



Consolidated Financial Statements,
Supplementary Information and Report of
Independent Certified Public Accountants

Beebe Medical Center, Inc.
d/b/a Beebe Healthcare

June 30, 2018 and 2017



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Grant Thornton LLP
Two Commerce Square
2001 Market St., Suite 700
Philadelphia, PA 19103
T 215.561.4200
F 215.561.1066
GrantThornton.com
[linkd.in/GrantThorntonUS](https://www.linkedin.com/company/grantthorntonus)
twitter.com/GrantThorntonUS

Report of Independent Certified Public Accountants

Board of Directors
Beebe Medical Center, Inc.
d/b/a Beebe Healthcare

We have audited the accompanying consolidated financial statements of Beebe Medical Center, Inc., d/b/a Beebe Healthcare (“the System”), which comprise the consolidated balance sheets as of June 30, 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 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.

Auditors’ responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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.

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 consolidated financial position of Beebe Medical Center, Inc. as of June 30, 2018 and 2017, and the results of its operations, 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.

Emphasis of matter

As discussed in Note B.21 to the consolidated financial statements, in 2018 the System adopted Accounting Standards Update 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. Our opinion is not modified with respect to this matter.

Supplementary information

Our audits were performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating information as of June 30, 2018 and for the year then ended is presented for the purpose of additional analysis, rather than to present the financial position, results of operations and changes in net assets, and cash flows of the individual entities, and is not a required part of the consolidated financial statements. Such supplementary 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 our audits of the consolidated financial statements and certain additional procedures. These additional procedures include comparing and reconciling the 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 consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.



Philadelphia, Pennsylvania

October 26, 2018

Beebe Medical Center, Inc.

CONSOLIDATED BALANCE SHEETS

June 30,

	<u>2018</u>	<u>2017</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 65,214,085	\$ 67,663,855
Patient accounts receivable, net of allowance for doubtful accounts of \$10,296,000 in 2018 and \$8,574,000 in 2017	44,059,962	41,942,296
Prepaid expenses and other current assets	<u>18,117,968</u>	<u>13,787,738</u>
Total current assets	127,392,015	123,393,889
Assets limited as to use		
Board designated funds	78,831,114	74,317,880
Under bond indenture agreement	144,040	2,316
Collateral funds for line of credit	7,713,605	7,182,738
Donor-restricted funds	<u>16,925,197</u>	<u>11,489,189</u>
Subtotal	103,613,956	92,992,123
Other board designated assets - land	1,838,339	1,838,339
Donor-restricted pledges receivable, net	10,197,003	1,702,511
Assets held in charitable remainder trust	672,432	643,713
Beneficial interest in perpetual trust	<u>336,878</u>	<u>327,797</u>
Total assets limited as to use	116,658,608	97,504,483
Property and equipment, net	143,569,850	143,195,973
Other assets	<u>11,413,139</u>	<u>10,661,253</u>
Total assets	<u>\$ 399,033,612</u>	<u>\$ 374,755,598</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable and accrued expenses	\$ 45,936,651	\$ 43,056,892
Estimated third-party payor settlements	7,169,716	11,520,171
Current portion of long-term debt	<u>3,593,150</u>	<u>4,379,822</u>
Total current liabilities	56,699,517	58,956,885
Accrued retirement benefits	50,475,182	76,694,369
Other liabilities	16,694,570	16,775,642
Long-term debt, less current portion	<u>44,339,089</u>	<u>46,336,778</u>
Total liabilities	168,208,358	198,763,674
Net assets		
Unrestricted	204,427,346	162,568,144
Temporarily restricted	23,900,248	11,023,415
Permanently restricted	<u>2,497,660</u>	<u>2,400,365</u>
Total net assets	<u>230,825,254</u>	<u>175,991,924</u>
Total liabilities and net assets	<u>\$ 399,033,612</u>	<u>\$ 374,755,598</u>

The accompanying notes are an integral part of these statements.

**CONSOLIDATED STATEMENTS OF OPERATIONS
AND CHANGES IN NET ASSETS**

For the year ended June 30,

	2018	2017
Unrestricted net assets		
Unrestricted revenues and other support		
Net patient service revenue before bad debt	\$ 430,822,710	\$ 415,682,361
Less: Provision for bad debt	<u>(16,213,223)</u>	<u>(10,206,021)</u>
Net patient service revenue less provision for bad debt	414,609,487	405,476,340
Other revenues	4,274,684	4,606,325
Net assets released from restrictions used for operations	<u>805,898</u>	<u>20,046</u>
Total unrestricted revenues and other support	419,690,069	410,102,711
Expenses		
Salaries and benefits, physician fees, and contract labor	236,656,007	224,921,899
Medical, surgical, and patient-related supplies and services	87,608,831	82,615,285
Repairs, maintenance and utilities	16,319,925	15,247,153
Other	46,235,996	42,873,598
Depreciation and amortization	20,273,719	19,752,556
Interest	<u>1,272,660</u>	<u>1,200,790</u>
Total expenses	<u>408,367,138</u>	<u>386,611,281</u>
Income from operations	11,322,931	23,491,430
Nonoperating gains (losses)		
Contributions	267,684	208,591
Investment income	4,138,558	2,996,943
Other accrued retirement costs	<u>(4,106,861)</u>	<u>(3,468,000)</u>
Total nonoperating gains (losses), net	<u>299,381</u>	<u>(262,466)</u>
Excess of revenues and gains over expenses and losses	11,622,312	23,228,964

(Continues on following page.)

**CONSOLIDATED STATEMENTS OF OPERATIONS
AND CHANGES IN NET ASSETS - CONTINUED**

For the year ended June 30,

	2018	2017
Excess of revenues and gains over expenses and losses <i>(continued from previous page)</i>	\$ 11,622,312	\$ 23,228,964
Other changes in unrestricted net assets		
Net assets released from restrictions used for property and equipment purchases	521,253	3,626,704
Other changes in accrued retirement benefits	27,965,248	5,067,912
Changes in unrealized gains and losses on investments	1,738,404	5,553,029
Other	11,985	(554,023)
Increase in unrestricted net assets	41,859,202	36,922,586
Temporarily restricted net assets		
Contributions	13,896,259	4,074,243
Net investment income and realized gains on investments	307,725	321,310
Net assets released from restrictions used for:		
Property and equipment purchases	(521,253)	(3,626,704)
Operations	(805,898)	(20,046)
Other	-	171,248
Increase in temporarily restricted net assets	12,876,833	920,051
Permanently restricted net assets		
Contributions	68,434	60,680
Change in value of beneficial interest in perpetual trust	9,081	17,570
Realized and unrealized gains on investments	19,780	37,668
Increase in permanently restricted net assets	97,295	115,918
Increase in net assets	54,833,330	37,958,555
Net assets, beginning of year	175,991,924	138,033,369
Net assets, end of year	\$ 230,825,254	\$ 175,991,924

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the year ended June 30,

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities		
Increase in net assets	\$ 54,833,329	\$ 37,958,555
Adjustments to reconcile increase in net assets to net cash provided by operating activities		
Other changes in accrued retirement benefits	(27,965,248)	(5,067,912)
Depreciation and amortization	20,273,719	19,752,556
Restricted contributions, net	(14,292,198)	(4,493,901)
Change in values of remainder trusts and beneficial interest in perpetual trust	(37,800)	(56,393)
Provision for bad debt	16,213,223	10,206,021
Gains on disposition of property and equipment	(265,896)	(290,044)
Net realized and unrealized gains	(4,085,033)	(6,953,716)
Changes in operating assets and liabilities		
Patients accounts receivable	(18,330,889)	(10,385,206)
Prepaid expenses and other current assets	(4,330,230)	(1,802,653)
Accounts payable and other accrued expenses	6,214,738	(219,379)
Estimated third-party payor settlements	(4,350,455)	(6,915,244)
Other assets	(751,886)	(1,925,917)
Net cash provided by operating activities	<u>23,125,374</u>	<u>29,806,767</u>
Cash flows from investing activities		
Purchase of property and equipment	(19,998,075)	(16,252,336)
Net purchases of investments and assets limited as to use	<u>(6,536,800)</u>	<u>(765,128)</u>
Net cash used in investing activities	(26,534,875)	(17,017,464)
Cash flows from financing activities		
Proceeds from restricted contributions	5,797,707	2,872,788
Payments of long-term debt	(4,837,976)	(4,098,701)
Proceeds from issuance of long-term debt	<u>-</u>	<u>1,735,674</u>
Net cash provided by financing activities	<u>959,731</u>	<u>509,761</u>
Net (decrease) increase in cash and cash equivalents	(2,449,770)	13,299,064
Cash and cash equivalents		
Beginning of year	<u>67,663,855</u>	<u>54,364,791</u>
End of year	<u>\$ 65,214,085</u>	<u>\$ 67,663,855</u>
Supplemental noncash investing activities		
Change in property and equipment acquired through accounts payable	<u>\$ (1,852,324)</u>	<u>\$ (1,531,283)</u>
Supplemental noncash financing activities		
Assets and liabilities acquired through capital lease obligations	<u>\$ 1,997,588</u>	<u>\$ 409,488</u>
Supplementary cash flow information		
Cash paid for interest	<u>\$ 1,303,254</u>	<u>\$ 1,169,399</u>

The accompanying notes are an integral part of these statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2018 and 2017

NOTE A - ORGANIZATION AND BASIS OF PRESENTATION

Beebe Medical Center, Inc., d/b/a Beebe Healthcare (the “Medical Center”) is a not-for-profit, tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and is incorporated in Delaware. The Medical Center, located in Lewes, Delaware, is the sole member of the following affiliates: Delmarva Health Network, LLC (“DHN”), Beebe Physician Network, d/b/a Beebe Medical Group (“BPN”), and Beebe Medical Foundation (the “Foundation”), collectively, “the System.” The System generally treats patients from Sussex County, Delaware and surrounding areas.

