (2010 loan) approximates the carrying value based on the incremental borrowing rate of the System of as of December 31, 2018 and 2017, respectively.

8. NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions are restricted for the following purposes or periods as of December 31, 2018 and 2017:

	2018	Restated 2017
Subject to expenditure for specific purpose		
Capital items	\$ 1,206,944	\$ 889,151
Program expenditures	3,650,000	3,187,000
Total net assets with donor restrictions	\$ 4,856,944	\$ 4,076,151

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

9. LONG-TERM DEBT AND LEASES

The following is a summary of long-term debt as of December 31, 2018 and 2017:

	2018	2017
Mortgage note payable (project 073-22274) in the original amount of approximately \$266,600,000 bearing fixed interest on the unpaid balance at 3.33%, payable in monthly installments of principal and interest of approximately \$1,310,000, maturing on September 1, 2041, collateralized by property and equipment with a net book value of approximately \$270,551,000 as of December 31, 2018.	\$ 250,008,431	\$ 257,872,031
Loan payable in monthly principal and interests installments of approximately \$40,000 commencing in fiscal 2010 through fiscal 2026. Fixed term with variable interest rate set monthly (payable monthly) at 5.01% in 2017. Secured by net revenues and receivables of the Corporation with a net book value of approximately \$49,000,000 as of December 31, 2018.	2,832,000	3,141,700
Loans payable for purchases of medical group service lines in June 2015 and October 2017, due April 2019 and September 2021, respectively, with monthly installments of approximately \$102,000 and \$69,000, respectively, and fixed interest rates of 3.25% and 4.25%, respectively. The loans are unsecured.	2,854,543	4,825,088
Capital leases and other	20,170,538	20,590,620
Total long-term debt	275,865,512	286,429,439
Less current portion	9,289,113	10,600,023
Less unamortized debt issue costs	3,851,537	4,158,823
	\$ 262,724,862	\$ 271,670,593

The scheduled maturities and mandatory redemptions of long-term debt are as follows:

Year Ending December 31,	
2019	\$ 9,289,113
2020	9,154,206
2021	9,316,042
2022	8,833,022
2023	9,116,655
Thereafter	230,156,474
	\$ 275,865,512

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

During August 2016, the System refinanced outstanding debt (Series 2011, 2007, 1993, and 2014A bonds) with an approximate \$266,600,000 mortgage loan insured by the U.S. Department of Housing and Urban Development (HUD), authorized pursuant to Section 242 of the National Housing Act and the corresponding Regulations issued thereunder. The lender of this mortgage is Jones Lang LaSalle Multifamily, LLC. The agreement has monthly principal and interest payments of approximately \$1,310,000 from September 2016 through September 2041.

In June 2015 and October 2017, the Corporation financed the purchase of a medical group's Cardiac Cath Lab and Non-Invasive Cardiology service lines for approximately \$4,600,000 and \$3,330,000, respectively. The terms of the loans used to finance the purchases are shown in the summary table above. Payments made during the years ended December 31, 2018 and 2017 totaled approximately \$1,971,000 and \$1,335,000, respectively. The related intangible assets, reflecting primarily of the fair value of medical records and a non-compete contracts, are a component of intangible assets at net value within the consolidated balance sheets.

The System is also required to meet certain financial covenants. The System believes it is in compliance with all covenants as of December 31, 2018 and 2017.

The System leases buildings, medical equipment, and software under capital leases with various expiration dates. Cost and accumulated depreciation of the buildings and equipment under capital leases was approximately \$19,600,000 and \$20,300,000, respectively, and \$2,900,000 and \$2,700,000, respectively, at December 31, 2018 and 2017. These leases expire at varying dates through 2063.

The following is a schedule by year of future minimum lease payments under capital leases as of December 31, 2018, that have initial or remaining lease terms in excess of one year.

Year Ending December 31,	
2019	\$ 2,134,728
2020	2,099,645
2021	2,067,568
2022	2,067,660
2023	2,053,812
Thereafter	75,953,047
	<u>86,376,460</u>
Less imputed interest	66,205,922
	<u>\$ 20,170,538</u>

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

The System has operating leases for medical equipment and office space. Total rent and lease expense for the years ended December 31, 2018 and 2017 was approximately \$10,200,000 and \$11,100,000, respectively. Future minimum lease payments under noncancelable operating leases as of December 31, 2018 that have initial or remaining lease terms in excess of one year are as follows:

Year Ending December 31,	
2019	\$ 11,100,871
2020	2,900,900
2021	2,457,271
2022	1,290,955
2023	270,893
Thereafter	136,250
	<u>\$ 18,157,140</u>

10. NONCONTROLLING INTEREST

The following table depicts the changes in consolidated net assets attributable to the controlling financial interest of the Corporation and the 49% non-controlling interest Clinical Management Solutions, LLC holds in Union Hospital Therapy, LLC (UHT).

