

**Blanchard Valley Health System  
and Subsidiaries**  
Independent Auditor's Reports  
and Consolidated Financial Statements  
December 31, 2017 and 2016



**Blanchard Valley Health System and Subsidiaries**  
**December 31, 2017 and 2016**

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## Independent Auditor's Report

Board of Trustees  
Blanchard Valley Health System and Subsidiaries  
Findlay, Ohio

We have audited the accompanying consolidated financial statements of Blanchard Valley Health System and Subsidiaries (Corporation), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations, 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.

### *Auditor's Responsibility*

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

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

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

***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Blanchard Valley Health System and Subsidiaries as of December 31, 2017 and 2016, and the results of its operations, 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.

*BKD, LLP*

Fort Wayne, Indiana  
April 24, 2018

# Blanchard Valley Health System and Subsidiaries

## Consolidated Balance Sheets

**December 31, 2017 and 2016**

(Dollar Amounts in Thousands)

|   | 2017              | 2016              |
|---|-------------------|-------------------|
| <b>Assets</b>   |                   |                   |
| <b>Current Assets</b>                                       |                   |                   |
| Cash and cash equivalents                                   | \$ 18,845         | \$ 8,765          |
| Accounts receivable   |                   |                   |
| Patient, net of allowance; 2017 - \$12,290, 2016 - \$10,500 | 44,445            | 48,477            |
| Other   | 6,456             | 10,286            |
| Contributions receivable                                    | 956               | 1,108             |
| Inventories   | 9,177             | 9,594             |
| Prepaid expenses  | <u>2,983</u>      | <u>1,677</u>      |
| Total current assets  | <u>82,862</u>     | <u>79,907</u>     |
| <b>Assets Limited as to Use</b>                             |                   |                   |
| Internally designated                                       | 331,257           | 288,579           |
| Externally restricted by donors                             | 11,961            | 10,551            |
| Held by trustee   | <u>13,982</u>     | <u>17,001</u>     |
|   | <u>357,200</u>    | <u>316,131</u>    |
| <b>Property and Equipment, net</b>                          | <u>176,125</u>    | <u>178,547</u>    |
| <b>Other Assets</b>   |                   |                   |
| Contributions receivable, less current portion              | 845               | 887               |
| Investments in equity investees                             | 950               | 1,018             |
| Beneficial interest in perpetual trusts                     | 17,482            | 17,715            |
| Intangible assets, net                                      | 17,979            | 22,673            |
| Other   | <u>122</u>        | <u>41</u>         |
|   | <u>37,378</u>     | <u>42,334</u>     |
| <b>Total assets</b>   | <u>\$ 653,565</u> | <u>\$ 616,919</u> |

|   | <b>2017</b>       | <b>2016</b>       |
|---|-------------------|-------------------|
| <b>Liabilities and Net Assets</b>               |                   |                   |
| <b>Current Liabilities</b>                      |                   |                   |
| Current maturities of long-term debt            | \$ 6,229          | \$ 5,996          |
| Accounts payable and accrued expenses           | 23,059            | 23,893            |
| Accrued wages, withholdings and payroll taxes   | 17,856            | 15,411            |
| Estimated amounts due to third-party payers     | 1,329             | 1,528             |
| Other   | <u>1,113</u>      | <u>1,173</u>      |
| Total current liabilities                       | <u>49,586</u>     | <u>48,001</u>     |
| <b>Other Liabilities</b>                        |                   |                   |
| Long-term debt                                  | 136,734           | 130,068           |
| Deferred revenue                                | 538               | 470               |
| Pension liability                               | 35,731            | 38,085            |
| Interest rate swap agreement                    | 20,742            | 22,337            |
| Other long-term obligations                     | <u>10,119</u>     | <u>9,614</u>      |
| Total liabilities                               | <u>203,864</u>    | <u>200,574</u>    |
| <b>Net Assets</b>                               |                   |                   |
| Unrestricted                                    |                   |                   |
| Blanchard Valley Health System and Subsidiaries | 372,211           | 340,814           |
| Noncontrolling interest                         | (3,199)           | (2,540)           |
| Temporarily restricted                          | 10,620            | 9,433             |
| Permanently restricted                          | <u>20,483</u>     | <u>20,637</u>     |
| Total net assets                                | <u>400,115</u>    | <u>368,334</u>    |
| Total liabilities and net assets                | <u>\$ 653,565</u> | <u>\$ 616,919</u> |

# Blanchard Valley Health System and Subsidiaries

## Consolidated Statements of Operations Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

|  | 2017             | 2016             |
|--|------------------|------------------|
| <b>Unrestricted Revenue, Gains and Other Support</b>   |                  |                  |
| Patient service revenue (net of contractual discounts and allowances)                                  | \$ 335,054       | \$ 328,986       |
| Provision for uncollectable accounts   | <u>(14,793)</u>  | <u>(13,835)</u>  |
| Net patient service revenue less provision for uncollectable accounts                                  | 320,261          | 315,151          |
| Rental revenue   | 271              | 207              |
| Other revenue  | 7,432            | 7,402            |
| Net assets released from restrictions used for operations  | <u>503</u>       | <u>290</u>       |
| Total unrestricted revenue, gains and other support  | <u>328,467</u>   | <u>323,050</u>   |
| <b>Expenses and Losses</b>   |                  |                  |
| Compensation, contract wages and benefits  | 189,614          | 177,702          |
| Purchased and contracted services  | 19,530           | 22,595           |
| Medical and professional fees  | 4,475            | 5,363            |
| Medical and pharmacy supplies  | 56,254           | 52,723           |
| Insurance  | 1,682            | 2,190            |
| Depreciation and amortization of fixed assets and intangibles  | 21,061           | 15,446           |
| Interest and amortization of deferred financing costs  | 6,871            | 6,893            |
| Other and allocated costs  | 23,882           | 23,105           |
| Loss on disposal of property and equipment   | <u>(1)</u>       | <u>(75)</u>      |
| Total expenses and losses  | <u>323,368</u>   | <u>305,942</u>   |
| <b>Operating Income</b>  | <u>5,099</u>     | <u>17,108</u>    |
| <b>Nonoperating Gains and Other</b>  |                  |                  |
| Investment return  | 43,177           | 18,907           |
| Gain on investment in equity investee  | 969              | 4,949            |
| Change in fair value of interest rate swap agreement   | 1,595            | 942              |
| Loss on extinguishment of debt   | (12,813)         | —                |
| Net fundraising activity and other   | <u>(1,165)</u>   | <u>(1,854)</u>   |
| Total nonoperating gains and other   | <u>31,763</u>    | <u>22,944</u>    |
| <b>Excess of Revenue Over Expenses</b>   | 36,862           | 40,052           |
| <b>Excess of Revenue Over Expenses Attributable to Noncontrolling Interest</b>                         | <u>(4,461)</u>   | <u>(5,618)</u>   |
| <b>Excess of Revenue Over Expenses Attributable to Blanchard Valley Health System and Subsidiaries</b> | <u>32,401</u>    | <u>34,434</u>    |
| <b>Other Changes in Unrestricted Net Assets</b>  |                  |                  |
| Net assets released from restriction used for purchase of property and equipment                       | 1,211            | 1,953            |
| Contribution expense   | -                | (1,621)          |
| Defined benefit pension plan   |                  |                  |
| Change in gains and losses and prior service cost  | (1,019)          | (2,486)          |
| Change in noncontrolling interest  | (652)            | (44)             |
| Other changes in net assets  | <u>(1,203)</u>   | <u>(1,185)</u>   |
| Total other changes in unrestricted net assets   | <u>(1,663)</u>   | <u>(3,383)</u>   |
| <b>Increase in Unrestricted Net Assets</b>   | <u>\$ 30,738</u> | <u>\$ 31,051</u> |

# Blanchard Valley Health System and Subsidiaries

## Consolidated Statements of Changes in Net Assets

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

|   | 2017       | 2016       |
|---|------------|------------|
| <b>Unrestricted Net Assets</b>  |            |            |
| Excess of revenue over expenses attributable to Blanchard Valley Health System and Subsidiaries | \$ 32,401  | \$ 34,434  |
| Net assets released from restriction used for purchase of property and equipment                | 1,211      | 1,953      |
| Contribution expense  | -          | (1,621)    |
| Defined benefit pension plan  |            |            |
| Change in gains and losses and prior service cost   | (1,019)    | (2,486)    |
| Change in noncontrolling interest   | (650)      | (44)       |
| Other changes in net assets   | (1,203)    | (1,185)    |
| Total other changes in unrestricted net assets  | (1,661)    | (3,383)    |
| Increase in unrestricted net assets   | 30,738     | 31,051     |
| <b>Temporarily Restricted Net Assets</b>  |            |            |
| Donations   | 2,141      | 2,467      |
| Investment return   | 760        | 310        |
| Net assets released from restrictions   | (1,714)    | (2,243)    |
| Increase in temporarily restricted net assets   | 1,187      | 534        |
| <b>Permanently Restricted Net Assets</b>  |            |            |
| Donations   | 79         | 55         |
| Change in beneficial interest in perpetual trusts   | (233)      | (561)      |
| Decrease in permanently restricted net assets   | (154)      | (506)      |
| <b>Change in Net Assets</b>   | 31,771     | 31,079     |
| <b>Net Assets, Beginning of Year</b>  | 368,344    | 337,265    |
| <b>Net Assets, End of Year</b>  | \$ 400,115 | \$ 368,344 |