DHN was originally organized as an accountable-care organization (“ACO”) created as a Delaware Limited Liability Company to coordinate patient care and manage chronic diseases to improve patient outcomes and patient experience. During the year ended June 30, 2018, DHN was reorganized and is no longer an ACO, rather a clinically integrated network. DHN is treated as a disregarded entity for Federal tax purposes as its operations are covered under the Federal tax exemption of the Medical Center.

BPN is a not-for-profit tax-exempt corporation that operates a physician network providing integrated physician services in coordination with the Medical Center. BPN operates a hospitalist program, 11 primary care practices, 4 walk-in offices, 3 wellness centers and 12 specialty practices, and employs 71 physicians as of June 30, 2018.

The Foundation is a not-for-profit, tax-exempt corporation, which engages in fundraising activities solely for the benefit of the Medical Center.

The consolidated financial statements of Beebe Medical Center, Inc. include the Medical Center, DHN, BPN and the Foundation. All significant inter-company transactions and accounts have been eliminated.

The accompanying consolidated financial statements and supplementary consolidating information have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“US GAAP”).

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Use of Estimates

The preparation of consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant management estimates and assumptions relate to the determination of allowance for doubtful accounts and contractual allowances for patient accounts receivable, estimated third-party payor settlements, useful lives of property and equipment, actuarial estimates for accrued retirement benefits, professional liability and workers’ compensation costs, the asset retirement obligation and the reported fair values of certain of the assets and liabilities. Actual results could differ from those estimates.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

2. Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with original maturities of three months or less, excluding amounts limited as to use by board designation or donor restrictions or other arrangements under trust agreements.

3. Prepaid Supplies

Prepaid supplies are valued at cost using the first-in first-out costing method and represent approximately 5% and 6%, respectively, of total current assets at June 30, 2018 and 2017.

4. Investments

Investments in equity and debt securities, including mutual funds and exchange-traded funds, with readily determinable fair values are measured at fair value. Fair values are based on quoted market prices. Investment income on assets limited as to use under bond indenture agreements is recorded as other revenue. All other investment income and realized gains and losses on investments are recorded as nonoperating gains and losses, or as a change to temporarily or permanently restricted net assets, if such income is restricted by the donor. Unrealized gains and losses on all investments are excluded from the excess of revenues and gains over expenses and reported as a separate component of changes in net assets, except when the fair value of a security has declined below cost and is deemed to be other than temporary, impairment has occurred and the excess cost over fair value is included in excess of revenues and gains over expenses.

Investment securities, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the consolidated financial statements.

5. Assets Limited as to Use

Assets limited as to use by the Board of Directors (the "Board") are resources that have been designated by the Board for specific purposes. Assets limited as to use under bond indenture agreements are held by a trustee for the purchase of property and equipment. Assets limited as to use collateral funds are held in a separate account as collateral for the line of credit (Note I). Assets limited as to use externally restricted by donors are held until the donor restrictions have been met. Other board designated assets of \$1,838,339 at both June 30, 2018 and 2017 are comprised of the adjusted cost of land held for sale.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

6. Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method, with depreciation beginning the month the asset is put into service. Interest costs associated with the construction of certain capital assets is capitalized and amortized over the life of the asset being depreciated. The range for depreciation is as follows:

Land improvements	3-21 years
Buildings and fixed equipment	10-50 years
Moveable equipment	3-20 years

Capital leases are recognized as an asset and also as a liability for future payments to be made on the leased asset in the month the equipment is put into service. The lease is recognized on the consolidated statements of operations and changes in net assets through depreciation expense and interest expense associated with the lease payment. All of the capital leases are included in movable equipment.

Gifts of long-lived assets such as land, building or equipment are reported as unrestricted support, unless explicit donor stipulations specify how the donated assets must be used and are recorded at fair value on the date of the gift. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and unspent gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

7. Beneficial Interest in Perpetual Trust and Assets Held in Charitable Remainder Trust

Beneficial interest in perpetual trust represents the System's beneficial interest in a perpetual trust, which is administered by an independent trustee. Because the trust is perpetual and the original corpus cannot be violated, it is reported as permanently restricted net assets. The System has several charitable remainder trust arrangements with donors, the terms of which generally provide for an annual distribution to a donor beneficiary for their lifetime, after which the assets are distributed to the System. Assets held in charitable trusts have been recorded net of estimated present value of expected future cash flows to be paid to the beneficiary.

8. Deferred Financing Costs

Deferred financing costs are amortized over the life of the related bond issue. The accumulated amortization totaled \$291,518 and \$209,575 at June 30, 2018 and 2017, respectively.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

9. Goodwill

Other assets includes goodwill of \$3,104,085 at both June 30, 2018 and 2017.

The System performs an annual goodwill impairment assessment. Management has performed a goodwill step zero analysis in accordance with US GAAP. This approach does not require a calculation of the fair value of the System, rather a qualitative analysis of the operational and economic factors. If any of these assumptions change, the resulting decline in the estimated fair value could result in a material impairment charge to goodwill. No impairment charge is required at June 30, 2018, the date the assessment was performed.

10. Investment in Premier, Inc.

The System owns 172,074 Class B Common Shares of Premier, Inc., a publicly traded health care consulting and group purchasing organization. As part of the Amended and Restated Limited Partnership Agreement and Exchange Agreement between the System and Premier, Inc., the System has the right to exchange its Class B Common Shares for Class A Common shares of Premier, Inc. on a one-to-one basis vesting annually for a seven-year period beginning October 31, 2014. The System has not exchanged any Class B Common Shares to Class A Common Shares to date. The fair value of this vesting feature at June 30, 2018 and 2017 is \$3,966,787 and \$3,072,494, respectively, and is included in other assets.

11. Medical Malpractice Insurance

The System is insured for medical malpractice incidents through a claims-made policy. The provision for estimated medical malpractice claims includes actuarially determined estimates of the ultimate costs for both reported claims and incurred but not reported claims.

12. Allowance for Doubtful Accounts

The System provides an allowance for doubtful accounts for estimated losses resulting from the unwillingness or inability of patients to make payments for services. The allowance is determined by analyzing specific accounts and historical data and trends. Patient accounts receivable are charged off against the allowance for doubtful accounts when management determines that recovery is unlikely and the System ceases collection efforts.

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 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). For receivables associated with self-pay patients, the System records a significant provision for bad debts 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.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

The difference between the billed rates and the amounts actually collected after all reasonable internal collection efforts have been exhausted is charged off against the allowance for doubtful accounts. During 2018, the System increased the allowance for doubtful accounts by \$1,722,110 or 20%, offset by a 29% decrease in charity care. Federal regulations, the Affordable Care Act, insurance exchange, higher deductibles and restrictions on credit bureau reporting have all had an impact on this shift.

13. Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments due to future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as these matters are no longer subject to such audits, reviews, or investigations.

14. Other Operating Revenues

Other operating revenues consists mainly of income received from the operation of an employee cafeteria and deli, an adult daycare center, tuition for the school of nursing, property rentals, wellness clinics at local high schools, distributions from group purchasing organizations and interest income on assets limited as to use under bond indenture agreements.

15. Other Operating Expenses

Included in other operating expenses are consulting fees, computer expenses, purchased services and various other categories.

16. Excess of Revenues and Gains over Expenses

The consolidated statements of operations and changes in net assets include the excess of revenues and gains over expenses. Other changes in unrestricted net assets excluded from excess of revenues and gains over expenses and losses, consistent with industry practice, include net unrealized gains and losses on investments to the extent such losses are considered temporary, contributions for long-lived assets, and other changes in accrued retirement benefits.

17. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use are limited by donors to fund the acquisition of specific property and equipment expansion projects (Beebe Capital Campaign) including donor-restricted pledges. Permanently restricted net assets consist of assets that have been restricted by a donor to be maintained in perpetuity. Changes in restricted net assets include investment gains and losses, contributions, change in value of beneficial interest in perpetual trust, and net assets released from restrictions for property and equipment purchases.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

18. Donor-Restricted Gifts

Unconditional promises to give cash and other assets are reported at fair value at the date the promise to give is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions.

Donor-restricted pledges receivable at June 30, 2018 and 2017, follows:

	<u>2018</u>	<u>2017</u>
Unconditional promises expected to be collected in:		
Less than one year	\$ 382,956	\$ 197,151
One year to five years	<u>11,476,865</u>	<u>1,718,906</u>
	11,859,821	1,916,057
Less: unamortized discounts and allowance on contributions receivable	<u>(1,662,819)</u>	<u>(213,546)</u>
	<u>\$ 10,197,002</u>	<u>\$ 1,702,511</u>

Contributions receivable over more than one year are discounted using a discount rate of 4.5% applicable to the year in which the pledge was made.

On July 12, 2017, the System received a \$10,000,000 pledge from the Ma-Ran Foundation for the Beebe Capital Campaign. A stock payment of \$2,021,136 was received in September 2017. On July 17, 2018, subsequent to the consolidated balance sheet date, a stock payment of \$2,025,875 was received. The remaining gross balance of \$5,952,989 is committed to be paid over the next three years.

19. Fair Value Measurements

US GAAP defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The System is required to provide additional disclosures as part of its consolidated financial statements.

US GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability (exit price) in an orderly transaction between market participants at the measurement date. US GAAP also establishes a fair value hierarchy that classifies the inputs to valuation techniques used to measure fair value into one of the following three levels:

- Level 1 Unadjusted quoted prices in active markets for identical assets, exchange-traded securities and mutual funds with quoted prices or liabilities.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- Level 2 Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.
- Level 3 Unobservable inputs derived from extrapolation or interpolation that cannot be substantiated by market data including other investment manager specific inputs such as projected cash flows.

The carrying amounts reported on the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable and accrued expenses approximate their fair value. The fair value of assets limited as to use, investments, charitable remainder trust and beneficial interest in perpetual trusts are described in Note E. The fair value of pension assets is described in Note H. The fair value of long-term obligations is calculated based upon yields available in the quoted market for bonds or debt of similar quality. The carrying amount and the estimated fair value of long-term debt is described in Note I.

20. Tax Status

The System follows the accounting guidance for uncertainties in income tax positions which requires that a tax position be recognized or derecognized based on a “more likely than not” threshold. This applies to positions taken or expected to be taken in a tax return. The System does not believe its consolidated financial statements include any material uncertain tax positions. At June 30, 2018, the System’s tax years ended June 30, 2015 through 2018 for the federal tax jurisdiction remain open.

21. Recently Adopted Accounting Pronouncement

In March 2017, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This standard intends to make changes to employers that sponsor defined benefit pension and/or other postretirement benefit plans to present the net periodic benefit cost in the income statement. Employers will present the service cost component of net periodic benefit cost in the same income statement line item(s) as other employee compensation costs arising from services rendered during the period. Only the service cost component will be eligible for capitalization in assets. Employers will present the other components of the net periodic benefit cost separately from the line item(s) that include(s) the service cost and outside of any subtotal of operating income, if one is presented. The new standard is effective for annual financial statements after December 15, 2017. Early application is permitted. The System elected for early adoption of this standard during the year ended June 30, 2018. The effect of this change was to reclassify the current year expense less the service costs for both the pension and postretirement expenses. This change resulted in a reclassification of the expense from operating to nonoperating, totaling \$4,106,861 and \$3,467,855 for the years ended June 30, 2018 and 2017, respectively.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

22. Pending Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, to clarify the principles for recognizing revenue and to improve financial reporting by creating common revenue recognition guidance for US GAAP and International Financial Reporting Standards. The core principle of the 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 these goods and services. This standard is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early application is not permitted. An entity will apply the amendments in this update using either a full retrospective application, which applies the standard to each prior period presented, or under the modified retrospective application, in which an entity recognizes the cumulative effect of initially applying the new standard as an adjustment to the opening balance sheet of net assets at the date of initial application. Revenue in periods presented before that date will continue to be reported under guidance in effect before the change.

In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*, to make targeted improvements to how entities: (1) account for equity investments; (2) present and disclose financial instruments; and (3) measure the valuation allowance on deferred tax assets related to available-for-sale debt securities. The new standard is effective for fiscal years beginning after December 15, 2017. Early application of the guidance in ASU 2016-01 is not permitted.

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. This standard intends to make certain improvements to the current reporting requirements for not-for-profit entities including: (1) the presentation for two classes of net assets at the end of the period, rather than the currently required three classes, as well as the annual change in each of the two classes; (2) the removal of the requirement to present or disclose the indirect method (reconciliation) when using the direct method for the statement of cash flows; and (3) the requirement to provide various enhanced disclosures relating to various not-for-profit specific topics. The new standard is effective for annual financial statements beginning after December 15, 2017.

In February 2016, the FASB issued ASU 2016-02, *Leases*, which requires that most leased assets be recognized on the balance sheet as assets and liabilities for the rights and obligations created by these leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018. Early application is permitted. An entity is required to apply the amendments in the standard under the modified retrospective transition approach. This approach includes a number of optional practical expedients, which are described in the final standard. Under these practical expedients, an organization will continue to account for leases that commence before the effective date in accordance with current US GAAP, unless the lease is modified. However, lessees are required to recognize on the balance sheet leased assets and liabilities for operating leases at each reporting date.

The System has not determined the impact of the new standards at this time.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE C - CHARITY CARE

The System provides care to patients who meet certain criteria under its charity care policy at amounts less than its established rates. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

The System maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy, and the estimated cost of those services and supplies using a cost-to-charge ratio.

The cost of charity care provided is estimated at \$2,876,000 and \$4,054,000 for the years ended June 30, 2018 and 2017, respectively.

NOTE D - NET PATIENT SERVICE REVENUE

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 payment arrangements of the third-party payors within which the System transacts a significant volume of business follows:

Medicare and Medicaid

Inpatient acute care services rendered to and defined capital costs related to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors based on a DRG (Diagnostic Classification Groupings). Outpatient payments are primarily based on a combination of prospectively determined ambulatory payment classifications and fee schedules referred to as APCs. Nursing education costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology subject to certain limitations. The System is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare fiscal intermediary. The Medicare cost reports have been audited and settled by the Medicare fiscal intermediary through June 30, 2016.

Delaware Health and Social Services has contracted with two managed care companies for the provision of health care services to Medicaid beneficiaries. The two managed care companies have, in turn, contracted with the System for the provision of physician, acute inpatient and outpatient services under which the System is generally paid based upon inpatient case rates, subject to outlier payments, outpatient and emergency as a percentage of the State of Delaware Medicaid rates, and physician services based on a fee schedule. All reimbursement rates are based on a percentage of the State of Delaware Medicaid reimbursement.

The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments for eligible hospitals and professionals that implement and achieve meaningful use of certified electronic health record (“EHR”) technology. For Medicare and Medicaid EHR incentive payments, the System utilizes the contingency accounting model to recognize revenue. Under this accounting policy, EHR incentive payments are recognized as revenue when final audit and settlement is complete by the federal government or its designee.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE D - NET PATIENT SERVICE REVENUE - Continued

In the opinion of management, adequate provision has been made for any adjustments that may result from final settlement of Medicare and Medicaid cost reports. Net patient service revenue increased approximately \$5,540,000 and \$9,433,000 for the years ended June 30, 2018 and 2017, respectively, as a result of favorable adjustments and settlements to estimates previously recorded applicable to prior-year third-party cost reports, including approximately \$691,000 and \$1,388,000 for the years ended June 30, 2018 and 2017, respectively, of EHR revenue.

Net revenue from the Medicare and Medicaid programs accounted for approximately 42% and 10%, and 42% and 11%, respectively, of the System's net patient service revenue for the years ended June 30, 2018 and 2017. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation, and noncompliance could result in significant regulatory action, including fines and penalties. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The System believes that it is in compliance with applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subjected to future government review and interpretations as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medicaid program.

Commercial Insurance

The System has contracted with Highmark Blue Cross of Delaware ("Highmark"), commercial insurers, carriers, and health maintenance organizations. The basis for payment to the System for covered inpatient, outpatient and physician services under these agreements includes discounted charges or fee schedules for certain outpatient services and physician services subject to co-pay and deductible provisions of policies. The basis for payment for inpatients is the Medicare DRG Methodology with modified DRG weights relative to the Highmark population.