	Controlling Interest	Noncontrolling Interest	Total
Balance December 31, 2016	\$ 119,596,488	\$ 548,149	\$ 120,144,637
Excess of revenue over (under) expenses	(25,751,890)	1,486,584	(24,265,306)
Other changes in net assets without donor restrictions	45,320,628	(1,505,038)	43,815,590
Change in net assets without donor restrictions	<u>19,568,738</u>	<u>(18,454)</u>	<u>19,550,284</u>
Balance December 31, 2017	\$ 139,165,226	\$ 529,695	\$ 139,694,921
Excess of revenue over (under) expenses	28,291,077	1,468,062	29,759,139
Other changes in net assets without donor restrictions	(4,282,605)	(1,487,451)	(5,770,056)
Change in net assets without donor restrictions	<u>24,008,472</u>	<u>(19,389)</u>	<u>23,989,083</u>
Balance December 31, 2018	<u>\$ 163,173,698</u>	<u>\$ 510,306</u>	<u>\$ 163,684,004</u>

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

11. PENSION PLANS AND OTHER POST RETIREMENT BENEFITS

The Corporation had a noncontributory, defined-benefit plan (the Plan) covering substantially all of its employees who were at least 21 years old and had completed one year of service, and certain employees meeting those requirements of affiliated organizations. The Plan provided for retirement, survivor, and severance benefits. Employees with five or more years of service were entitled to monthly pension benefits beginning at normal retirement age (65) equal to their credited service multiplied by 1/60th of 1% of the total of their annual compensation for the five consecutive plan years, which produced the highest total. The Corporation agreed to contribute such amounts as are necessary to provide assets sufficient to meet the benefits to be paid to plan members. Contributions included normal cost, interest on unfunded prior service cost, and amortization of prior service cost over a period not exceeding 30 years. The Plan met the minimum funding requirements of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

During 2017, the Corporation terminated the defined-benefit plan, resulting in pension termination costs of approximately \$48,910,000 for the year. Lump sum payments to participants amounted to approximately \$68,029,000 and annuities purchased from the insurance company set up for participants amounted to approximately \$42,979,000 for the year ended December 31, 2017.

The following table sets forth the defined-benefit pension plan's benefit obligations, fair value of the Plan's assets, and unfunded status at December 31, 2017:

	2017
Change in benefit obligation	
Benefit obligation, beginning of year	\$ 101,492,815
Interest cost	3,951,628
Benefits paid	(111,008,307)
Actuarial loss	5,563,864
Benefit obligation, ending of year	<u>\$ -0-</u>
Changes in plan assets	
Fair value of plan assets, beginning of year	\$ 91,822,800
Actual return on plan assets	(521,827)
Employer contributions	19,707,334
Benefits paid	(111,008,307)
Fair value of plan assets, end of year	<u>\$ -0-</u>
Unfunded status	
Unfunded status of the plan, end of year	<u>\$ -0-</u>

During 2017, a lump sum payment was offered in lieu of annuities to all participating employees in the Plan as part of the termination. Approximately \$42,979,000 of lump sum payments were made during 2017 and are included as a component of benefits paid in the table above.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

The liability recorded to account for the unfunded status of the plan at year-end is recognized within the other liabilities on the consolidated balance sheet as of December 31, 2017.

The following is a summary of the components of net periodic pension costs:

	2017
Components of net benefit cost	
Interest cost	\$ 3,951,628
Expected return on plan assets	(1,850,421)
Actuarial loss	3,853,029
Net periodic benefit cost	<u>5,954,236</u>
Settlement cost related to plan termination	<u>48,909,624</u>
Net periodic benefit cost	<u>\$ 54,863,860</u>

The Corporation recognized a settlement loss due to the plan termination of approximately \$48,910,000 during 2017, which relates to the plan termination and related settlement payments. The losses represent a proportion of previously unrecognized losses included in net assets without donor restrictions. The settlement losses are included in the pension termination line in the 2017 consolidated statements of operations and changes in net assets.

The weighted-average assumptions used to determine the Plan's projected benefit obligation (PBO) and net periodic benefit costs (NPBC) for the year ended December 31, 2017 are as follows:

	2017
Discount rate	4.1%
Expected return on plan assets	2.0%
Rate of compensation increase - NPBC	Not Applicable

The principal long-term determinant of a portfolio's investment return is its asset allocation. In addition, active management strategies have added value relative to passive benchmark returns. The expected long-term rate of return assumption is based on the mix of assets in the Plan, the long-term earnings expected to be associated with each asset class, and the additional return expected through active management.

The Corporation also has a 403b defined contribution plan, which includes a 50% employer match up to 6% of employee deferrals in addition to an employer discretionary add-on of 1.67% for the years ended December 31, 2018 and 2017. The related contributions for the plan approximated \$3,359,000 and \$3,372,000 for the years ended December 31, 2018 and 2017, respectively.

UAPC also has a 401(k) discretionary defined contribution plan for which contributions during the years ended December 31, 2018 and 2017 were approximately \$2,029,000 and \$1,721,000, respectively.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

12. INVESTMENTS IN JOINT VENTURES

The Corporation is a member of a Vermont insurance company, Tecumseh Health Reciprocal Risk Retention Group (THRRRG), as means to comply with the Corporation's required portion of the insurance coverage pursuant to the Act, as well as its liability insurance. Membership in THRRRG includes 14 hospitals as of December 31, 2018. The Corporation's investment in THRRRG amounts to approximately \$3,850,000 and \$3,384,000 as of December 31, 2018 and 2017, respectively.

As stated in Note 4, UAPC is a member of CVM along with other independent physicians. UAPC's investment in CVM reflects a 50% ownership, is recorded under the equity method of accounting, and amounts to approximately \$1,876,000 as of December 31, 2018. Investment in CVM as of December 31, 2017 was immaterial to the consolidated balance sheet.