# Blanchard Valley Health System and Subsidiaries

## Consolidated Statements of Cash Flows Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

|   | 2017             | 2016            |
|---|------------------|-----------------|
| <b>Operating Activities</b>   |                  |                 |
| Change in net assets  | \$ 31,771        | \$ 31,079       |
| Change in net assets attributable to noncontrolling interests   | <u>652</u>       | <u>44</u>       |
| Change in net assets attributable to the Corporation  | 32,423           | 31,123          |
| Items not requiring (providing) operating cash flow   |                  |                 |
| Gain on disposal of property and equipment  | (1)              | (75)            |
| Loss on extinguishment of debt  | 12,813           | —               |
| Depreciation and amortization of fixed assets and intangibles   | 21,061           | 15,446          |
| Amortization of deferred financing costs  | 155              | 162             |
| Gain on equity investments  | (969)            | (4,949)         |
| Net gain on assets limited as to use  | (31,311)         | (12,888)        |
| Change in fair value of interest rate swap agreement  | (1,595)          | (942)           |
| Change in beneficial interest in perpetual trusts   | 233              | 561             |
| Provision for uncollectable accounts  | 14,793           | 13,835          |
| Noncontrolling interest   | 4,461            | 5,618           |
| Change in defined benefit pension plan liability  | (2,354)          | (434)           |
| Contributions and investment return received restricted for long-term investment or for acquisition of long-term assets | (839)            | (365)           |
| Changes in  |                  |                 |
| Accounts and contributions receivable   | (6,737)          | (29,366)        |
| Prepaid expenses and other current assets   | (889)            | (1,488)         |
| Other assets and liabilities  | 1,202            | 4,180           |
| Accounts payable, accrued expenses and accrued wages, withholdings and payroll taxes                                    | 4,853            | 8,543           |
| Deferred revenue  | <u>68</u>        | <u>(164)</u>    |
| Net cash provided by operating activities   | <u>47,367</u>    | <u>28,797</u>   |
| <b>Investing Activities</b>   |                  |                 |
| Net change in assets limited as to use  | (9,758)          | (8,032)         |
| Purchases of property and equipment and intangibles - software  | <u>(17,186)</u>  | <u>(16,582)</u> |
| Net cash used in investing activities   | <u>(26,944)</u>  | <u>(24,614)</u> |
| <b>Financing Activities</b>   |                  |                 |
| Contributions and investment return received restricted for long-term investment or for acquisition of long-term assets | 839              | 365             |
| Proceeds from issuance of long-term debt  | 130,247          | —               |
| Escrow funded on debt defeasance  | (11,711)         | —               |
| Deferred financing costs  | (1,279)          | —               |
| Principal payments on long-term debt  | (123,326)        | (5,768)         |
| Distributions to minority interest holders  | <u>(5,113)</u>   | <u>(5,477)</u>  |
| Net cash used in financing activities   | <u>(10,343)</u>  | <u>(10,880)</u> |
| <b>Increase (Decrease) in Cash and Cash Equivalents</b>   | 10,080           | (6,697)         |
| <b>Cash and Cash Equivalents, Beginning of Year</b>   | <u>8,765</u>     | <u>15,462</u>   |
| <b>Cash and Cash Equivalents, End of Year</b>   | <u>\$ 18,845</u> | <u>\$ 8,765</u> |
| <b>Supplemental Cash Flows Information</b>  |                  |                 |
| Interest paid   | \$ 6,443         | \$ 6,443        |
| Property and equipment included in accounts payable   | 517              | 3,759           |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

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

#### *Nature of Operations, Organization, Principles of Consolidation and Noncontrolling Interest*

Blanchard Valley Health System (Corporation) is a nonprofit, integrated regional health system based in Findlay, Ohio and provides a wide range of health care services to the residents in Findlay and the surrounding areas of northwest Ohio. The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries: Blanchard Valley Regional Health Center (Health Center), Blanchard Valley Continuing Care Services, Inc. (Continuing Care Services), Blanchard Valley Health Foundation (Foundation), Blanchard Valley Medical Practice, LLC (BVMP) and CITAS, Inc. (CITAS).

The Corporation provides executive administrative support, strategic planning and oversight to all subsidiaries. The Corporation is the sole shareholder of Hanco Ambulance, Inc. (Hanco), a local pre-emergency medical care and transportation ambulance company that serves the residents of Findlay, Ohio and Hancock County, Ohio. The Corporation is also the sole member of Beyond MedSpa (MedSpa), a local cosmetic and medical treatment company that has locations in Findlay and Bluffton, Ohio.

The Health Center operates a 150-bed general acute care, hospital in Findlay, Ohio (Blanchard Valley Hospital) and a 25-bed critical access hospital in Bluffton, Ohio (Bluffton Hospital). The Health Center has a 51 percent interest in Blanchard Valley Pain Management, LLC (BVPM), which owns and operates a pain management center; a 67 percent interest in TechniCore Clinical Engineering Services, LLC (TCES), a biomedical engineering services company; and a 9 percent interest in Fresenius Medical Care Creighton Dialysis LLC (Dialysis), which provides hemodialysis and peritoneal dialysis services in Findlay, Ohio. During the year ended December 31, 2016, the Health Center sold 51 percent of its 60 percent interest in Creighton Dialysis LLC (Creighton) to an unrelated third party.

Continuing Care Services operates a 190,000 square foot retirement community in Findlay (Birchaven Village), consisting of 136-bed licensed skilled nursing facility, 23 assisted living units and a congregate care living facility of 71 total units which are dually certified as independent living/assisted living. Also, Continuing Care Services operates a separate 50-bed licensed skilled nursing facility and a 27-unit senior living apartment facility in Fostoria (Independence House). Continuing Care Services is also the sole member of Blanchard Valley Home Care Services, LLC (Bridge), which provides home health, hospice and private care services and Birchaven Estates at Eastern Woods, Ltd. (Estates), which is a condominium development for seniors on approximately 16 acres adjacent to Birchaven. Continuing Care Services has a 73 percent interest in Northwest Ohio Medical Equipment (NOME), a provider of home medical and oxygen equipment.

The Foundation solicits and manages donations in support of the operation of the Corporation and its subsidiaries.

BVMP operates several family practice physician offices and specialty physician offices that are primarily located in Findlay and the surrounding communities, as well as an urgent care center.

CITAS currently performs physician recruiting on behalf of the Corporation.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

Significant intercompany accounts and transactions have been eliminated in consolidation.

Noncontrolling interest represents the 49 percent interest in BVPM and the 33 percent interest in TCES that the Health Center does not own, as well as the 27 percent interest in NOME that Continuing Care Services does not own.

### ***Mission Statement and Nonoperating Gains and Losses***

The Corporation's mission statement is "*Caring for a lifetime.*" The Corporation's primary mission is to provide exceptional health care services through its acute care, long-term care and ambulatory facilities. Primarily those activities directly associated with the furtherance of this purpose are considered to be operating activities.

Other activities that result in gains or losses unrelated to the Corporation's primary mission are considered to be nonoperating. Nonoperating gains and losses include realized and unrealized investment earnings other than on trustee-held investments related to borrowed funds, unrestricted gifts and bequests, gains and losses on equity investments, net fundraising activities and changes in the market value of interest rate swap agreements.

### ***Use of Estimates***

The preparation of 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 and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

### ***Cash and Cash Equivalents***

The Corporation considers all liquid investments, other than those limited as to use, with original maturities of three months or less to be cash equivalents. At December 31, 2017 and 2016, cash equivalents consisted primarily of money market accounts and certificates of deposit.

At December 31, 2017, the Corporation's cash accounts exceeded federally insured limits by approximately \$18,437.

### ***Investments, Investment Return and Assets Limited as to Use***

Investments in equity securities having a readily determinable fair value and in all debt securities are carried at fair value. The investments in equity investees are reported on the equity method of accounting. Other investments are valued at fair value. Management's estimate of the fair value of investments without quoted market prices is determined based on valuations provided by the external investment managers. The valuations for these investments without quoted market prices necessarily involve estimates, appraisals, assumptions and methods which are reviewed by the Corporation.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

Investment return includes dividend, interest and other investment income; realized and unrealized gains and losses on investments carried at fair value; and realized gains and losses on other investments.

Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year is included in unrestricted net assets. Other investment return is reflected in the consolidated statements of operations and changes in net assets as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

Assets limited as to use include: (1) assets held by trustees, including medical malpractice trust, (2) assets restricted by donors and (3) assets set aside by the Board of Trustees for future capital improvements over which the Board retains control and may at its discretion subsequently use for other purposes.

### ***Patient Accounts Receivable***

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the Corporation analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for uncollectible accounts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Corporation analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for uncollectible accounts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely).

For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Corporation records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or provided by policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

The Corporation's allowance for doubtful accounts for self-pay patients increased from 87 percent of self-pay accounts receivable at December 31, 2016, to 88 percent of self-pay accounts receivable at December 31, 2017. In addition, the Corporation's write-offs increased \$958 from \$13,835 for the year ended December 31, 2016, to \$14,793 for the year ended December 31, 2017. Both changes were the result of trends in self-pay activity for the year as well as continuing trends experienced in the collection of amounts from both primary and secondary coverage of self-pay patients.

# **Blanchard Valley Health System and Subsidiaries**

## **Notes to Consolidated Financial Statements**

**Years Ended December 31, 2017 and 2016**

(Dollar Amounts in Thousands)

### ***Inventories***

At December 31, 2017, the Corporation states supplies inventories at the lower of cost or net realizable value. At December 31, 2016, the Corporation stated supplies inventories at the lower of cost, using the first-in, first-out method or market.

### ***Property and Equipment***

Property and equipment acquisitions are recorded at cost and are depreciated on a straight-line basis over the estimated useful life of each asset. Expenditures for renewals or betterments are capitalized and expenditures for maintenance and repairs are charged to expense. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The cost and related accumulated depreciation of property and equipment that is sold or retired are removed from the consolidated financial statements and the resulting gain or loss is recorded as operating expense.

Donations of property and equipment are reported at fair value as an increase in unrestricted net assets unless use of the assets is restricted by the donor. Monetary gifts that must be used to acquire property and equipment are reported as restricted support. The expiration of such restrictions is reported as an increase in unrestricted net assets when the donated asset is placed in service.

### ***Long-Lived Asset Impairment***

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

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

### ***Deferred Financing Costs***

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt and are amortized on the bonds outstanding method over the term of the debt. Amortization expense was \$155 and \$162 during the years ended December 31, 2017 and 2016, respectively, and is reported as a component of interest expense.

### ***Deferred Revenue***

In 2004, Continuing Care Services received approximately \$1,000 for advanced rental payments for space, which was recorded as deferred revenue and is being recognized in income over a 25-year period ending in 2028. The remaining amount of deferred revenue to be recognized in future periods was \$390 and \$430 at December 31, 2017 and 2016, respectively.

Other revenues which relate to future periods are also included in deferred revenue.

# **Blanchard Valley Health System and Subsidiaries**

## **Notes to Consolidated Financial Statements**

**Years Ended December 31, 2017 and 2016**

(Dollar Amounts in Thousands)

### ***Derivatives***

Derivatives are recognized as assets and liabilities on the consolidated balance sheet and measured at fair value. For exchange-traded contracts, fair value is based on quoted market prices. For nonexchange traded contracts, fair value is based on dealer quotes, pricing models, discounted cash flow methodologies or similar techniques for which the determination of fair value may require significant management judgement or estimation.

### ***Temporarily and Permanently Restricted Net Assets***

Temporarily restricted net assets contain donor-imposed restrictions of a particular time period or purpose that permit the Corporation to use or expend the assets as specified.

Permanently restricted net assets contain donor-imposed restrictions that stipulate the resources, including original donation, unrealized net gains and undistributed investment income, be maintained permanently, but permit the Corporation to use or expend part or all of the income derived from the donated assets for either specified or unspecified purposes. For many restricted assets, the Corporation receives the higher of traditional trust income or 5 percent of the Applicable Fund Value (average market value), in accordance with the Institutional Trust Fund Act.

### ***Net Patient Service Revenue***

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

### ***Charity Care***

The Corporation accepts all patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain established policies of the Corporation. Essentially, these policies define charity care as those services for which no payment is anticipated. In assessing a patient's inability to pay, the Corporation utilizes generally recognized poverty income levels but also includes certain cases where incurred charges are significant when compared to income. Charity care provided in 2017 and 2016, measured at estimated cost, approximated \$1,525 and \$1,620, respectively, with the decline in current year activity associated with increased third-party insurance coverage associated with Medicaid expansion as well as the Corporation's implementation of the community health needs assessment under the Affordable Care Act. Estimated cost is derived from a ratio of total operating expenses as a percentage of gross charges. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

# **Blanchard Valley Health System and Subsidiaries**

## **Notes to Consolidated Financial Statements**

**Years Ended December 31, 2017 and 2016**

(Dollar Amounts in Thousands)

### ***Contributions***

Unconditional promises to give cash and other assets are accrued at estimated fair value at the date each promise is received. Gifts received with donor stipulations are reported as either temporarily or permanently restricted support. When a donor restriction expires, that is, when a time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified and reported as an increase in unrestricted net assets. Donor-restricted contributions whose restrictions are met within the same year as received are reported as restricted contributions and released from restriction. Conditional contributions are reported as liabilities until the condition is eliminated or the contributed assets are returned to the donor.

### ***Self-Funded Insurance***

The Corporation maintains self-funded health insurance and workers' compensation insurance plans covering substantially all employees. Contributions are made to the administrators of these plans as claims are paid, while expenses are accrued as incurred. The Corporation has purchased insurance that limits its exposure for individual health claims to \$250 per employee.

### ***Estimated Malpractice Costs***

An annual estimated provision is accrued for the self-insured portion of medical malpractice claims and includes an estimate of the ultimate costs for both reported claims and claims incurred, but not reported.

### ***Transfers Between Fair Value Hierarchy Levels***

Transfers in and out of Level 1 (quoted market prices), Level 2 (other significant observable inputs) and Level 3 (significant unobservable inputs) are recognized on the period beginning date.

### ***Income Taxes***

The Corporation and its subsidiaries are incorporated under the laws of the state of Ohio. The Corporation, the Health Center, Continuing Care Services, and the Foundation are not-for-profit corporations. CITAS is a for-profit corporation. The Internal Revenue Service has determined the not-for-profit corporations to be exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. However, the Corporation's tax-exempt entities are subject to federal income tax on any unrelated business taxable income.

### ***Excess of Revenue Over Expenses***

The consolidated statements of operations include excess of revenue over expenses. Changes in unrestricted net assets which are excluded from excess of revenue over expenses, consistent with industry practice, include permanent transfers to and from affiliates for other than goods and services and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets), changes in noncontrolling interests, contributions and changes in the defined benefit pension plan.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### ***Electronic Health Records Incentive Program***

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals and eligible professionals that demonstrate meaningful use of certified electronic health records technology (EHR). Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs are contingent on the hospital and professionals continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Corporation recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

In 2017, the Corporation completed the requirements under the Medicare and Medicaid programs for professionals and has recorded revenue of \$324, which is included in other revenue within operating revenues in the consolidated statement of operations.

In 2016, the Corporation completed the third-year requirements under the Medicare program and the fourth-year requirements under the Medicaid program and has recorded revenue of \$621, which is included in other revenue within operating revenues in the consolidated statement of operations.

### ***Intangible Assets***

Intangible assets with finite lives represent software licensing agreements. Amounts are amortized over five years. Such assets are periodically evaluated as to the recoverability of the carrying values.

### ***Reclassifications***

Certain reclassifications have been made to the 2016 consolidated financial statements to conform to the 2017 consolidated financial statement presentation. These reclassifications had no effect on the change in net assets.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### Note 2: Net Patient Service Revenue

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

The Health Center and certain other subsidiaries of the Corporation have agreements with third-party payers that provide for payments at amounts different from established rates. A summary of the payment arrangements with third-party payers follows:

*Medicare and Medicaid* – The Health Center and certain other subsidiaries of the Corporation are providers of services under the Medicare and Medicaid programs.

Inpatient and most outpatient services rendered to Medicare and Medicaid program beneficiaries of Blanchard Valley Hospital are paid at prospectively determined rates per discharge or encounter. These prospectively determined rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Other Medicare outpatient services are reimbursed at established fee schedules. Medicaid outpatient services are reimbursed on a prospectively determined fixed rate. While Medicaid inpatient operations costs are paid using a prospectively determined rate, capital costs for Medicaid inpatient services are reimbursed based on a cost reimbursement methodology.

Bluffton Hospital is certified as a critical access hospital (CAH) by Medicare. As a CAH, the Bluffton Hospital is reimbursed for substantially all inpatient and outpatient services to Medicare beneficiaries based on reasonable costs. Additionally, as a CAH, Bluffton Hospital's licensed beds are limited to 25 and acute average length of stay may not exceed 96 hours. Bluffton Hospital is reimbursed for substantially all services at tentative rates with final settlement determined after submission of annual cost reports by Bluffton Hospital and audits thereof by the Medicare Administration Contractors.