For uninsured patients who do not qualify for charity care, the System recognizes revenue based on established rates, subject to certain discounts as determined by the System. An estimated provision for bad debts is recorded that results in net patient service revenue being reported at the net amount expected to be received. The System has determined that patient service revenue is primarily recorded prior to assessing the patient's ability to pay, and as such, the entire provision for bad debts related to patient revenue is recorded as a deduction from patient service revenue in the accompanying consolidated statements of operations and changes in net assets.

Percentages of patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized from these major payor sources based on primary insurance designation, for the years ended June 30, 2018 and 2017, are as follows:

	<u>Third-Party Payors</u>	<u>Self-Pay</u>	<u>Total All Payors</u>
<u>2018</u>			
Patient service revenue (net of contractual allowances and discounts)	<u>97%</u>	<u>3%</u>	<u>100%</u>
<u>2017</u>			
Patient service revenue (net of contractual allowances and discounts)	<u>99%</u>	<u>1%</u>	<u>100%</u>

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE D - NET PATIENT SERVICE REVENUE - Continued

Deductibles and copayments under third-party payment programs within the third-party payor amount above are patients' responsibility, and the System considers these amounts in its determination of the provision for bad debts based on collection experience.

NOTE E - INVESTMENTS

The composition of investments classified as assets limited as to use, at June 30, 2018 and 2017, is set forth in the following table:

	<u>2018</u>	<u>2017</u>
Assets limited as to use		
Cash and cash equivalents	\$ 3,757,508	\$ 3,156,738
Domestic and foreign equities	99,856,448	75,539,001
Mutual funds/exchange-traded funds ("ETFs")	<u>-</u>	<u>14,296,384</u>
	<u>\$ 103,613,956</u>	<u>\$ 92,992,123</u>

The fair value hierarchy of assets limited as to use, investments, the assets held in charitable remainder trust, and the beneficial interest in perpetual trust at June 30, 2018 and 2017, classified by the market approach valuation technique, is as follows:

<u>June 30, 2018</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets				
Cash and cash equivalents	\$ 3,757,508	\$ -	\$ -	\$ 3,757,508
Domestic and foreign equities	99,856,448	-	-	99,856,448
Assets held in charitable remainder trust	-	-	672,432	672,432
Beneficial interest in perpetual trust	<u>-</u>	<u>-</u>	<u>336,878</u>	<u>336,878</u>
	<u>\$ 103,613,956</u>	<u>\$ -</u>	<u>\$ 1,009,310</u>	<u>\$ 104,623,266</u>
 <u>June 30, 2017</u>				
Assets				
Cash and cash equivalents	\$ 3,156,738	\$ -	\$ -	\$ 3,156,738
Domestic and foreign equities	75,539,001	-	-	75,539,001
Mutual funds/ETFs	14,296,384	-	-	14,296,384
Assets held in charitable remainder trust	-	-	643,713	643,713
Beneficial interest in perpetual trust	<u>-</u>	<u>-</u>	<u>327,797</u>	<u>327,797</u>
	<u>\$ 92,992,123</u>	<u>\$ -</u>	<u>\$ 971,510</u>	<u>\$ 93,963,633</u>

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE E - INVESTMENTS - Continued

The following is a comparative roll forward of the Level 3 assets held in charitable remainder trust and beneficial interest in perpetual trust for the years ended June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Beginning of year balance	\$ 971,510	\$ 915,117
Net unrealized gains	<u>37,800</u>	<u>56,393</u>
Ending of year balance	<u>\$ 1,009,310</u>	<u>\$ 971,510</u>

Investment income and gains for assets limited as to use and cash equivalents are comprised of the following for the years ended June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Other revenues		
Investment income	<u>\$ 5,214</u>	<u>\$ 2,075</u>
Nonoperating gains		
Investment income	\$ 1,791,929	\$ 1,596,256
Net realized gains on sales of investments	<u>2,346,629</u>	<u>1,400,687</u>
	<u>\$ 4,138,558</u>	<u>\$ 2,996,943</u>
Other changes in unrestricted net assets		
Changes in unrealized gains and losses on investments	<u>\$ 1,738,404</u>	<u>\$ 5,553,029</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE F - PROPERTY AND EQUIPMENT

A summary of property and equipment at June 30, 2018 and 2017 follows:

	<u>2018</u>	<u>2017</u>
Property and equipment		
Land	\$ 10,542,972	\$ 10,595,946
Land improvements	913,485	1,188,972
Building and fixed equipment	182,085,771	181,376,757
Moveable equipment	<u>150,147,684</u>	<u>138,598,658</u>
Total property and equipment	343,689,912	331,760,333
Less: Accumulated depreciation and amortization	<u>(216,252,628)</u>	<u>(201,837,330)</u>
Subtotal	127,437,284	129,923,003
Construction in progress	<u>16,132,566</u>	<u>13,272,970</u>
Total property and equipment, net	<u>\$ 143,569,850</u>	<u>\$ 143,195,973</u>
Capital leases, included in property and equipment		
Moveable equipment	\$ 17,052,254	\$ 14,312,314
Less: Accumulated amortization	<u>(13,302,856)</u>	<u>(11,078,774)</u>
	<u>\$ 3,749,398</u>	<u>\$ 3,233,540</u>

Depreciation and amortization expense related to property and equipment for the years ended June 30, 2018 and 2017 was \$20,091,385 and \$19,529,907, respectively.

At June 30, 2018, the System is committed to property and equipment purchases totaling approximately \$9,667,000.

NOTE G - ENDOWMENTS

The System's endowment includes approximately 20 individual donor-restricted endowment funds and three funds designated by the Board to function as endowments. The net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor restrictions.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE G - ENDOWMENTS - Continued

The System's interpretation of the State of Delaware enacted version of the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") requires a not-for-profit organization to classify a portion of donor-restricted endowment fund of perpetual endurance as permanently restricted net assets. The amount classified as permanently restricted is the amount of the fund that must be retained permanently in accordance with explicit donor stipulations or that the organization's board determines must be retained permanently consistent with the relevant law. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the System in a manner consistent with the standard of prudence prescribed by UPMIFA.

In accordance with UPMIFA, the System considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- a. The duration and preservation of the fund.
- b. The purpose of the organization and the donor-restricted endowment fund.
- c. General economic conditions.
- d. The possible effect of inflation and deflation.
- e. The expected total return from income and appreciation of investments.
- f. Other resources of the organization.
- g. Investment policies of the organization.

Endowment funds are categorized in the following net asset classes as of June 30, 2018 and 2017:

	2018		2017	
	Board designated endowment funds	Donor- restricted endowment funds	Board designated endowment funds	Donor- restricted endowment funds
Unrestricted	\$ 3,421,929	\$ -	\$ 3,171,053	\$ -
Temporarily restricted		1,856,442	-	1,679,854
Permanently restricted	-	2,497,660	-	2,400,365
Total endowment funds	\$ 3,421,929	\$ 4,354,102	\$ 3,171,053	\$ 4,080,219

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE G - ENDOWMENTS - Continued

Changes in endowment funds by net asset classification for the year ended June 30, 2018 are summarized as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 3,171,053	\$ 1,679,854	\$ 2,400,365	\$ 7,251,272
Donations	38,270	250	49,432	87,952
Endowment match	17,725	-	17,725	35,450
Transfer to spending accounts	(139,749)	(83,731)	-	(223,480)
Other	(80,207)	80,207	-	-
Investment return:				
Investment income	90,145	38,451	14,707	143,303
Net appreciation (realized and unrealized)	326,349	142,141	15,515	484,005
Administrative expense	<u>(1,657)</u>	<u>(730)</u>	<u>(84)</u>	<u>(2,471)</u>
Total investment return	<u>414,837</u>	<u>179,862</u>	<u>30,138</u>	<u>624,837</u>
Endowment net assets, end of year	<u>\$ 3,421,929</u>	<u>\$ 1,856,442</u>	<u>\$ 2,497,660</u>	<u>\$ 7,776,031</u>

Changes in endowment funds by net asset classification for the year ended June 30, 2017 are summarized as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 2,691,499	\$ 1,191,594	\$ 2,284,449	\$ 6,167,542
Donations	-	-	60,680	60,680
Endowment match	(15,744)	15,744	-	-
Disbursed for restricted purpose	-	(29,950)	-	(29,950)
Transfer to spending accounts	(154,932)	(35,821)	-	(190,753)
Other	(182,281)	182,281	-	-
Investment return:				
Investment income	92,176	38,508	21,701	152,385
Net appreciation (realized and unrealized)	752,483	322,529	34,070	1,109,082
Administrative expense	<u>(12,148)</u>	<u>(5,031)</u>	<u>(535)</u>	<u>(17,714)</u>
Total investment return	<u>832,511</u>	<u>356,006</u>	<u>55,236</u>	<u>1,243,753</u>
Endowment net assets, end of year	<u>\$ 3,171,053</u>	<u>\$ 1,679,854</u>	<u>\$ 2,400,365</u>	<u>\$ 7,251,272</u>

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE G - ENDOWMENTS - Continued

Description of Amounts classified as Temporarily Restricted Net Assets and Permanently Restricted Net Assets (Endowments Only)

	June 30,	
	<u>2018</u>	<u>2017</u>
Temporarily restricted net assets		
Restricted for program support	\$ <u>1,856,442</u>	\$ <u>1,679,854</u>
Total endowment assets classified as temporarily restricted net assets	\$ <u>1,856,442</u>	\$ <u>1,679,854</u>
Permanently restricted net assets		
Restricted for nursing scholarships	\$ 809,406	\$ 754,227
Restricted for program support	<u>1,688,254</u>	<u>1,646,138</u>
Total endowment assets classified as permanently restricted net assets	\$ <u>2,497,660</u>	\$ <u>2,400,365</u>

Endowments with Eroded Corpus

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Foundation to retain as a fund of perpetual duration. There were no deficiencies of this nature that are reported in unrestricted net assets at June 30, 2018 and 2017.