The interest is recorded in investments in joint ventures on the consolidated balance sheets and the Corporation's gain on its investment in these joint ventures are recorded in other non-operating gains (losses) on the consolidated statements of operations and changes in net assets.

The Corporation has ownership interest in other joint ventures accounted for under the equity method, the effects of which are immaterial to the consolidated financial statements as a whole. OSG and ASMS II, which are reflected in Note 4, are considered to have immaterial effects as noted herein.

13. COMMITMENTS AND CONTINGENCIES

The System is involved in other litigation arising in the normal course of business. After consultation with legal counsel, it is management's opinion that these matters will be resolved without a material adverse effect on the System's financial position or consolidated results of operations, changes in net assets, and cash flows.

14. LIQUIDITY AND AVAILABILITY OF RESOURCES

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the consolidated balance sheet date, comprise the following:

Financial assets	
Cash and cash equivalents	\$ 71,169,772
Patient accounts receivable	55,567,042
Other accounts receivable due within one year	7,146,453
Total financial assets	<u>\$ 133,883,267</u>

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

As a part of the System's liquidity management, it has a policy to structure financial assets to be available as its general expenditures, liabilities and other obligations come due. In addition, the System periodically invests excess cash in investments. The System does not intend to spend from the board-designated investments, though these amounts could be made available, if necessary.

15. BOARD-DESIGNATED NET ASSETS

The System's net assets without donor restrictions consist of the following:

	<u>2018</u>	<u>2017</u>
Net assets without donor restrictions		
Undesignated	\$ 95,627,900	\$ 79,009,796
Board-designated	67,545,798	60,155,430
Total	<u>\$ 163,173,698</u>	<u>\$ 139,165,226</u>

The Board of Directors of the System has established an operating reserve with the objective of setting funds aside to be drawn upon in the event of financial distress, immediate liquidity need, or to fund future capital needs. Total board designed funds amounted to approximately \$67,546,000 and \$60,155,000 as of December 31, 2018 and 2017.

16. EXPENSES BY BOTH NATURE AND FUNCTION

The consolidated financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the System. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include depreciation, which is allocated based on square footage, salaries and benefits, which are allocated based on estimates of time and effort, and employee benefits, which are allocated based on a percentage of salaries and benefits. The remaining operating expenses below were allocated based on an identified percentage developed through the System's analysis of indirect cost. Although the methods used were appropriate, alternative methods may provide different results.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2018 AND 2017

Expenses related to providing these services for the year ended December 31, 2018 were as follows:

	Healthcare Services	Administrative & General	Total
Physician, mid-level, and other provider salaries and wages	\$ 44,483,487	\$ 9,961,737	\$ 54,445,224
Other salaries and wages	92,561,366	20,728,411	113,289,777
Employee benefits	25,800,396	5,777,802	31,578,198
Medical supplies and drugs	92,093,272	-0-	92,093,272
Physician services	17,082,688	3,825,538	20,908,226
Contract services	79,865,085	17,885,175	97,750,260
Rent and leases	8,356,129	1,871,291	10,227,420
Utilities, supplies, and other	28,196,928	6,314,486	34,511,414
Hospital assessment fee	21,906,132	-0-	21,906,132
Depreciation and amortization	21,527,022	4,820,812	26,347,834
Interest	-0-	12,939,582	12,939,582
	\$ 431,872,505	\$ 84,124,834	\$ 515,997,339

Expenses related to providing these services for the year ended December 31, 2017 were as follows:

	2017
Healthcare Services	\$ 469,845,265
Administrative & General	74,895,302
	\$ 544,740,567

SUPPLEMENTARY INFORMATION

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEETS DECEMBER 31, 2018

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Union Health System
Assets				
Current assets				
Cash and cash equivalents	\$ 66,865,536	\$ 4,304,236	\$ -0-	\$ 71,169,772
Patient accounts receivable, net	49,139,252	6,427,790	-0-	55,567,042
Inventories	5,295,361	478,181	-0-	5,773,542
Due from related parties	-0-	329,082	(329,082)	-0-
Prepaid expenses and other current assets	14,164,722	5,291,595	(834,716)	18,621,601
Total current assets	<u>135,464,871</u>	<u>16,830,884</u>	<u>(1,163,798)</u>	<u>151,131,957</u>
Investments limited as to use				
Funds held by trustee	7,127,367	-0-	-0-	7,127,367
Board designated	67,545,798	-0-	-0-	67,545,798
Total investments limited as to use	<u>74,673,165</u>	<u>-0-</u>	<u>-0-</u>	<u>74,673,165</u>
Property and equipment				
Land and improvements	38,280,140	-0-	-0-	38,280,140
Buildings and fixed equipment	357,423,327	19,556,552	-0-	376,979,879
Movable equipment	169,691,836	8,827,562	-0-	178,519,398
	<u>565,395,303</u>	<u>28,384,114</u>	<u>-0-</u>	<u>593,779,417</u>
Less allowances for depreciation	316,809,124	6,905,099	-0-	323,714,223
	<u>248,586,179</u>	<u>21,479,015</u>	<u>-0-</u>	<u>270,065,194</u>
Construction in progress	486,164	-0-	-0-	486,164
Total property and equipment, net	<u>249,072,343</u>	<u>21,479,015</u>	<u>-0-</u>	<u>270,551,358</u>
Other assets				
Due from Union Health Foundation, Inc.	3,650,489	-0-	-0-	3,650,489
Intangible assets, net and other	3,486,829	130,129	-0-	3,616,958
Investment in joint ventures	3,849,891	2,404,055	-0-	6,253,946
	<u>10,987,209</u>	<u>2,534,184</u>	<u>-0-</u>	<u>13,521,393</u>
Total assets	<u>\$ 470,197,588</u>	<u>\$ 40,844,083</u>	<u>\$ (1,163,798)</u>	<u>\$ 509,877,873</u>