Continuing Care Services is reimbursed for skilled nursing services to Medicare patients under prospectively determined per diem rates that vary based on a patient's acuity and assistance needed in activities of daily living. Reimbursement for Medicaid patients of Birchaven and Independence House is based on prospectively determined per diem rates.

*Other Payers* – The Health Center, Continuing Care Services and certain divisions of the Corporation have also entered into agreements with certain commercial carriers, health maintenance organizations and preferred provider organizations. The basis for payment under these agreements includes prospectively determined rates per service, discounts from established charges and prospectively determined daily rates.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

Provision is made currently in the consolidated financial statements for estimated settlements under third-party reimbursement contracts. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Management is of the opinion that adequate provision has been made for the unsettled cost reports.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Health Center, Continuing Care Services and certain divisions of the Corporation believe that they are in compliance with all applicable laws and regulations and are not aware of any pending or threatened investigations involving allegations of potential wrongdoing. Noncompliance with such laws and regulations can be subject to regulatory action including fines, penalties and exclusion from the Medicare and Medicaid programs. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

Patient service revenue, net of contractual allowances and discounts (but before the provision for uncollectible accounts), recognized in the years ended December 31, 2017 and 2016, respectively, was approximately:

|                          | <u>2017</u>       | <u>2016</u>       |
|--------------------------|-------------------|-------------------|
| Medicare                 | \$ 90,665         | \$ 87,142         |
| Medicaid                 | 36,014            | 37,926            |
| Other third-party payers | 191,942           | 184,090           |
| Self-pay                 | <u>16,433</u>     | <u>19,828</u>     |
| Total                    | <u>\$ 335,054</u> | <u>\$ 328,986</u> |

The 2017 and 2016 net patient service revenue increased approximately \$199 and \$600, respectively, due to changes of previously estimated amounts as a result of final settlements.

### Note 3: Concentration of Credit Risk

The Health Center and certain other subsidiaries of the Corporation grant credit without collateral to patients, most of whom are local residents and are insured under third-party payer agreements. The mix of gross receivables from patients and third-party payers for the Health Center and certain other subsidiaries of the Corporation at December 31, 2017 and 2016, are as follows:

|                    | <u>2017</u> | <u>2016</u> |
|--------------------|-------------|-------------|
| Medicare           | 39%         | 36%         |
| Commercial         | 31          | 35          |
| Medicaid           | 14          | 16          |
| Self-pay and other | <u>16</u>   | <u>13</u>   |
|                    | <u>100%</u> | <u>100%</u> |

Self-insured patients include patients with no insurance, co-payments and deductibles for patients with insurance and patients under contract.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### Note 4: Investments and Investment Return

#### **Assets Limited as to Use**

Assets limited as to use at December 31 are as follows:

|  | 2017       | 2016       |
|--|------------|------------|
| Cash   | \$ 2,209   | \$ 2,739   |
| Money market mutual funds                                      | 2,750      | 1,301      |
| Domestic equity mutual funds                                   | 102,528    | 108,050    |
| International equity mutual funds                              | 80,410     | 61,311     |
| Pooled investment and limited partnership funds, at fair value | 59,463     | 54,890     |
| Corporate bonds  | 4,979      | 2,194      |
| Municipal bonds  | 36         | 1,966      |
| Domestic fixed income mutual funds                             | 96,441     | 71,708     |
| International fixed income mutual funds                        | 8,384      | 11,972     |
|  | \$ 357,200 | \$ 316,131 |

The following tables present information regarding the nature and significant terms of the Corporation's pooled investment and limited partnership funds at December 31, 2017 and 2016:

| 2017                        |            |                      |                                    |                          |  |
|-----------------------------|------------|----------------------|------------------------------------|--------------------------|--|
| Investments                 | Fair Value | Unfunded Commitments | Redemption Frequency (if Eligible) | Redemption Notice Period |  |
| Limited partnerships (A)    | \$ 3,520   | \$ 110               | None                               | N/A                      |  |
| Pooled investment funds (B) | 55,943     | —                    | Quarterly to annually              | 15 – 370 days            |  |
| 2016                        |            |                      |                                    |                          |  |
| Investments                 | Fair Value | Unfunded Commitments | Redemption Frequency (if Eligible) | Redemption Notice Period |  |
| Limited partnerships (A)    | \$ 3,912   | \$ 241               | None                               | N/A                      |  |
| Pooled investment funds (B) | 50,978     | —                    | Quarterly to annually              | 15 – 370 days            |  |

- (A) This category includes several private equity funds that invest in early stage, high-growth private companies, growth equity financing, leverage buyouts, securities and other obligations of distressed businesses and financially troubled companies. These investments can never be redeemed with the funds. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the funds. These investments are planned to be held and it is estimated that the underlying assets of the funds will be liquidated in approximately ten years. The fair value of the investments in this category have been estimated using the Corporation's ownership interests in partners' capital.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

- (B) This category includes investments in hedge funds that invest primarily in other hedge funds, limited partnerships and investment companies. Management of these funds employs a variety of strategies and has the ability to shift investments based on market, economic, political and government driven events. The fair values of the investments in this category have been estimated using the net asset value per share of the investments. These investments can be redeemed and currently there are no restrictions.

Most of the Corporation's investments are pooled into one managed account. Invested amounts relate to the unrestricted, temporarily restricted and permanently restricted net assets and each net asset category receives an allocation of asset type and income based on its relative contribution to the managed accounts. The types of investments and credit risks associated with the managed accounts are limited through the Corporation's investment policy (Policy), which is to provide for long-term growth of capital without undue exposure to risk. To achieve this objective, the Policy provides for a predetermined asset allocation method, which is reviewed annually.

Total investment return is comprised of the following:

|  | 2017      | 2016      |
|--|-----------|-----------|
| Interest and dividend income                               | \$ 14,220 | \$ 7,753  |
| Net settlement payments under interest rate swap agreement | (1,594)   | (1,424)   |
| Realized gains (losses) on trading securities              | 9,286     | (3,476)   |
| Unrealized gains on trading securities                     | 22,025    | 16,364    |
|  | \$ 44,238 | \$ 19,217 |

Total investment return is reflected in the consolidated statements of operations and changes in net assets as follows:

|                                   | 2017      | 2016      |
|-----------------------------------|-----------|-----------|
| Unrestricted net assets           |           |           |
| Other nonoperating income         | \$ 43,177 | \$ 18,907 |
| Temporarily restricted net assets | 760       | 310       |
|                                   | \$ 43,937 | \$ 19,217 |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### Note 5: Property and Equipment

Property and equipment and related accumulated depreciation at December 31, 2017 and 2016, are as follows:

|   | 2017       | 2016       |
|---|------------|------------|
| Land  | \$ 10,663  | \$ 10,461  |
| Land improvements   | 13,912     | 12,708     |
| Building  | 206,220    | 193,868    |
| Leasehold improvements  | 2,737      | 2,737      |
| Equipment   | 139,430    | 127,517    |
| Construction in progress (estimated cost to complete of \$1.3 million at December 31, 2017) | 3,664      | 15,409     |
|   | 376,626    | 362,700    |
| Less allowance for depreciation and amortization  | (200,501)  | (184,153)  |
|   | \$ 176,125 | \$ 178,547 |

### Note 6: Beneficial Interest in Perpetual Trusts

The Corporation is an income beneficiary of several perpetual trusts controlled by unrelated third-party trustees. The beneficial interests in the assets of these trusts are included in the Corporation's consolidated financial statements as permanently restricted net assets. Income is distributed in accordance with the individual trust documents and is included in investment return. The estimated value of the expected future cash flows is \$17,482 and \$17,715, which represents the fair value of the trust at December 31, 2017 and 2016, respectively. Trust income distributed to the Corporation for the years ended December 31, 2017 and 2016, was \$853 and \$1,318, respectively.

### Note 7: Acquired Intangible Assets

The Corporation entered into a license agreement for the implementation of a new information system and electronic medical record platform. Total incurred implementation fees approximated \$23,470. The information system was placed in service in 2016. These amounts are recorded as an intangible asset and will be amortized straight-line over five years. The carrying basis and accumulated amortization of the recognized intangible asset at December 31, 2017 and 2016, were:

|  | Gross Carrying Amount | Accumulated Amortization | Net Carrying Value |
|--|-----------------------|--------------------------|--------------------|
| <b>December 31, 2017</b>                         |                       |                          |                    |
| Amortized intangible assets licensing agreements | \$ 23,490             | \$ (5,511)               | \$ 17,979          |
|  | \$ 23,490             | \$ (5,511)               | \$ 17,979          |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

| December 31, 2016                                | Gross Carrying<br>Amount | Accumulated<br>Amortization | Net Carrying<br>Value |
|--|--------------------------|-----------------------------|-----------------------|
| Amortized intangible assets licensing agreements | \$ 23,490                | \$ (800)                    | \$ 22,673             |
|  | \$ 23,490                | \$ (800)                    | \$ 22,673             |

### Note 8: Medical Malpractice Claims

Prior to March 22, 2004, the Corporation was covered under an occurrence-based policy for professional liabilities with an aggregate deductible of \$150.