Return Objectives and Risk Parameters

The System has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding for programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor specified period, as well as board designated funds. Under this policy, the endowment assets are invested in a manner that is intended to produce results that meet or exceed investment returns of a blended portfolio of 64% equity/36% fixed income as measured by the Russell 3000 Index TR and MSCI All Country World ex-US TR for equities and the Barclays Capital Aggregate Bond Index for fixed income. The System expects its endowment funds, over the long term, to earn a total real return (inflation-adjusted return), net of investment fees that achieves at least the fund's spending rate. Actual returns in any given year may vary from this amount.

Under the System's policy, the board designated assets are invested in a manner that is intended to produce results that meet or exceed investment returns of a blended portfolio of 64% equity/36% fixed income as measured by the Russell 3000 Index TR and MSCI All Country World ex-US TR for equities and the Barclays Capital Aggregate Bond Index for fixed income. The System expects the total annualized net investment return from all investments and each asset class to meet or exceed the annualized return of the designated benchmark for rolling five-year periods. Actual returns in any given year may vary from this amount.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE G - ENDOWMENTS - Continued

Endowment funds will also maintain sufficient liquidity to meet payment obligations and other expenses, while minimizing the risk of large losses.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate of return objectives, the System relies on a total return strategy in which the investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The System targets a well-diversified, multi-asset portfolio, which facilitates control of investment risk and affords reasonably predictable long-term investment returns. Significant diversification can be accomplished through asset allocation, portfolio structure, and the selection of different investment managers.

NOTE H - RETIREMENT PLANS

Defined Benefit Plan

The System has a noncontributory defined benefit pension plan (“Pension benefits”) covering a number of employees hired before January 1, 2014. The employees hired after January 1, 2014, are offered a defined contribution plan. The benefits are based on years of service and the employees’ compensation. The System makes contributions to the plan based upon actuarially determined amounts intended to provide not only for benefits attributed to service to date, but also for those expected to be earned in the future. The mortality table used for projecting the benefit obligations is the RP-2014 Generational Mortality Table with annual updates for projected improvements.

In addition, the System sponsors a defined benefit health care plan that provides postretirement health care benefits (“Other benefits”) to employees with at least 10 years of continuous service (working 1,000 hours in each year) and who are at least 55 years of age. During 2013, the Other benefits plan was closed, and participants who were age 45 or older, with at least 10 years of service as of January 1, 2013, remained in the plan. The Other benefits plan offers new participants a subsidy of \$2,000 per year to enter into a Medicare supplemental plan. During 2018, changes were made to the subsidy to include a reduction in the annual increases in the subsidy from 5% to 1%. The annual increase will be assessed periodically to ensure the System is offering a competitive benefit.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE H - RETIREMENT PLANS - Continued

The following table summarizes information about the benefit plans:

	Pension benefits		Other benefits	
	June 30,			
	2018	2017	2018	2017
Accumulated benefit obligation	\$ <u>96,203,349</u>	\$ <u>97,861,973</u>	\$ <u>N/A</u>	\$ <u>N/A</u>
Change in benefit obligation				
Benefit obligation at beginning of year	\$ 106,604,444	\$ 98,391,821	\$ 41,638,714	\$ 43,813,702
Service cost	4,492,807	4,763,465	705,785	875,414
Interest cost	3,726,994	3,113,886	1,396,198	1,270,378
Plan participants' contributions	-	-	191,579	171,257
Actuarial (gain) loss	(5,320,421)	2,523,745	(15,473,419)	(2,891,427)
Plan amendments	-	-	(3,318,227)	-
Benefits paid	<u>(4,876,971)</u>	<u>(2,188,473)</u>	<u>(1,930,972)</u>	<u>(1,600,610)</u>
Benefit obligation at end of year	<u>104,626,853</u>	<u>106,604,444</u>	<u>23,209,658</u>	<u>41,638,714</u>
Change in plan assets				
Fair value of the plan assets at beginning of year	70,003,789	61,575,623	-	-
Actual return on plan assets	4,869,512	5,616,639	-	-
Employer contributions	6,000,000	5,000,000	1,739,393	1,429,353
Plan participants' contributions	-	-	191,579	171,257
Benefits paid	<u>(4,876,971)</u>	<u>(2,188,473)</u>	<u>(1,930,972)</u>	<u>(1,600,610)</u>
Fair value of the plan assets at end of year	<u>75,996,330</u>	<u>70,003,789</u>	<u>-</u>	<u>-</u>
Funded status at year end	\$ <u>(28,630,523)</u>	\$ <u>(36,600,655)</u>	\$ <u>(23,209,658)</u>	\$ <u>(41,638,714)</u>
Net amounts recognized in the consolidated balance sheets consist of:				
Current liabilities, as accounts payable and accrued expenses	\$ -	\$ -	\$ (1,710,000)	\$ (1,795,000)
Noncurrent liabilities	<u>(28,630,523)</u>	<u>(36,600,655)</u>	<u>(21,499,658)</u>	<u>(39,843,714)</u>
Accrued retirement benefits	\$ <u>(28,630,523)</u>	\$ <u>(36,600,655)</u>	\$ <u>(23,209,658)</u>	\$ <u>(41,638,714)</u>

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE H - RETIREMENT PLANS - Continued

	Pension benefits		Other benefits	
	June 30,			
	2018	2017	2018	2017
Amounts recognized in unrestricted net assets but not yet recognized in net periodic benefit costs consist of:				
Net actuarial loss (gain)	\$ 25,909,586	\$ 33,543,684	\$ (351,619)	\$ 16,770,566
Prior service credit	<u>-</u>	<u>-</u>	<u>(3,318,227)</u>	<u>(109,262)</u>
	<u>\$ 25,909,586</u>	<u>\$ 33,543,684</u>	<u>\$ (3,669,846)</u>	<u>\$ 16,661,304</u>
Components of net periodic benefit cost:				
Components recognized in salaries, benefits, physician fees and contract labor:				
Service cost	\$ 4,492,807	\$ 4,763,465	\$ 705,785	\$ 875,414
Components recognized in nonoperating gains (losses):				
Interest cost	3,726,994	3,113,886	1,396,198	1,270,378
Expected return on plan assets	(5,065,771)	(4,437,951)	-	-
Amortization of prior service cost (credit)	-	103,433	(109,262)	(1,220,755)
Amortization of actuarial loss	<u>2,509,936</u>	<u>2,676,553</u>	<u>1,648,766</u>	<u>1,962,311</u>
	<u>1,171,159</u>	<u>1,455,921</u>	<u>2,935,702</u>	<u>2,011,934</u>
Net periodic benefit cost	5,663,966	6,219,386	3,641,487	2,887,348
Other changes in benefit obligations recognized in other changes in unrestricted net assets:				
Net gain	(7,634,098)	(1,331,496)	(17,122,185)	(4,853,738)
Prior service (cost) credit	<u>-</u>	<u>(103,433)</u>	<u>(3,208,965)</u>	<u>1,220,755</u>
	<u>(7,634,098)</u>	<u>(1,434,929)</u>	<u>(20,331,150)</u>	<u>(3,632,983)</u>
Total recognized in net benefit cost and other changes in unrestricted net assets	<u>\$ (1,970,132)</u>	<u>\$ 4,784,457</u>	<u>\$ (16,689,663)</u>	<u>\$ (745,635)</u>

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE H - RETIREMENT PLANS - Continued

At June 30, 2018, the expected estimated amount from unrestricted net assets into net periodic benefit cost for the next year is:

	<u>Pension benefits</u>	<u>Other benefits</u>
Net actuarial loss	<u>\$ 1,866,000</u>	<u>\$ 2,509,000</u>

Assumptions used in the accounting for benefit obligations were:

	<u>Pension benefits</u>		<u>Other benefits</u>	
	<u>June 30,</u>			
	<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
Weighted-average assumptions used to determine benefit obligations were:				
Discount rate	4.24%	3.93%	4.16%	3.88%
Rate of compensation increase	4.00%	4.00%	N/A	N/A
Measurement date	June 30	June 30	June 30	June 30
Weighted-average assumptions used to determine net periodic benefit costs were:				
Discount rate	3.93%	3.74%	3.88%	3.71%
Expected long-term return on plan assets	7.00%	7.00%	N/A	N/A
Rate of compensation increase	4.00%	4.00%	N/A	N/A
			<u>Other benefits</u>	
			<u>2018</u>	<u>2017</u>

Trend rate of increase per capita cost of covered health care benefits:

Initial trend	7%	7%
Ultimate trend	5%	5%

The ultimate trend rate will be reached in 2023.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE H - RETIREMENT PLANS - Continued

Assumed health care cost trend rates have a significant effect on the amounts reported for the other benefits. A one-percentage-point change in the assumed health care cost trend rate would have the following effects:

	<u>1% increase</u>	<u>1% (decrease)</u>
Incremental effect on total service and interest cost components of benefit cost	\$ 432,630	\$ (342,309)
Incremental effect on postretirement benefit obligation	337,387	(318,407)

Fair Value of the Plan Assets

The tables below present the fair values of the pension assets by level within the fair value hierarchy:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<u>June 30, 2018</u>				
Assets				
Cash and cash equivalents	\$ 827,149	\$ -	\$ -	\$ 827,149
Fixed income	26,044,738	-	-	26,044,738
Domestic and foreign equities	<u>49,124,443</u>	<u>-</u>	<u>-</u>	<u>49,124,443</u>
	<u>\$ 75,996,330</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 75,996,330</u>
<u>June 30, 2017</u>				
Assets				
Cash and cash equivalents	\$ 552,846	\$ -	\$ -	\$ 552,846
Fixed income	26,739,494	-	-	26,739,494
Domestic and foreign equities	39,950,655	-	-	39,950,655
Mutual funds/ETFs	<u>2,760,794</u>	<u>-</u>	<u>-</u>	<u>2,760,794</u>
	<u>\$ 70,003,789</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 70,003,789</u>

Investment Strategies

The investment objectives of the defined benefit plan are to maintain the purchasing power of the assets and future contributions, to maintain the ability to pay all benefits and expense obligations when due, to maximize returns within prudent levels of risk, and to control the cost of administering the defined benefit plan and managing investments. Assets are diversified throughout a multitude of asset classes. The Investment Committee, as sub-committee of the Board of Directors, has established the following basic asset allocation parameters:

Cash and cash equivalents	0% - 5%
Bond portfolio	34% - 44%
Equity portfolio	55% - 65%

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE H - RETIREMENT PLANS - Continued

Certain types of investments are generally prohibited (e.g., private placements, commodities, real estate, derivatives and options, short and margin transactions). Professional investment managers manage the plan's investment, and investment objectives include stability, capital preservation and diversification, rate of return, investment quality, liquidity and turnover. Investment consultants report quarterly to the Finance and Investment Committees. In selecting the expected long-term rate of return on assets, the System considered the asset allocation policy and the expected returns likely to be earned over the life of the defined benefit plan.

The Pension benefits' weighted average asset allocation at June 30, 2018 and 2017, by asset category, follows:

	<u>Pension benefits</u>	
	<u>2018</u>	<u>2017</u>
Plan asset allocation		
Cash and cash equivalents	1%	1%
Bond portfolio:		
Fixed income	34	38
Equity portfolio:		
Domestic and foreign equities	65	57
Mutual funds/ETFs	<u>-</u>	<u>4</u>
 Total	 <u>100%</u>	 <u>100%</u>

Cash Flows

The System expects to contribute approximately \$6,000,000 in Pension benefits and \$1,710,000 related to Other benefits, respectively, for contributions to the plans during the year ending June 30, 2019.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be made in the next ten years:

	<u>Pension</u>	<u>Other</u>
	<u>benefits</u>	<u>benefits</u>
2019	\$ 2,876,251	\$ 1,710,000
2020	3,568,783	1,739,000
2021	4,047,161	1,802,000
2022	3,965,693	1,842,000
2023	4,631,021	1,854,000
2024-2028	28,564,794	9,027,000

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE H - RETIREMENT PLANS - Continued

Defined Contribution Plan

The System offers a defined contribution retirement plan (the "Plan"), and all employees are eligible at date of hire. The System matches 50% of the first 4% of eligible compensation and provides for 100% vesting immediately. Loans are permitted with this Plan. The System provides for a discretionary employer contribution for all employees, exclusive of the Beebe Medical Group, who are hired after December 31, 2013 and have one year of service. The employer contribution is based on eligible salary and years of vested service, and is 2% of eligible salary for participants with 10 years or less of vested service, 3% of eligible salary for participants with more than 10 years but less than 21 years of vested service, and 4% of eligible salary for participants with more than 20 years of vested service. The Plan provides for 100% vesting of the discretionary employer contributions after three years of vested service. Loans are not permitted on the discretionary employer contributions. The System's expense for the Plan for the years ended June 30, 2018 and 2017 was \$3,129,490 and \$2,706,502, respectively.

NOTE I - LONG-TERM DEBT

A summary of long-term debt at June 30, 2018 and 2017 follows:

	<u>2018</u>	<u>2017</u>
Delaware Health Facilities Authority Revenue Bonds, Series 2015A including unamortized premium of \$251,700 and \$294,147 at June 30, 2018 and 2017, respectively	\$ 13,361,700	\$ 14,254,147
Delaware Health Facilities Authority Variable Rate Revenue Bonds, Series 2014A	27,660,000	28,540,000
Delaware Health Facilities Authority Revenue Bonds, Series 2014B	4,800,000	5,465,000
Obligations under capital leases, at imputed interest rates of 1.00% to 8.34%	<u>2,667,680</u>	<u>3,096,537</u>
	48,489,380	51,355,684
Less: Unamortized deferred financing costs, net	(557,141)	(639,084)
Current portion	<u>(3,593,150)</u>	<u>(4,379,822)</u>
	<u>\$ 44,339,089</u>	<u>\$ 46,336,778</u>

On September 3, 2015, Delaware Health Facilities Authority (the "Authority") and the Medical Center issued Beebe Medical Center Revenue Bonds Series 2015A (the "2015A Bonds") with a principal value of \$15,820,000. The 2015A Bonds include serial bonds bearing interest at rates ranging from 3.00% to 5.00%, with maturities annually through June 1, 2030, with principal payment ranging from \$850,000 to \$1,335,000. The 2015A Bonds were issued to (1) refund for savings the outstanding par amount of, plus accrued interest on the Series 2005A Bonds, and (2) pay a portion of the issuance costs related. The 2015A Bonds are subject to optional redemption prior to maturity, at the direction of the Medical Center, as a whole or in part by lot, on or after June 1, 2025 at a price of 100% of principal amount plus accrued interest.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE I - LONG-TERM DEBT - Continued

On June 1, 2014, the Authority and the Medical Center issued Beebe Medical Center Variable Rate Revenue Bonds Series 2014A (the "2014A Bonds") with a maximum principal value of \$31,020,000 and Beebe Medical Center Revenue Bonds Series 2014B (the "2014B Bonds") with a principal value of \$9,670,000. As of June 30, 2017, the Medical Center had drawn all of the funds available. The 2014A Bonds were issued to (1) redeem the outstanding principal amount of the Authority's Variable Rate Refunding Revenue Bonds, Beebe Medical Center Project, Series 2002 and (2) to finance capital expenditures. The 2014B Bonds were issued to redeem the outstanding \$12,740,000 of the Authority's Revenue Refunding Bonds, Beebe Medical Center Project Series 2004A. The 2014A Bonds and the 2014B Bonds were a direct placement with PNC, NA; both have an expiration date of June 2, 2021, and are subject to a mandatory redemption.

The 2014A Bonds bear interest at 75.5% of one-month LIBOR plus 0.81%, which was 2.32% and 1.72% on June 30, 2018 and 2017, respectively. The 2014A Bonds mature in June 2040. The 2014B Bonds bear interest at a fixed rate of 2.02% and mature in June 2024. Neither bond series has a mandatory sinking fund; however, both are subject to optional redemption prior to the stated maturity, at the direction of the Medical Center, at a redemption price equal to 100% of principal plus accrued interest.

The Medical Center has granted the Authority a security interest in certain real and personal property and granted the Trustee (The Bank of New York Trust) a security interest in its gross revenue. The payments required by the Medical Center are assigned and pledged by the Authority to the Trustee to secure the payment of the bonds.