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEETS DECEMBER 31, 2018

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Union Health System
Liabilities and net assets				
Current liabilities				
Accounts payable and other current liabilities	\$ 31,567,357	\$ 1,142,921	\$ -0-	\$ 32,710,278
Salaries, wages and related liabilities	22,038,410	13,745,731	(834,716)	34,949,425
Estimated third party settlements	1,577,262	-0-	-0-	1,577,262
Current portion of long-term debt	9,262,906	26,207	-0-	9,289,113
Total current liabilities	<u>64,445,935</u>	<u>14,914,859</u>	<u>(834,716)</u>	<u>78,526,078</u>
Long-term liabilities				
Long-term debt, less current portion	243,408,104	19,316,758	-0-	262,724,862
Other long-term liabilities	415,067	-0-	(329,082)	85,985
Total long-term liabilities	<u>243,823,171</u>	<u>19,316,758</u>	<u>(329,082)</u>	<u>262,810,847</u>
Total liabilities	308,269,106	34,231,617	(1,163,798)	341,336,925
Net assets				
Without donor restrictions	156,561,232	6,612,466	-0-	163,173,698
Noncontrolling interests in UHT, LLC	510,306	-0-	-0-	510,306
Total net assets without donor restrictions	<u>157,071,538</u>	<u>6,612,466</u>	<u>-0-</u>	<u>163,684,004</u>
With donor restrictions	4,856,944	-0-	-0-	4,856,944
Total net assets	<u>161,928,482</u>	<u>6,612,466</u>	<u>-0-</u>	<u>168,540,948</u>
Total liabilities and net assets	<u>\$ 470,197,588</u>	<u>\$ 40,844,083</u>	<u>\$ (1,163,798)</u>	<u>\$ 509,877,873</u>

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEETS DECEMBER 31, 2017 – RESTATED

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Union Health System
Assets				
Current assets				
Cash and cash equivalents	\$ 49,826,085	\$ 1,269,163	\$ -0-	\$ 51,095,248
Patient accounts receivable, net	61,134,667	6,390,945	-0-	67,525,612
Inventories	5,325,620	564,913	-0-	5,890,533
Due from related parties	-0-	752,145	(752,145)	-0-
Prepaid expenses and other current assets	15,104,465	1,747,002	(411,653)	16,439,814
Total current assets	<u>131,390,837</u>	<u>10,724,168</u>	<u>(1,163,798)</u>	<u>140,951,207</u>
Investments limited as to use				
Funds held by trustee	3,939,955	-0-	-0-	3,939,955
Board designated and	60,155,430	-0-	-0-	60,155,430
Total investments limited as to use	<u>64,095,385</u>	<u>-0-</u>	<u>-0-</u>	<u>64,095,385</u>
Property and equipment				
Land and improvements	37,685,526	-0-	-0-	37,685,526
Buildings and fixed equipment	349,809,901	19,556,552	-0-	369,366,453
Movable equipment	160,371,108	8,157,481	-0-	168,528,589
	<u>547,866,535</u>	<u>27,714,033</u>	<u>-0-</u>	<u>575,580,568</u>
Less allowances for depreciation	294,495,876	4,965,125	-0-	299,461,001
	<u>253,370,659</u>	<u>22,748,908</u>	<u>-0-</u>	<u>276,119,567</u>
Construction in progress	7,847,106	3,959	-0-	7,851,065
Total property and equipment, net	<u>261,217,765</u>	<u>22,752,867</u>	<u>-0-</u>	<u>283,970,632</u>
Other assets				
Due from Union Health Foundation, Inc.	3,187,376	-0-	-0-	3,187,376
Intangible assets, net and other	5,514,074	27,764	-0-	5,541,838
Investment in joint ventures	3,383,980	928,552	-0-	4,312,532
	<u>12,085,430</u>	<u>956,316</u>	<u>-0-</u>	<u>13,041,746</u>
Total assets	<u>\$ 468,789,417</u>	<u>\$ 34,433,351</u>	<u>\$ (1,163,798)</u>	<u>\$ 502,058,970</u>

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEETS DECEMBER 31, 2017 – RESTATED