Subsequent to that date, the Corporation provides for professional and general liability risk under a self-insured retention program (SIR). Under the SIR, the Corporation has self-insured the first \$2,000 of losses related to each claim, with a \$4,000 aggregate loss limit per year.

The Corporation has established SIR trust to hold assets designated to pay losses. The fair value of the SIR trust assets was \$13,132 (including unrealized gains of \$176) and \$16,161 (including unrealized gains of \$680) at December 31, 2017 and 2016, respectively. These assets were included in assets limited as to use as of December 31, 2017 and 2016.

The Corporation has purchased umbrella insurance for claims exceeding the SIR retention amounts. The umbrella insurance is through an excess carrier that covers aggregate claims up to \$15,000. Premium payments are amortized over the coverage period of the policy. Any liability for deductibles or claims exceeding coverage limits is recorded at the time it becomes probable and estimable.

The accrued medical malpractice claims liability was \$9,289 and \$8,756 at December 31, 2017 and 2016, respectively, and is included in the other long-term obligations liability in the accompanying consolidated balance sheets. The provision for expenses related to medical liability risks for 2017 and 2016, presented net of expected insurance recoveries in the consolidated statements of operations, are a net loss of \$533 and \$1,204 for 2017 and 2016, respectively.

The accrued medical malpractice claims liability represents the estimated ultimate cost of all reported and unreported losses incurred through the respective consolidated balance sheet dates. The liability for unpaid losses and loss expenses is estimated using actuarial analyses. Those estimates are subject to the effects of trends in loss severity and frequency. The estimates are continually reviewed and adjustments are recorded as experience develops or new information becomes known. The time period required to resolve these claims can vary depending upon whether the claim is settled or litigated. It is reasonably possible that this estimate could change materially in the near term.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### Note 9: Long-Term Debt

Long-term debt at December 31, 2017 and 2016, consists of the following:

|   | 2017              | 2016              |
|---|-------------------|-------------------|
| 2012 Note, Health Center (A)                        | \$ —              | \$ 7,875          |
| 2017 Note, Health Center (B)                        | 7,575             | —                 |
| Health Center Series 2011A Revenue Bonds (C)        | 12,575            | 99,700            |
| Health Center Series 2017 Revenue Bonds (D)         | 85,150            | —                 |
| 2010 Notes, Continuing Care Services (E)            | 499               | 28,680            |
| 2017 Note, Continuing Care Services (F)             | 26,507            | —                 |
| 2007 Promissory Notes, Continuing Care Services (G) | <u>921</u>        | <u>1,066</u>      |
|   | 133,227           | 137,321           |
| Plus unamortized premium on bonds                   | 11,015            | —                 |
| Less deferred financing costs                       | (1,279)           | (1,257)           |
| Less current maturities                             | <u>(6,229)</u>    | <u>(5,996)</u>    |
|   | <u>\$ 136,734</u> | <u>\$ 130,068</u> |

- (A) In June 2012, the Health Center issued the 2012 Note (2012 Note, Health Center). In connection with the issuance of the 2012 Note, Fifth Third Bank (Lessor), The Village of Anna, Ohio (Lessee) and the Health Center (Sublessee) simultaneously entered into Master Lease-Purchase and Sublease-Purchase Agreements related to the financed project, consisting of the renovation of the Bluffton Hospital and for future equipment acquisitions, facility renovations and reimbursement of certain prior capital expenditures. Under the terms of the agreement, the Health Center was required to make semiannual payments to the Lessor which were sufficient to meet the rental payments as required by the agreement. The Health Center held title to the project which it leased to the Lessor for \$1. At the conclusion of the lease period and payment of all related lease amounts, the Health Center retains title to the project assets. The 2012 Note was refinanced in December 2017, as further described in the 2017 Note, Health Center.
- (B) In December 2017, the Health Center issued the 2017 Note (2017 Note, Health Center). The 2017 Note was issued to refinance the 2012 Note. In connection with the issuance of the 2017 Note, Fifth Third Bank (Lessor), The Village of Bluffton, Ohio (Lessee) and the Health Center (Sublessee) simultaneously entered into Master Lease-Purchase and Sublease-Purchase Agreements related to the financed project, consisting of the renovation of the Bluffton Hospital and for future equipment acquisitions, facility renovations and reimbursement of certain prior capital expenditures. Under the terms of the agreement, the Health Center is required to make semiannual payments to the Lessor which are sufficient to meet the rental payments as required by the agreement. The Health Center holds title to the project which it leases to the Lessor for \$1. At the conclusion of the lease period and payment of all related lease amounts, the Health Center retains title to the project assets.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

The semiannual principal payments range from \$150 to \$238 (\$300 to \$475 per annum), plus interest. The lease obligation has a variable monthly interest payment that is calculated based on a factor of the one-month LIBOR rate (0.62 percent at December 31, 2017) and matures in December 2036. The Lessor, in its sole discretion, may require the Sublessee to purchase the project for the remaining principal payments due on the lease on December 31, 2024, and on any December 1 of each year thereafter, with 90-day notice. The Notes may be prepaid by the Sublessee at any time with no penalty.

- (C) The County of Hancock, Ohio (County) issued the Series 2011A Hospital Facilities Revenue Bonds (Series 2011A Bonds) in April 2011. The Series 2011A Bonds were issued to provide refunding of the Series 2004 Bonds. The Amended and Restated Lease dated March 1, 2011 (2011 Lease), required the Health Center to lease the Leased Premises from the County and make monthly basic rent payments sufficient to pay the principal and interest as they become due.

The Series 2011A Bonds were issued in the form of Serial Bonds of \$29,975 and Term Bonds of \$78,700 with maturities continuing through December 2034. Annual principal payments range from \$1,000 to \$7,600. The interest rates on these Serial Bonds and Term Bonds range from 3.00 percent to 6.50 percent. Total deferred issuance costs associated with the Series 2011A Bonds were \$1,257 at December 31, 2016. As a result of the issuance of the Series 2017 Bonds, remaining issuance costs were fully amortized in 2017 resulting in a loss on extinguishment of \$1,102.

The debt is subject to a Master Trust Indenture and a Supplemental Indenture (Master Indenture) which include various covenants. The Series 2011A Bonds are guaranteed by a pledge of gross receipts of each member of the Obligated Group (as defined in the Master Indenture) and a mortgage lien on certain facilities of the Health Center and Corporation. The Corporation, the Health Center, the Foundation, Continuing Care Services and BVMP are members of the Obligated Group.

In December 2017, an advance refunding of a portion of the Series 2011A Bonds occurred. The remaining 2011A Revenue Bonds have annual principal payments ranging from \$4,025 to \$4,350 and mature in December 2020. In addition to the loss recognized above related to remaining issuance costs, an escrow deposit agreement was established simultaneously with the issuance of the Series 2017 Bonds (see D below) to hold the Series 2011A Bonds that were advance refunded until maturity, which was funded in part by the proceeds from the Series 2017 Bonds and an additional escrow deposit of \$11,711, resulting in a total loss on extinguishment of \$12,813 associated with the advance refunding.

- (D) The Village of Bluffton, Ohio issued the Series 2017 Hospital Facilities Revenue Refunding Bonds (Series 2017 Bonds) in December 2017. The Series 2017 Bonds were issued to provide advance refunding of a portion of the Series 2011A Hospital Facilities Revenue Bonds.

The Series 2017 Bonds were issued in the form of serial bonds of \$85,150 with maturities continuing through December 2034. Annual principal payments range from \$4,925 to \$7,130. The interest rates on these Serial Bonds range from 4.00 percent to 5.00 percent. Total deferred issuance cost associated with the Series 2017 Bonds were \$1,203 at December 31, 2017. The Series 2017 Bonds were issued at a premium of \$11,015.

**Blanchard Valley Health System and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**Years Ended December 31, 2017 and 2016**  
(Dollar Amounts in Thousands)

The debt is subject to the same Lease, Master Trust Indenture and a Supplemental Indenture (Master Indenture) as the Series 2011A Bonds, which include various covenants. The Corporation, the Health Center, the Foundation, Continuing Care Services and BVMP are members of the Obligated Group.

- (E) In December 2010, Continuing Care Services issued the 2010 Notes (2010 Notes, Continuing Care Services). In connection with the issuance of the 2010 Notes, the Village of Bluffton (Lessee), Fifth Third Bank (Lessor) and Continuing Care Services (Sublessee) simultaneously entered into Master Lease-Purchase and Sublease-Purchase Agreements related to the financed projects. Continuing Care Services is required to make semiannual payments to the Lessee, which are sufficient to meet the rental payments as required by the Agreements. The Lessee holds the title to certain leasehold improvements, which Continuing Care Services subleases to operate and use certain improvements and additions from the financed projects, until the 2010 notes mature, at which time ownership will be transferred to the Sublessee. In addition, Continuing Care Services has agreed to maintain and properly insure the projects and pay other similar expenses. These agreements are secured by certain property, equipment and revenue of Continuing Care Services and are subject to the Master Trust Indenture including the various covenants.