The agreements require the Medical Center to meet various financial and non-financial covenants, with the most restrictive requiring the Medical Center to maintain 75 days of operating cash as of the end of each semi-annual period ending June 30 and December 31, and to generate "net income available for debt service," as defined therein, of 110% of maximum annual debt service for each of the years ended June 30, 2018 and 2017. Additionally, summary financial information is required quarterly. The Medical Center was in compliance with such financial covenants at June 30, 2018 and 2017.

Scheduled principal repayments on long-term debt are as follows:

	Series <u>2015A Bonds</u>	Series <u>2014A Bonds</u>	Series <u>2014B Bonds</u>	Obligations Under Capital <u>Leases</u>
Year ending June 30,				
2019	\$ 885,000	\$ 905,000	\$ 695,000	\$ 1,184,271
2020	925,000	930,000	735,000	696,624
2021	970,000	960,000	775,000	443,962
2022	995,000	990,000	820,000	404,773
2023	1,025,000	1,020,000	865,000	99,403
Thereafter	<u>8,310,000</u>	<u>22,855,000</u>	<u>910,000</u>	<u>-</u>
	13,110,000	27,660,000	4,800,000	2,829,033
Less: amount representing interest under capital lease obligations	<u>-</u>	<u>-</u>	<u>-</u>	<u>(161,353)</u>
	<u>\$ 13,110,000</u>	<u>\$ 27,660,000</u>	<u>\$ 4,800,000</u>	<u>\$ 2,667,680</u>

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE I - LONG-TERM DEBT - Continued

The fair value of the long-term debt, exclusive of obligations under capital leases, was approximately \$45,635,000 and \$48,356,000 at June 30, 2018 and 2017, respectively. Fair value of the long-term debt is based on current traded value, excluding accrued interest. As such, management has classified this as Level 2 within the fair value hierarchy.

The Medical Center has a \$5,000,000 line of credit with a bank, which expires June 30, 2019. At June 30, 2018, \$2,608,000 has been used as a letter of credit for the Medical Center's workers' compensation insurance program. The letter of credit is collateralized by specific investments held by the Medical Center that are classified as assets limited as to use on the consolidated balance sheets. The stand-by letters of credit automatically renew each year at various dates throughout the year.

NOTE J - INSURANCE PROGRAMS

The System carries claims-made professional liability insurance in the amount of \$1,000,000 per claim and \$3,000,000 annual aggregate through a commercial policy. The System is subject to a \$500,000 limit per claim and a \$2,000,000 annual aggregate deductible under this policy. The System carries umbrella coverage up to \$10,000,000 per occurrence and in the aggregate with a commercial policy plus an excess coverage up to \$20,000,000 with two different insurance companies for \$10,000,000 each. The umbrella and excess policies provide coverage for malpractice and general liability, auto, workers' compensation and helipad.

The System has workers' compensation coverage with an insurance company on an occurrence basis. The policy provides coverage in accordance with the workers' compensation laws of the State of Delaware and is subject to a self-retention limit of \$400,000 per claim and \$4,650,000 in the annual aggregate.

The System recorded estimated claims payable based on actuarial reports, and has provided for future claims and recorded estimated receivables against those claims at June 30, 2018 and 2017 as follows:

	Professional		Workers' Compensation	
	2018	2017	2018	2017
Receivables:				
Prepaid and other current assets	\$ 494,444	\$ 316,226	\$ 127,403	\$ 195,223
Other assets	<u>1,019,660</u>	<u>800,539</u>	<u>3,322,607</u>	<u>3,683,578</u>
Total receivables	<u>1,514,104</u>	<u>1,116,765</u>	<u>3,450,010</u>	<u>3,878,801</u>
Payables:				
Accounts payable and accrued expenses	1,647,311	1,399,905	1,256,223	1,401,346
Other liabilities	<u>5,828,693</u>	<u>5,437,265</u>	<u>5,743,015</u>	<u>6,319,483</u>
Gross undiscounted liability	<u>7,476,004</u>	<u>6,837,170</u>	<u>6,999,238</u>	<u>7,720,829</u>
Net undiscounted liability	<u>\$ 5,961,900</u>	<u>\$ 5,720,405</u>	<u>\$ 3,549,228</u>	<u>\$ 3,842,028</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE K - CONCENTRATIONS OF CREDIT RISK

The System grants credit without collateral to patients, most of whom are local residents and are insured under third-party agreements. The mix of accounts receivable, net, from patients and third-party payors at June 30, 2018 and 2017, was as follows:

	<u>2018</u>	<u>2017</u>
Medicare	35%	35%
Medicaid	23	18
Commercial	39	45
Patients	<u>3</u>	<u>2</u>
	<u>100%</u>	<u>100%</u>

In addition, the System invests its cash and cash equivalents primarily with banks and financial institutions. These deposits may be in excess of federally insured limits. Management believes that the credit risk related to these deposits is minimal.

NOTE L - FUNCTIONAL EXPENSES

The System provides general health care services to residents within its geographic location. Expenses related to providing these services for the years ended June 30, 2018 and 2017, are as follows:

	<u>2018</u>	<u>2017</u>
Health care services	\$ 351,768,787	\$ 336,511,257
General and administration	55,504,306	49,308,593
Fundraising and special events	<u>1,094,045</u>	<u>791,431</u>
	<u>\$ 408,367,138</u>	<u>\$ 386,611,281</u>

NOTE M - COMMITMENTS AND CONTINGENCIES

General Litigation

The System is a defendant in various civil actions seeking damages for alleged medical malpractice or other civil litigation. These actions are being defended by the System's insurance carriers or counsel selected by the System. Counsel to the System in those matters and management are of the opinion that failure of the System to prevail in these various actions will not materially adversely affect the financial position of the System.

(Continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE M - COMMITMENTS AND CONTINGENCIES - Continued

The Medical Center was party to a lawsuit from 2008, with regards to a former privileged physician. A class action was filed and ultimately settled at a fairness hearing in 2012. The agreed-upon settlement required the Medical Center's insurance carriers to pay into a fund created on behalf of the plaintiffs. The Medical Center also agreed to contribute an additional \$100,000 a year over a 5-year period which ended October 2017 and provide as much as \$1,000,000 in free medical care to the plaintiffs over a 15-year period ending October 2027. As of June 30, 2018, there is approximately \$811,000 of free medical care available under this agreement.

The remaining settlement liability at June 30, 2018 and 2017 is included in the consolidated balance sheets as follows:

	<u>2018</u>	<u>2017</u>
Accounts payable and accrued expenses	\$ -	\$ 100,000
Other liabilities	<u>810,787</u>	<u>867,291</u>
	<u>\$ 810,787</u>	<u>\$ 967,291</u>

Operating Leases

The System leases property and equipment through lease agreements expiring on various dates through the year 2029. Certain of these leases contain options to extend the lease terms. Lease expense for the years ended June 30, 2018 and 2017 was \$3,690,240 and \$3,185,368, respectively. Future minimum lease payments, excluding options to extend lease payments, are as follows for the years ending June 30:

2019	\$ 3,690,127
2020	3,477,402
2021	3,306,967
2022	3,316,024
2023	3,259,968
Thereafter	<u>12,900,980</u>
	<u>\$ 29,951,468</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2018 and 2017

NOTE N - ASSET RETIREMENT OBLIGATIONS

The Medical Center's asset retirement obligation is attributed to a 2005 study on the existence and removal of asbestos material in several older buildings still in use.

The following is a reconciliation of the asset retirement obligation, which is included in other liabilities on the consolidated balance sheets as of June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Asset retirement obligation at beginning of year	\$ 3,800,835	\$ 3,620,014
Accretion expense, included in depreciation and amortization	<u>182,334</u>	<u>180,821</u>
Asset retirement obligation at end of year	<u>\$ 3,983,169</u>	<u>\$ 3,800,835</u>

NOTE O - RELATED-PARTY TRANSACTIONS

The Medical Center and each of its affiliates have Boards of Directors that are comprised of community members and 20 physicians in 2018 and in 2017 who are related parties. Payments to community members, primarily for property rentals and other services for the years ended June 30, 2018 and 2017, were \$776,464 and \$825,210, respectively. The System has arrangements with many physicians to compensate them for Medical Director and Leadership responsibilities, practice guarantees, pay-for-call (emergency department) and fees for professional services rendered that are included in the salaries and benefits, physician fees, and contract labor expense line. During the years ended June 30, 2018 and 2017, amounts paid to related-party physicians aggregated \$4,020,249 and \$4,113,307, respectively. Amounts received from a related-party physician group were \$508,000 during the year ended June 30, 2018 and none during the year ended June 30, 2017. At June 30, 2018, amounts receivable from related-party physicians aggregated \$508,000 and payables to related-party physicians were \$194,308. At June 30, 2017, amounts receivable from related-party physicians aggregated \$1,016,000 and payables to related-party physicians were \$65,720. These receivables are reflected as prepaid expenses and other current assets, and the payables are reflected as accounts payable and accrued expenses.