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Union Health System
Liabilities and net assets				
Current liabilities				
Accounts payable and other current liabilities	\$ 33,492,465	\$ 9,537,933	\$ -0-	\$ 43,030,398
Salaries, wages and related liabilities	23,273,329	7,688,070	(411,653)	30,549,746
Estimated third party settlements	2,142,902	-0-	-0-	2,142,902
Current portion of long-term debt	10,575,204	24,819	-0-	10,600,023
Total current liabilities	<u>69,483,900</u>	<u>17,250,822</u>	<u>(411,653)</u>	<u>86,323,069</u>
Long-term liabilities				
Long-term debt, less current portion	252,327,628	19,342,965	-0-	271,670,593
Other long-term liabilities	1,046,381	-0-	(752,145)	294,236
Total long-term liabilities	<u>253,374,009</u>	<u>19,342,965</u>	<u>(752,145)</u>	<u>271,964,829</u>
Total liabilities	322,857,909	36,593,787	(1,163,798)	358,287,898
Net assets				
Without donor restrictions	141,325,662	(2,160,436)	-0-	139,165,226
Noncontrolling interests in UHT, LLC	529,695	-0-	-0-	529,695
Total net assets without donor restrictions	<u>141,855,357</u>	<u>(2,160,436)</u>	<u>-0-</u>	<u>139,694,921</u>
With donor restrictions	4,076,151	-0-	-0-	4,076,151
Total net assets	<u>145,931,508</u>	<u>(2,160,436)</u>	<u>-0-</u>	<u>143,771,072</u>
Total liabilities and net assets	<u>\$ 468,789,417</u>	<u>\$ 34,433,351</u>	<u>\$ (1,163,798)</u>	<u>\$ 502,058,970</u>

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED DECEMBER 31, 2018

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Union Health System
Operating revenue				
Net patient service revenue	\$ 503,406,707	\$ 49,520,320	\$ -0-	\$ 552,927,027
Less provision for bad debts	37,655,511	1,435,167	-0-	39,090,678
Net patient service revenue net of provision for bad debts	465,751,196	48,085,153	-0-	513,836,349
Other revenue	14,267,322	12,732,328	(3,251,795)	23,747,855
Total operating revenue	480,018,518	60,817,481	(3,251,795)	537,584,204
Operating expenses				
Physician, Mid-level, and other provider salaries and wages	19,378,465	35,066,759	-0-	54,445,224
Other salaries and wages	101,149,258	12,140,519	-0-	113,289,777
Employee benefits	24,392,987	7,185,211	-0-	31,578,198
Medical supplies and drugs	84,356,088	7,737,184	-0-	92,093,272
Physician services	20,908,226	-0-	-0-	20,908,226
Contract services	79,466,685	20,929,170	(2,645,595)	97,750,260
Rent and leases	7,728,724	3,097,571	(598,875)	10,227,420
Utilities, supplies, and other	29,275,157	5,243,582	(7,325)	34,511,414
Hospital assessment fee	21,906,132	-0-	-0-	21,906,132
Depreciation and amortization	24,407,859	1,939,975	-0-	26,347,834
Interest	10,834,431	2,105,151	-0-	12,939,582
Total operating expenses	423,804,012	95,445,122	(3,251,795)	515,997,339
Income (loss) from operations	56,214,506	(34,627,641)	-0-	21,586,865
Non-operating gains (losses)				
Investment income, net	2,218,157	8,889	-0-	2,227,046
Other	347,228	5,598,000	-0-	5,945,228
Total non-operating gains (losses)	2,565,385	5,606,889	-0-	8,172,274
Excess of revenue over (under) expenses	\$ 58,779,891	\$ (29,020,752)	\$ -0-	\$ 29,759,139

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED DECEMBER 31, 2018

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Total Reporting Unit
Other changes in net assets without donor restrictions				
Distribution to non-controlling interests	(1,450,729)	-0-	-0-	(1,450,729)
Net unrealized loss on investments	(4,324,417)	-0-	-0-	(4,324,417)
Transfers for property and equipment additions	5,090	-0-	-0-	5,090
Transfers between Union Hospital, Inc. and UAPC	(37,793,654)	37,793,654	-0-	-0-
Change in net assets without donor restrictions	<u>15,216,181</u>	<u>8,772,902</u>	-0-	<u>23,989,083</u>
Net assets with donor restrictions				
Other changes in receivable from Union Health Foundation, Inc.	785,883	-0-	-0-	785,883
Net assets released for property and equipment	(5,090)	-0-	-0-	(5,090)
Change in net assets with donor restrictions	<u>780,793</u>	<u>-0-</u>	<u>-0-</u>	<u>780,793</u>
Change in net assets	15,996,974	8,772,902	-0-	24,769,876
Net assets				
Beginning of year	145,931,508	(2,160,436)	-0-	143,771,072
End of year	<u>\$ 161,928,482</u>	<u>\$ 6,612,466</u>	<u>\$ -0-</u>	<u>\$ 168,540,948</u>

See Report of Independent Auditors on Pages 1 - 3.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED DECEMBER 31, 2017 – RESTATED