A portion of the 2010 Notes were restructured and refinanced in December 2017, as further described in the 2017 Notes, Continuing Care Services.

The semiannual principal payment of the remaining 2010 Note is \$17 (\$33 per annum), plus interest. This Note has a variable monthly interest payment that is calculated based on a factor of the one-month LIBOR rate (1.98 percent at December 31, 2017) and matures in December 2032. The Lessor, in its sole discretion, may require the Sublessee to purchase the project for the remaining principal payments due on the lease on December 1 of any year commencing December 1, 2018 and thereafter, with 180 days notice. The Note may be prepaid by the Sublessee at any time with no penalty.

- (F) In December 2017, Continuing Care Services is the 2017 Note (2017 Note, Continuing Care Services). The 2017 Note was issued to refund and restructure a portion of the 2010 Notes. In connection with the issuance of the 2017 Note, Fifth Third Bank (Lessor), The Village of Bluffton (Lessee) and the Continuing Care Services (Sublessee) simultaneously entered into Master Lease-Purchase and Sublease-Purchase Agreements related to the financed projects. Continuing Care Services is required to make semiannual payments to the Lessee, which are sufficient to meet the rental payments as required by the Agreements. The Lessee holds the title to certain leasehold improvements, which Continuing Care Services subleases to operate and use certain improvements and additions from the financed projects, until the 2017 Note matures, at which time ownership will be transferred to the Sublessee. In addition, Continuing Care Services has agreed to maintain and properly insure the projects and pay other similar expenses. These agreements are secured by certain property, equipment and revenue of Continuing Care Services and are subject to the Master Trust Indenture including the various covenants.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

**Years Ended December 31, 2017 and 2016**

(Dollar Amounts in Thousands)

Semiannual principal payments range from \$189 to \$1,165 (\$382 to \$2,306 per annum), plus interest. The lease obligation has a variable monthly interest payment that is calculated based on a factor of the one-month LIBOR rate (2.25 percent at December 31, 2017) and matures in December 2032. The Lessor, in its sole discretion, may require the Sublessee to purchase the leased assets for the remaining principal payments due on the lease on December 1 of any year commencing December 1, 2024, with 90 days notice. The Note may be prepaid by the Sublessee at any time with no penalty. Total deferred issuance cost associated with the 2017 Note were \$76 at December 31, 2017.

- (G) In December 2007, Continuing Care Services entered into two promissory notes, related to the purchase of Independence House assets for \$2,844 (2007 Promissory Notes, Continuing Care Services). Monthly principal and interest payments commenced in 2008 in the amount of \$26 (\$312 per annum). During 2011, one of the promissory notes was paid in full. The remaining promissory note is due in January 2023, bears interest at a rate of 7 percent and is unsecured.

Future principal payments based on stated terms of debt obligations by year and in the aggregate, for the long-term debt at December 31, 2017, consist of the following:

|            | <b>2017 Note,<br/>Health<br/>Center</b> | <b>Series 2011A<br/>Bonds</b> | <b>Series 2017<br/>Bonds</b> | <b>2010 Notes,<br/>Continuing<br/>Care Services</b> | <b>2017 Notes,<br/>Continuing<br/>Care Services</b> | <b>2007<br/>Promissory<br/>Note</b> | <b>Total</b>      |
|------------|---|-------------------------------|------------------------------|---|---|-------------------------------------|-------------------|
| 2018       | \$ 300                                  | \$ 4,025                      | \$ -                         | \$ 33   | \$ 1,715  | \$ 156                              | \$ 6,229          |
| 2019       | 300                                     | 4,200                         | -                            | 33  | 1,789   | 167                                 | 6,489             |
| 2020       | 350                                     | 4,350                         | -                            | 33  | 1,868   | 180                                 | 6,781             |
| 2021       | 375                                     | -                             | 4,925                        | 33  | 1,950   | 193                                 | 7,476             |
| 2022       | 425                                     | -                             | 5,115                        | 33  | 2,036   | 206                                 | 7,815             |
| Thereafter | <u>5,825</u>                            | <u>-</u>                      | <u>75,110</u>                | <u>334</u>  | <u>17,149</u>                                       | <u>19</u>                           | <u>98,437</u>     |
|            | <u>\$ 7,575</u>                         | <u>\$ 12,575</u>              | <u>\$ 85,150</u>             | <u>\$ 499</u>                                       | <u>\$ 26,507</u>                                    | <u>\$ 921</u>                       | <u>\$ 133,227</u> |

Fair values of the Corporation's notes payable and long-term debt approximate the carrying value amounts at December 31, 2017 and 2016.

In early 2017, the Corporation entered into a \$30,000 line of credit. As of December 31, 2017, the line of credit was reduced to \$15,000. There were no draws on the line of credit through the issuance of the consolidated financial statements for 2017.

**Blanchard Valley Health System and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**Years Ended December 31, 2017 and 2016**  
(Dollar Amounts in Thousands)

**Note 10: Interest Rate Swap Agreement**

***2004 Swap***

In May 2004, the Health Center entered into an interest rate swap (2004 Swap) for a notional amount equal to the total amount of the 2004 Series Bonds. The 2004 Swap is a fixed rate payer swap that terminates in December 2034, and originally amortized in coordination with the 2004 Series Bonds. Under this agreement, the Health Center pays a fixed fee of 4.040 percent and receives a floating rate equal to 67 percent of one month of USD-LIBOR (0.912 percent at December 31, 2017). The original objective of the 2004 Swap was to hedge the risk of overall changes in the variable interest payments on the Series 2004 Bonds. The fair value of the 2004 Swap represents a payable to the counterparty and is recorded as a liability of \$20,742 and \$22,337 at December 31, 2017 and 2016, respectively. Under the 2004 Swap agreement, the Corporation pays or receives the net interest amounts monthly, with the monthly settlement amounts included in investment return.

The 2004 Swap was initially designated as a cash flow hedge and the effective portion of changes in the fair value of the 2004 Swap were recorded as a component of other changes in net assets.

On March 31, 2008, the 2004 Swap no longer qualified as an effective hedge due to volatility in the Series 2004 Bond R-FLOATS variable interest rates. Changes in fair value of the 2004 Swap after April 1, 2008, are being recorded in nonoperating gains (losses). The effective portion of the 2004 Swap not previously recognized in excess of revenue over expenses as of March 31, 2008, (\$14,939) was being amortized into nonoperating income over the remaining term of the 2004 Swap. In April 2012, the 2004 Swap was amended by mutual consent of the Health Center and the counterparty, changing the notional amount to equal the outstanding debt on the original Series 2004 Bonds repayment schedule, along with changes to other terms. As a result of the amendment, the notional amount of the 2004 Swap is no longer allocated to any specific debt and the remaining unamortized loss of approximately \$13,399 was recognized in net excess of revenue over expenses in full in 2011.

In 2012, The Health Center elected to make a partial termination payment on the 2004 Swap in the amount of \$5,811. The result of the termination payment was a \$60,730 reduction to the notional value of the swap during the periods of 2012 through 2014. This reduction in notional value reduced the monthly settlement amounts that the Health Center paid or received, with the monthly settlement amounts included in investment return. In 2014, this agreement was extended through 2016 and the Health Center made an additional payment of \$5,156. In April 2017, this agreement was further extended through April 2020 with no additional payment required.

The 2004 Swap agreement requires the Corporation to post collateral for negative fair value amounts above various threshold levels, ranging from \$0 to \$20,000, depending on the occurrence of an adverse surety event, as defined by the swap agreement. As of December 31, 2017 and 2016, no such adverse surety event has occurred.

A settlement of the fair value is required for the 2004 Swap upon the occurrence of various events, including a bond rating on the Series 2017 Bonds below Baa3 as determined by Moody's Investor's Service or BBB as determined by Standard & Poor's Rating Service.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

The table below presents certain information regarding the Corporation's 2004 interest rate swap agreement:

|  | 2017        | 2016        |
|--|-------------|-------------|
| Fair value of interest rate swap agreement | \$ (20,742) | \$ (22,337) |
| Change in fair value of 2004 Swap          | 1,595       | 942         |

The Corporation did not have any derivative instruments at December 31, 2017 and 2016, which were designated as hedging instruments.