NOTE P - SUBSEQUENT EVENTS

The System evaluated its June 30, 2018 consolidated financial statements for subsequent events through October 26, 2018, the date the consolidated financial statements were available to be issued. The System is not aware of any subsequent events which would require recognition or disclosure in the consolidated financial statements, except as noted elsewhere in the footnotes to the consolidated financial statements.

SUPPLEMENTARY INFORMATION

Beebe Medical Center, Inc.

CONSOLIDATING BALANCE SHEET

June 30, 2018

	Beebe Medical Center, Inc.	Delmarva Health Network	Beebe Medical Group	Beebe Medical Foundation	Consolidating Entries	Consolidated Totals
ASSETS						
Current assets						
Cash and cash equivalents	\$ 63,602,178	\$ 250,098	\$ 1,085,690	\$ 276,119	\$ -	\$ 65,214,085
Patient accounts receivable, net	41,420,212	-	2,639,750	-	-	44,059,962
Prepaid expenses and other current assets	17,620,827	124,501	327,350	45,290	-	18,117,968
Total current assets	122,643,217	374,599	4,052,790	321,409	-	127,392,015
Assets limited as to use						
Board designated funds	75,262,974	-	-	3,568,140	-	78,831,114
Beneficial interest in Foundation unrestricted net assets	4,646,788	-	-	-	(4,646,788)	-
Under bond indenture agreement	144,040	-	-	-	-	144,040
Collateral funds for line of credit	7,713,605	-	-	-	-	7,713,605
Donor-restricted funds	3,323	-	-	16,921,874	-	16,925,197
Subtotal	87,770,730	-	-	20,490,014	(4,646,788)	103,613,956
Beneficial interest in Foundation restricted net assets	26,089,789	-	-	-	(26,089,789)	-
Other board designated assets - land	1,838,339	-	-	-	-	1,838,339
Donor-restricted pledges receivable, net	-	-	-	10,197,003	-	10,197,003
Assets held in charitable remainder trust	672,432	-	-	-	-	672,432
Beneficial interest in perpetual trust	336,878	-	-	-	-	336,878
Total assets limited as to use	116,708,168	-	-	30,687,017	(30,736,577)	116,658,608
Property and equipment, net	141,267,743	-	2,297,840	4,267	-	143,569,850
Due from affiliates	376,690	-	-	-	(376,690)	-
Other assets	11,413,139	-	-	-	-	11,413,139
Total assets	<u>\$ 392,408,957</u>	<u>\$ 374,599</u>	<u>\$ 6,350,630</u>	<u>\$ 31,012,693</u>	<u>\$ (31,113,267)</u>	<u>\$ 399,033,612</u>
LIABILITIES AND NET ASSETS						
Current liabilities						
Accounts payable and accrued expenses	\$ 39,300,500	\$ 157,419	\$ 6,332,234	\$ 146,498	\$ -	\$ 45,936,651
Estimated third-party payor settlements	7,169,716	-	-	-	-	7,169,716
Current portion of long-term debt	3,593,150	-	-	-	-	3,593,150
Total current liabilities	50,063,366	157,419	6,332,234	146,498	-	56,699,517
Accrued retirement benefits	50,475,182	-	-	-	-	50,475,182
Due to affiliates	-	119,176	165,824,372	127,274	(166,070,822)	-
Other liabilities	16,706,066	-	-	2,344	(13,840)	16,694,570
Long-term debt, less current portion	44,339,089	-	-	-	-	44,339,089
Total liabilities	161,583,703	276,595	172,156,606	276,116	(166,084,662)	168,208,358
Net assets						
Unrestricted	204,427,346	98,004	(165,805,976)	4,646,788	161,061,184	204,427,346
Temporarily restricted	23,900,248	-	-	23,679,761	(23,679,761)	23,900,248
Permanently restricted	2,497,660	-	-	2,410,028	(2,410,028)	2,497,660
Total net assets	230,825,254	98,004	(165,805,976)	30,736,577	134,971,395	230,825,254
Total liabilities and net assets	<u>\$ 392,408,957</u>	<u>\$ 374,599</u>	<u>\$ 6,350,630</u>	<u>\$ 31,012,693</u>	<u>\$ (31,113,267)</u>	<u>\$ 399,033,612</u>

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

For the year ended June 30, 2018

	Beebe Medical Center, Inc.	Delmarva Health Network	Beebe Medical Group	Beebe Medical Foundation	Consolidating Entries	Consolidated Totals
Unrestricted net assets						
Unrestricted revenues and other support						
Net patient service revenue before bad debt	\$ 399,288,649	\$ -	\$ 31,534,061	\$ -	\$ -	\$ 430,822,710
Less: Provision for bad debt	(16,072,439)	-	(140,784)	-	-	(16,213,223)
Net patient service revenue less provision for bad debt	383,216,210	-	31,393,277	-	-	414,609,487
Other revenues	3,544,706	159,845	5,940,223	-	(5,370,090)	4,274,684
Net assets released from restrictions used for operations	805,898	-	-	-	-	805,898
Total unrestricted revenues and other support	387,566,814	159,845	37,333,500	-	(5,370,090)	419,690,069
Expenses						
Salaries and benefits, physician fees, and contract labor	189,937,552	217,662	50,720,776	1,150,107	(5,370,090)	236,656,007
Medical, surgical, and patient-related supplies and services	85,338,685	-	2,210,842	59,304	-	87,608,831
Repairs, maintenance and utilities	15,657,180	-	662,745	-	-	16,319,925
Other	37,981,199	819,896	7,311,500	123,401	-	46,235,996
Depreciation and amortization	19,690,774	-	582,135	810	-	20,273,719
Interest	1,272,660	-	-	-	-	1,272,660
Total expenses	349,878,050	1,037,558	61,487,998	1,333,622	(5,370,090)	408,367,138
Income (loss) from operations	37,688,764	(877,713)	(24,154,498)	(1,333,622)	-	11,322,931
Nonoperating gains (losses)						
Contributions	-	-	-	267,684	-	267,684
Investment income	4,017,778	-	-	120,780	-	4,138,558
Equity losses and gains in consolidated affiliates	(24,827,263)	-	-	-	24,827,263	-
Other accrued retirement costs	(4,106,861)	-	-	-	-	(4,106,861)
Contribution (to) from Foundation	(1,150,106)	-	-	1,150,106	-	-
Total nonoperating (losses) gains, net	(26,066,452)	-	-	1,538,570	24,827,263	299,381
Excess of (deficiency in) revenues and gains over expenses and losses	11,622,312	(877,713)	(24,154,498)	204,948	24,827,263	11,622,312
Other changes in unrestricted net assets						
Net assets released from restrictions used for property and equipment purchases	521,253	-	-	-	-	521,253
Other changes in accrued retirement benefits	27,965,248	-	-	-	-	27,965,248
Change in interest in Foundation unrestricted net assets	(995,260)	-	-	-	995,260	-
Transfers	1,469,792	-	-	(1,469,792)	-	-
Changes in unrealized gains and losses on investments	1,468,820	-	-	269,584	-	1,738,404
Other	(192,963)	905,890	-	-	(700,942)	11,985
Increase (decrease) in unrestricted net assets	41,859,202	28,177	(24,154,498)	(995,260)	25,121,581	41,859,202
Temporarily restricted net assets						
Contributions	-	-	-	13,896,259	-	13,896,259
Net investment income and realized gains on investments	-	-	-	307,725	-	307,725
Net assets released from restrictions used for:						
Property and equipment purchases	(521,253)	-	-	-	-	(521,253)
Operations	(805,898)	-	-	-	-	(805,898)
Change in interest in Foundation temporarily restricted net assets	13,682,731	-	-	-	(13,682,731)	-
Transfers	521,253	-	-	(521,253)	-	-
Increase in temporarily restricted net assets	12,876,833	-	-	13,682,731	(13,682,731)	12,876,833
Permanently restricted net assets						
Contributions	1,281	-	-	67,153	-	68,434
Change in value of beneficial interest in perpetual trust	9,081	-	-	-	-	9,081
Realized and unrealized gains on investments	-	-	-	19,780	-	19,780
Change in interest in Foundation permanently restricted net assets	86,933	-	-	-	(86,933)	-
Increase in permanently restricted net assets	97,295	-	-	86,933	(86,933)	97,295
Increase (decrease) in net assets	54,833,330	28,177	(24,154,498)	12,774,404	11,351,917	54,833,330
Net assets, beginning of year	175,991,924	69,827	(141,651,478)	17,962,173	123,619,478	175,991,924
Net assets, end of year	\$ 230,825,254	\$ 98,004	\$ (165,805,976)	\$ 30,736,577	\$ 134,971,395	\$ 230,825,254



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