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Union Health System
Operating revenue				
Net patient service revenue	\$ 473,332,301	\$ 51,871,900	\$ -0-	\$ 525,204,201
Less provision for bad debts	26,227,684	2,577,873	-0-	28,805,557
Net patient service revenue net of provision for bad debts	447,104,617	49,294,027	-0-	496,398,644
Other revenue	12,994,178	6,039,956	(3,251,795)	15,782,339
Total operating revenue	460,098,795	55,333,983	(3,251,795)	512,180,983
Operating expenses				
Physician, Mid-level, and other provider salaries and wages	19,192,364	34,926,692	-0-	54,119,056
Other salaries and wages	101,384,908	156,789	-0-	101,541,697
Employee benefits	31,352,860	7,141,234	-0-	38,494,094
Supplies and drugs	81,399,317	8,154,413	-0-	89,553,730
Physician services	19,373,250	-0-	-0-	19,373,250
Contract services	72,103,851	25,131,779	(2,645,595)	94,590,035
Rent and leases	7,341,254	4,366,755	(598,875)	11,109,134
Utilities, supplies, and other	29,699,474	5,247,738	(7,325)	34,939,887
Hospital assessment fee	16,853,726	-0-	-0-	16,853,726
Depreciation and amortization	20,361,514	1,157,600	-0-	21,519,114
Interest	11,671,271	2,065,949	-0-	13,737,220
Total operating expenses	410,733,789	88,348,949	(3,251,795)	495,830,943
Income (loss) from operations	49,365,006	(33,014,966)	-0-	16,350,040
Pension termination				
	48,909,624	-0-	-0-	48,909,624
Income (loss) from operations after pension termination	455,382	(33,014,966)	-0-	(32,559,584)
Nonoperating gains (losses)				
Investment income	5,459,181	866	-0-	5,460,047
Other	514,979	2,319,252	-0-	2,834,231
Total nonoperating gains (losses)	5,974,160	2,320,118	-0-	8,294,278
Excess of revenue over (under) expenses	\$ 6,429,542	\$ (30,694,848)	\$ -0-	\$ (24,265,306)

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UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED DECEMBER 31, 2017 – RESTATED

	Union Hospital, Inc. and Subsidiaries	Union Associated Physician's Clinic	Eliminations	Total Reporting Unit
Other changes in net assets without donor restrictions				
Pension related changes other than net pension cost	\$ 44,826,541	\$ -0-	\$ -0-	\$ 44,826,541
Distribution to non-controlling interests	(1,505,038)	-0-	-0-	(1,505,038)
Net unrealized gain on investments	69,880	-0-	-0-	69,880
Transfers for property and equipment additions	424,207	-0-	-0-	424,207
Transfers between Union Hospital, Inc. and UAPC	(36,398,280)	36,398,280	-0-	-0-
Change in net assets without donor restrictions	<u>13,846,852</u>	<u>5,703,432</u>	-0-	<u>19,550,284</u>
Net assets with donor restrictions				
Other changes in receivable from Union Health Foundation, Inc.	1,302,688	-0-	-0-	1,302,688
Net assets released for property and equipment	(424,207)	-0-	-0-	(424,207)
Change in net assets with donor restrictions	<u>878,481</u>	<u>-0-</u>	-0-	<u>878,481</u>
Change in net assets	14,725,333	5,703,432	-0-	20,428,765
Net assets				
Beginning of year	131,206,175	(7,863,868)	-0-	123,342,307
End of year	<u>\$ 145,931,508</u>	<u>\$ (2,160,436)</u>	<u>\$ -0-</u>	<u>\$ 143,771,072</u>

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UNION HOSPITAL, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENTS OF OPERATIONS YEAR ENDED DECEMBER 31, 2018

	Union Hospital	Union Hospital Clinton	Total Union Hospital, Inc.	IPACS, Inc.	COH	UHT, LLC	Eliminations	Total Union Hospital, Inc. and Subsidiaries
Operating revenue								
Net patient service revenue	\$ 474,727,015	\$ 26,936,988	\$ 501,664,003	\$ -0-	\$ 1,742,704	\$ -0-	\$ -0-	\$ 503,406,707
Less provision for bad debts	34,284,784	3,370,727	37,655,511	-0-	-0-	-0-	-0-	37,655,511
Net patient service revenue net of provision for bad debts	440,442,231	23,566,261	464,008,492	-0-	1,742,704	-0-	-0-	465,751,196
Other revenue	15,194,328	362,863	15,557,191	1,142,200	-0-	10,106,153	(12,538,222)	14,267,322
Total operating revenue	455,636,559	23,929,124	479,565,683	1,142,200	1,742,704	10,106,153	(12,538,222)	480,018,518
Operating expenses								
Physician, Mid-level, and other provider salaries and wages	14,072,087	85,803	14,157,890	436,660	-0-	4,783,915	-0-	19,378,465
Other salaries and wages	94,125,247	7,024,011	101,149,258	-0-	-0-	-0-	-0-	101,149,258
Employee benefits	21,928,710	1,505,081	23,433,791	88,238	-0-	870,958	-0-	24,392,987
Medical supplies and drugs	82,050,235	1,880,710	83,930,945	-0-	425,143	-0-	-0-	84,356,088
Physician services	18,757,960	2,150,266	20,908,226	-0-	-0-	-0-	-0-	20,908,226
Contract services	74,879,934	3,271,846	78,151,780	97,084	1,334,286	1,242,207	(1,358,672)	79,466,685
Rent and leases	7,246,058	476,767	7,722,825	19,660	4,196	-0-	(17,957)	7,728,724
Utilities, supplies, and other	36,542,468	2,581,822	39,124,290	517,700	582,758	212,002	(11,161,593)	29,275,157
Hospital assessment fee	20,582,792	1,323,340	21,906,132	-0-	-0-	-0-	-0-	21,906,132
Depreciation and amortization	23,239,077	1,162,530	24,401,607	2,401	3,851	-0-	-0-	24,407,859
Interest	10,832,702	703	10,833,405	-0-	-0-	1,026	-0-	10,834,431
Total operating expenses	404,257,270	21,462,879	425,720,149	1,161,743	2,350,234	7,110,108	(12,538,222)	423,804,012
Income (loss) from operations	51,379,289	2,466,245	53,845,534	(19,543)	(607,530)	2,996,045	-0-	56,214,506
Non-operating gains (losses)								
Investment income, net	2,163,853	1,884	2,165,737	52,420	-0-	-0-	-0-	2,218,157
Other	1,301,734	(1,176)	1,300,558	-0-	-0-	-0-	(953,330)	347,228
Total non-operating gains (losses)	3,465,587	708	3,466,295	52,420	-0-	-0-	(953,330)	2,565,385
Excess of revenue over (under) expenses	\$ 54,844,876	\$ 2,466,953	\$ 57,311,829	\$ 32,877	\$ (607,530)	\$ 2,996,045	\$ (953,330)	\$ 58,779,891