### Note 11: Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets at December 31, 2017 and 2016, are available for the following purpose or periods:

|                                | 2017      | 2016     |
|--------------------------------|-----------|----------|
| Cancer center project          | \$ 660    | \$ 650   |
| Findlay campus                 | 2,130     | 1,744    |
| Heart care                     | 949       | 1,032    |
| Indigent care                  | 544       | 291      |
| Long-term care services        | 748       | 641      |
| Other health care services     | 3,497     | 3,930    |
| Accumulated endowment earnings | 2,092     | 1,145    |
|                                | \$ 10,620 | \$ 9,433 |

Permanently restricted net assets at December 31, 2017 and 2016, are restricted to:

|  | 2017      | 2016      |
|--|-----------|-----------|
| Endowment investments to be held in perpetuity, the income is to be used for the following purposes                    |           |           |
| Indigent care  | \$ 810    | \$ 792    |
| Equipment purchases  | 200       | 200       |
| Cancer center project  | 856       | 840       |
| Other health care services   | 1,135     | 1,090     |
| Total endowment investments  | 3,001     | 2,922     |
| Beneficial interest in perpetual trusts, the income is to be used for the indigent case and other health care services | 17,482    | 17,715    |
|  | \$ 20,483 | \$ 20,637 |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

The net assets released from restrictions were released for the following purposes:

|                      | <u>2017</u>     | <u>2016</u>     |
|----------------------|-----------------|-----------------|
| Health care services | \$ 503          | \$ 290          |
| Capital purchases    | <u>1,211</u>    | <u>1,953</u>    |
|                      | <u>\$ 1,714</u> | <u>\$ 2,243</u> |

### Note 12: Functional Expenses

The Corporation provides general health care services to residents in and around its geographic locations including medical/surgical, pediatric, critical, skilled nursing and emergency care.

Expenses relating to providing these services are as follows:

|                            | <u>2017</u>       | <u>2016</u>       |
|----------------------------|-------------------|-------------------|
| Health care services       | \$ 274,258        | \$ 260,455        |
| General and administrative | <u>49,110</u>     | <u>45,487</u>     |
|                            | <u>\$ 323,368</u> | <u>\$ 305,942</u> |

### Note 13: Defined Benefit Pension Plan

The Corporation has a noncontributory defined benefit pension plan (Plan) covering all employees who meet the eligibility requirements. The Corporation's funding policy is to make the minimum annual contribution that is required by applicable regulations, plus such amounts as the Corporation may determine to be appropriate from time to time. The Corporation expects to contribute approximately \$5,000 to the Plan in 2018.

Effective December 31, 2009, the Plan was amended to freeze all benefit accruals and will not permit any employees thereafter to become members of the Plan. As a result of the freeze, effective January 1, 2010, the employer match was increased in the defined contribution plan for all participants. Accordingly, the projected benefit obligation agrees to the accumulated benefit obligation as of December 31, 2017 and 2016.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

The Corporation uses a December 31 measurement date for the Plan. Information about the Plan's funded status follows:

|                                     | <b>2017</b>     | <b>2016</b>     |
|-------------------------------------|-----------------|-----------------|
| Change in benefit obligations       |                 |                 |
| Beginning of year                   | \$ (116,558)    | \$ (112,603)    |
| Interest and service cost           | (5,511)         | (5,484)         |
| Net actuarial gain (loss)           | (8,657)         | (4,274)         |
| Benefits paid                       | 4,866           | 5,046           |
| Expenses                            | 907             | 757             |
| End of year                         | (124,953)       | (116,558)       |
| Change in fair value of plan assets |                 |                 |
| Beginning of year                   | 78,473          | 74,084          |
| Actual return on plan assets        | 13,025          | 7,017           |
| Employer contributions              | 3,497           | 3,175           |
| Benefits paid                       | (4,866)         | (5,046)         |
| Expenses                            | (907)           | (757)           |
| End of year                         | 89,222          | 78,473          |
| <br>Funded status at end of year    | <br>\$ (35,731) | <br>\$ (38,085) |

Liabilities recognized in the consolidated balance sheets are as follows:

|                        | <b>2017</b> | <b>2016</b> |
|------------------------|-------------|-------------|
| Noncurrent liabilities | \$ (35,731) | \$ (38,085) |

Amounts not yet recognized as components of net periodic benefit cost consist of:

|                    | <b>2017</b> | <b>2016</b> |
|--------------------|-------------|-------------|
| Net actuarial loss | \$ 43,000   | \$ 41,981   |

The accumulated benefit obligation was \$124,953 and \$116,558 at December 31, 2017 and 2016, respectively.

Information for the pension plan with an accumulated benefit obligation in excess of Plan assets:

|                                | <b>2017</b>  | <b>2016</b>  |
|--------------------------------|--------------|--------------|
| Projected benefit obligation   | \$ (124,953) | \$ (116,558) |
| Accumulated benefit obligation | \$ (124,953) | \$ (116,558) |
| Fair value of Plan assets      | \$ 89,222    | \$ 78,473    |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

|   | 2017     | 2016     |
|---|----------|----------|
| Components of net periodic benefit costs                        |          |          |
| Interest and service cost                                       | \$ 5,511 | \$ 5,484 |
| Expected return on plan assets                                  | (6,239)  | (5,957)  |
| Recognized net actuarial loss                                   | 852      | 728      |
| Net periodic benefit cost (gain)                                | \$ 124   | \$ 255   |
| Other changes in Plan assets and benefit obligations recognized |          |          |
| other changes in unrestricted net assets                        |          |          |
| Amounts arising during period                                   |          |          |
| Net (gain) loss   | \$ 1,871 | \$ 3,214 |
| Amortization  |          |          |
| Net loss  | (852)    | (728)    |
| Total recognized in other changes in unrestricted net assets    | \$ 1,019 | \$ 2,486 |

The net loss and prior service cost that is estimated to be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are \$1,070 and \$0 for 2017, respectively. The net loss and prior service cost that is estimated to be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are \$946 and \$840 for 2016, respectively.

Significant assumptions include:

|  | 2017  | 2016  |
|--|-------|-------|
| Weighted-average assumptions used to determine benefit obligations |       |       |
| Discount rate  | 3.50% | 4.00% |
| Weighted-average assumptions used to determine benefit costs       |       |       |
| Discount rate  | 4.00% | 4.25% |
| Expected return on plan assets                                     | 7.75% | 7.75% |

The Corporation has estimated the long-term rate of return on Plan assets based primarily on historical returns on Plan assets, adjusted for changes in target portfolio allocations and recent changes in long-term interest rates based on publicly available information.

The following benefit payments are expected to be paid as of December 31, 2017:

|           |    |        |
|-----------|----|--------|
| 2018      | \$ | 5,100  |
| 2019      |    | 5,314  |
| 2020      |    | 5,493  |
| 2021      |    | 5,660  |
| 2022      |    | 5,879  |
| 2023-2027 |    | 31,830 |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

Plan assets are held by a bank-administered trust fund, which invests the Plan assets in accordance with the provisions of the Plan agreement. The Plan agreements permit investment in common stocks, corporate bonds and debentures, U.S. Government securities and other specified investments.

Asset allocation is primarily based on a strategy to provide stable earnings while still permitting the Plan to recognize potentially higher returns.

Plan assets are re-balanced quarterly. At December 31, 2017 and 2016, Plan assets by category are as follows:

|   | <u>2017</u> | <u>2016</u> |
|---|-------------|-------------|
| Equity securities                               | 59%         | 58%         |
| Debt securities                                 | 21          | 21          |
| Pooled investment and limited partnership funds | <u>20</u>   | <u>21</u>   |
|   | <u>100%</u> | <u>100%</u> |

### ***Pension Plan Assets***

Following is a description of the inputs and valuation methodologies used for pension plan assets measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of pension plan assets pursuant to the valuation hierarchy.

Where quoted market prices are available in an active market, plan assets are classified within Level 1 of the valuation hierarchy. Level 1 plan assets include money market mutual funds and exchange-traded mutual funds. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of plan assets with similar characteristics or discounted cash flows. Level 2 plan assets include pooled investment and limited partnerships funds. In certain cases where Level 1 or Level 2 inputs are not available, plan assets are classified within Level 3 of the hierarchy. There are no Level 3 plan assets.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