See Report of Independent Auditors on Pages 1 - 3.

UNION HOSPITAL, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENTS OF OPERATIONS YEAR ENDED DECEMBER 31, 2017 – RESTATED

	Union Hospital	Union Hospital Clinton	Total Union Hospital, Inc.	IPACS, Inc.	COH	UHT, LLC	Eliminations	Total Union Hospital, Inc.
Operating revenue								
Net patient service revenue	\$ 446,878,806	\$ 24,955,727	\$ 471,834,533	\$ -0-	\$ 1,497,768	\$ -0-	\$ -0-	\$ 473,332,301
Less provision for bad debts	23,646,333	2,581,351	26,227,684	-0-	-0-	-0-	-0-	26,227,684
Net patient service revenue net of provision for bad debts	423,232,473	22,374,376	445,606,849	-0-	1,497,768	-0-	-0-	447,104,617
Other revenue	13,913,394	400,773	14,314,167	1,168,344	-0-	9,746,881	(12,235,214)	12,994,178
Total operating revenue	437,145,867	22,775,149	459,921,016	1,168,344	1,497,768	9,746,881	(12,235,214)	460,098,795
Operating expenses								
Physician, Mid-level, and other provider salaries and wages	13,854,668	145,432	14,000,100	400,245	-0-	4,792,019	-0-	19,192,364
Other salaries and wages	93,758,020	7,626,888	101,384,908	-0-	-0-	-0-	-0-	101,384,908
Employee benefits	28,180,934	2,152,437	30,333,371	77,995	-0-	941,494	-0-	31,352,860
Supplies and drugs	79,229,651	2,019,044	81,248,695	-0-	150,622	-0-	-0-	81,399,317
Physician services	17,461,567	1,911,683	19,373,250	-0-	-0-	-0-	-0-	19,373,250
Contract services	68,128,018	3,129,796	71,257,814	75,906	1,378,449	801,911	(1,410,229)	72,103,851
Rent and leases	6,855,385	479,958	7,335,343	19,202	4,154	-0-	(17,445)	7,341,254
Utilities, supplies, and other	36,506,531	2,783,511	39,290,042	562,059	478,616	176,297	(10,807,540)	29,699,474
Hospital assessment fee	15,798,150	1,055,576	16,853,726	-0-	-0-	-0-	-0-	16,853,726
Depreciation and amortization	19,325,807	1,028,766	20,354,573	3,090	3,851	-0-	-0-	20,361,514
Interest	11,669,159	799	11,669,958	-0-	-0-	1,313	-0-	11,671,271
Total operating expenses	390,767,890	22,333,890	413,101,780	1,138,497	2,015,692	6,713,034	(12,235,214)	410,733,789
Income (loss) from operations	46,377,977	441,259	46,819,236	29,847	(517,924)	3,033,847	-0-	49,365,006
Pension Termination								
Income (loss) from operations after pension termination	(2,531,647)	441,259	(2,090,388)	29,847	(517,924)	3,033,847	-0-	455,382
Nonoperating gains (losses)								
Investment income	5,374,470	3,005	5,377,475	81,706	-0-	-0-	-0-	5,459,181
Other	1,650,870	5,000	1,655,870	-0-	-0-	-0-	(1,140,891)	514,979
Total nonoperating gains (losses)	7,025,340	8,005	7,033,345	81,706	-0-	-0-	(1,140,891)	5,974,160
Excess of revenue over (under) expenses	\$ 4,493,693	\$ 449,264	\$ 4,942,957	\$ 111,553	\$ (517,924)	\$ 3,033,847	\$ (1,140,891)	\$ 6,429,542

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES
SCHEDULE OF PROPERTY AND EQUIPMENT OF MORTGAGOR
YEAR ENDED DECEMBER 31, 2018

	Mortgagor	Other Activities	Consolidated System
Land and improvements	\$ 34,387,440	\$ 3,892,700	\$ 38,280,140
Buildings and fixed equipment	371,140,488	5,839,391	376,979,879
Movable equipment	178,519,398	-0-	178,519,398
	584,047,326	9,732,091	593,779,417
Less allowances for depreciation	316,936,809	6,777,414	323,714,223
Construction in progress	486,164	-0-	486,164
Total property and equipment, net	\$ 267,596,681	\$ 2,954,677	\$ 270,551,358

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED DECEMBER 31, 2018

Grantor/Pass-through Grantor/Program	Grant ID #	CFDA Number	Federal Expenditures
Major program			
U.S. Department of Housing and Urban Development			
Mortgage Insurance - Hospitals Section 242 *	073-22274	14.128	\$ 250,008,431
Non-major programs			
U.S. Department of Health and Human Services			
Pass through Health Resources and Services Administration (HRSA)			
Bureau of Health Workforce			
Primary Care Training and Enhancement	TOBHP28564-03	93.884	132,504
Primary Care Training and Enhancement	TOBHP28564-04	93.884	102,259
Total for CFDA 93.884			<u>234,763</u>
U.S. Department of Health and Human Services			
Pass through HRSA Office of Advancement of Telehealth			
Substance Abuse Treatment Network Grant Program	1H1WRH31447-01	93.211	109,801
Substance Abuse Treatment Network Grant Program	5H1WRH31447-02	93.211	29,008
Evidence-Based Tele-emergency Network Grant Program	6 G01RH32154-01-01	93.211	20,000
Evidence-Based Tele-emergency Network Grant Program	G01RH27871-04	93.211	267,049
Total for CFDA 93.211			<u>425,858</u>
Pass through Indiana State Department of Health			
Hospital Preparedness Program	14924	93.817	11,636
Pass through Indiana State Department of Health			
Assistance Programs for Chronic Disease Prevention and Control	22779	93.945	600
Pass through Indiana State Department of Health			
Assistance Programs for Chronic Disease Prevention and Control	22779	93.757	5,400
Pass through Indiana State University			
Indiana Area Health Education Centers Network	2U77HP23068-07-00	93.107	20,000
Pass through Indiana State Department of Health			
Small Rural Hospital Improvement Program Grant (SHIP)	21207	93.301	9,000
Total non-major programs			<u>707,257</u>
Total federal expenditures			<u>\$ 250,715,688</u>

* The U.S. Department of Housing and Urban Development – Mortgage Insurance for Hospital’s loan program continues to have compliance requirements. The amount noted as federal expenditures represents the remaining outstanding loan balance at the end of the year.

There were no entities that received pass-through federal awards from the Union Health System, Inc. and Subsidiaries (the System) during the year ended December 31, 2018.

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED DECEMBER 31, 2018

Note A - Basis of Presentation – The accompanying schedule of expenditures of federal awards (SEFA) includes the federal award activity of the System under programs of the federal government for the year ended December 31, 2018. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).

Because the SEFA presents only a selected portion of the operations of the System, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the System.

Note B- Summary of Significant Accounting Policies - Expenditures reported on the SEFA are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. The System has elected not to use the 10% de minimis indirect cost rate as allowed under the Uniform Guidance.



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REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Directors
Union Health System, Inc.
Terre Haute, Indiana

Report on the Consolidated Financial Statements

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and the Guideline for Examination of Entities Receiving Financial Assistance from Governmental Sources, issued by the Indiana State Board of Accounts, the consolidated financial statements of Union Health System, Inc. (the System), which comprise the consolidated balance sheet as of December 31, 2018 and the related consolidated statement of operations and changes in net assets, and consolidated statement of cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated April 16, 2019.

Internal Control over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the System's consolidated financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Board of Directors
Union Health System, Inc.
Terre Haute, Indiana

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose

Blue & Co., LLC

Indianapolis, Indiana
April 16, 2019



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REPORT OF INDEPENDENT AUDITORS ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

Board of Directors
Union Health System, Inc.
Terre Haute, Indiana

Report on Compliance for Each Major Federal Program

We have audited Union Health System, Inc.'s (the System) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the System's major federal programs for the year ended December 31, 2018. The System's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the System's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* ("Uniform Guidance"). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the System's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the System's compliance.

Board of Directors
Union Health System, Inc.
Terre Haute, Indiana

Opinion on Each Major Federal Program

In our opinion, the System complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2018.

Report on Internal Control over Compliance

Management of the System is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the System's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Blue & Co., LLC

Indianapolis, Indiana
April 16, 2019

UNION HEALTH SYSTEM, INC. AND SUBSIDIARIES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED DECEMBER 31, 2018

Summary of Auditor's Results

Consolidated Financial Statements

Type of auditor's report issued: Unmodified

Internal control over financial reporting:

Material weakness(es) identified? yes none reported

Significant deficiency(ies) identified that are not considered to be material weakness(es)? yes none reported

Noncompliance material to financial statements noted? yes none reported

Federal Awards

Internal controls over major programs:

Material weakness(es) identified? yes none reported

Significant deficiency(ies) identified that are not considered to be material weakness(es)? yes none noted

Type of auditor's report issued on compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported as defined by Uniform Guidance [2 CFR 200.516(a)]? yes no

Identification of major program:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
<p>█ 14.128</p>	<p style="text-align: center;">U.S. Department of Housing and Urban Development Mortgage Insurance - Hospitals Section 242</p>

Dollar threshold used to distinguish between type A and B programs: \$750,000

Auditee qualified as low-risk auditee? yes no

Section II – Findings related to financial statements reported in accordance with Government Auditing Standards:

No matters reported

Section III – Findings and questioned costs relating to Federal awards:

No matters reported

Section IV – Summary schedule of prior audit findings:

No matters reported