The fair values of the Corporation's pension plan assets at December 31, 2017 and 2016, by asset category are as follows:

| Asset Category                                  | 2017                          |  |   |   |                             |
|---|-------------------------------|--|---|---|-----------------------------|
|   | Fair Value Measurements Using |  |   |   |                             |
|   | Total Fair Value              | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Other Observable Inputs (Level 3) | Investments Measured at NAV |
| Money market mutual funds                       | \$ 108                        | \$ 108   | \$ —  | \$ —  | \$ —                        |
| Domestic equity mutual funds                    | 27,538                        | 27,538   | —   | —   | —                           |
| International equity mutual funds               | 25,330                        | 25,330   | —   | —   | —                           |
| Domestic fixed income mutual funds              | 17,496                        | 17,496   | —   | —   | —                           |
| International fixed income mutual funds         | 1,391                         | 1,391  | —   | —   | —                           |
| Pooled investment and limited partnership funds | <u>17,359</u>                 | <u>—</u>   | <u>—</u>                                      | <u>—</u>                                      | <u>17,359</u>               |
| Total   | <u>\$ 89,222</u>              | <u>\$ 71,863</u>   | <u>\$ 0</u>                                   | <u>\$ 0</u>                                   | <u>\$ 17,359</u>            |
| Asset Category                                  | 2016                          |  |   |   |                             |
|   | Fair Value Measurements Using |  |   |   |                             |
|   | Total Fair Value              | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Other Observable Inputs (Level 3) | Investments Measured at NAV |
| Money market mutual funds                       | \$ 36                         | \$ 36  | \$ —  | \$ —  | \$ —                        |
| Domestic equity mutual funds                    | 29,147                        | 29,147   | —   | —   | —                           |
| International equity mutual funds               | 16,436                        | 16,436   | —   | —   | —                           |
| Domestic fixed income mutual funds              | 12,706                        | 12,706   | —   | —   | —                           |
| International fixed income mutual funds         | 3,600                         | 3,600  | —   | —   | —                           |
| Pooled investment and limited partnership funds | <u>16,548</u>                 | <u>—</u>   | <u>—</u>                                      | <u>—</u>                                      | <u>16,548</u>               |
| Total   | <u>\$ 78,473</u>              | <u>\$ 61,925</u>   | <u>\$ 0</u>                                   | <u>\$ 0</u>                                   | <u>\$ 16,548</u>            |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts included above are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

The following tables present information regarding the nature and significant terms of the Corporation's pension plan assets invested in pooled investment and limited partnership funds at December 31, 2017 and 2016:

| <b>2017</b>                 |                   |                             |   |                                 |  |
|-----------------------------|-------------------|-----------------------------|---|---------------------------------|--|
| <b>Investments</b>          | <b>Fair Value</b> | <b>Unfunded Commitments</b> | <b>Redemption Frequency (if Eligible)</b> | <b>Redemption Notice Period</b> |  |
| Limited partnerships (A)    | \$ 1,400          | \$ 165                      | None                                      | N/A                             |  |
| Pooled investment funds (B) | 15,959            | —                           | Quarterly to annually                     | 15-370 days                     |  |
| <b>2016</b>                 |                   |                             |   |                                 |  |
| <b>Investments</b>          | <b>Fair Value</b> | <b>Unfunded Commitments</b> | <b>Redemption Frequency (if Eligible)</b> | <b>Redemption Notice Period</b> |  |
| Limited partnerships (A)    | \$ 2,186          | \$ 215                      | None                                      | N/A                             |  |
| Pooled investment funds (B) | 14,362            | —                           | Quarterly to annually                     | 15-370 days                     |  |

- (A) This category includes several private equity funds that invest in early stage, high-growth private companies, growth equity financing, leverage buyouts, securities and other obligations of distressed businesses and financially troubled companies. These investments can never be redeemed with the funds. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the funds. These investments are planned to be held and it is estimated that the underlying assets of the funds will be liquidated in approximately nine years. The fair value of the investments in this category have been estimated using the Corporation's ownership interests in partners' capital.
- (B) This category includes investments in hedge funds that invest primarily in other hedge funds, limited partnerships and investment companies. Management of these funds employs a variety of strategies and has the ability to shift investments based on market, economic, political and government driven events. The fair values of the investments in this category have been estimated using the net asset value per share of the investments. These investments can be redeemed and currently there are no restrictions.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### Note 14: Defined Contribution Pension Plan

The Corporation has a defined contribution pension plan for all qualified employees. The plan provides employer matching contributions based on employee contribution levels. The Corporation expensed approximately \$4,755 and \$4,579 in 2017 and 2016, respectively. The Corporation has no liability with respect to vested benefits under the plan.

### Note 15: Related Party Transactions

The Blanchard Valley Regional Health Center Auxiliary and the Bluffton Hospital Auxiliary are unincorporated nonprofit associations and are organized to conduct fundraising and promotional activities for the benefit of the Health Center. These Auxiliaries' bylaws provide that funds raised, net of expenses, be transferred to the Health Center for the specific purpose of acquiring equipment and related improvements. These Auxiliaries' bylaws also provide that amendments may be made only with the express approval of the Board of Trustees of the Corporation. Activities and management of the Auxiliaries are conducted by officers and committees elected and appointed by their members. These Auxiliaries contributed approximately \$220 and \$200 in 2017 and 2016, respectively, to the Health Center.

The Corporation maintains certain cash, investments and debt instruments at Fifth Third Bank, an institution where a Board member is an officer.

### Note 16: Investments in Equity Investees

Continuing Care Services has a 50 percent equity ownership joint venture in an assisted living project with Sunrise Assisted Living (Sunrise). As of December 31, 2017 and 2016, Continuing Care Services has a net book value related to this investment of \$0 and a liability related to cash distributions in excess of equity of \$1,111 and \$1,174, respectively. Birchaven does not guarantee the debt of Sunrise. Birchaven has recognized a gain of approximately \$63 and \$51 for its share of the 2017 and 2016 operating results, respectively.

The Health Center owns a 40 percent interest in a joint venture with area physicians to operate an ambulatory surgical center (Findlay Surgery). The Health Center recognized a gain (net of income taxes paid) of \$837 and a gain (net of income taxes paid) of \$829 on its share of the 2017 and 2016 operating results, respectively.

The Corporation has a 33 percent ownership in a joint venture with Wood County Hospital Association and Blakely Care Center to operate a diagnostic center called North Baltimore Medical and Diagnostic Center, LLC (North Baltimore). The Corporation recognized a loss of \$47 in 2017 on its share of the operating results. There was no gain or loss recognized for 2016.

The Corporation and its subsidiaries have minority ownership in a few additional joint ventures. The Corporation and its subsidiaries recognized a net gain of \$116 and a loss of \$51 in 2017 and 2016, respectively, on their share of the operating results.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

A summary of joint venture investments at December 31 is as follows:

|                 | 2017   | 2016     |
|-----------------|--------|----------|
| Sunrise         | \$ —   | \$ —     |
| Findlay Surgery | 608    | 648      |
| North Baltimore | 172    | 219      |
| Other           | 170    | 151      |
|                 | \$ 950 | \$ 1,018 |

Summary financial position information at December 31 for equity investees was as follows:

|                             | 2017      | 2016      |
|-----------------------------|-----------|-----------|
| Cash and investments        | \$ 3,006  | \$ 1,774  |
| Accounts receivable         | 2,082     | 1,090     |
| Property and equipment, net | 20,402    | 12,712    |
| Other assets                | 1,362     | 896       |
|                             | \$ 26,852 | \$ 16,472 |
| Accounts payable            | \$ 2,489  | \$ 1,232  |
| Long-term debt              | 16,267    | 16,187    |
|                             | 18,756    | 17,419    |
| Net assets (deficit)        | 8,096     | (947)     |
|                             | \$ 26,842 | \$ 16,472 |

### Note 17: Disclosures About Fair Value of Assets and Liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurement must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### Recurring Measurements

The following tables present the fair value measurements of financial assets and liabilities recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2017 and 2016:

|   | Fair Value Measurements Using                                  |   |   |      | Investments Measured at NAV |
|---|--|---|---|------|-----------------------------|
|   | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |      |                             |
| <b>December 31, 2017</b>                        |  |   |   |      |                             |
| <b>Assets</b>                                   |  |   |   |      |                             |
| Assets limited as to use                        |  |   |   |      |                             |
| Money market mutual funds                       | \$ 2,750   | \$ 2,750                                      | \$ —                                      | \$ — | \$ —                        |
| Domestic equity mutual funds                    | 102,528  | 102,528                                       | —   | —    | —                           |
| International equity mutual funds               | 80,410   | 80,410  | —   | —    | —                           |
| Domestic fixed income mutual funds              | 96,441   | 96,441  | —   | —    | —                           |
| International fixed income mutual funds         | 8,384  | 8,384   | —   | —    | —                           |
| Municipal bonds                                 | 36   | —   | 36  | —    | —                           |
| Corporate bonds                                 | 4,979  | —   | 4,979                                     | —    | —                           |
| Pooled investment and limited partnership funds | 59,463   | —   | —   | —    | 59,463                      |
| Beneficial interest in perpetual trusts         | 17,482   | —   | 17,482                                    | —    | —                           |
| <b>Liabilities</b>                              |  |   |   |      |                             |
| Interest rate swap agreement                    | (20,742)   | —   | (20,742)                                  | —    | —                           |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

|   | Fair Value Measurements Using |  |   |   | Investments Measured at NAV |
|---|-------------------------------|--|---|---|-----------------------------|
|   | Total                         | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |                             |
| <b>December 31, 2016</b>                        |                               |  |   |   |                             |
| <b>Assets</b>                                   |                               |  |   |   |                             |
| Assets limited as to use                        |                               |  |   |   |                             |
| Money market mutual funds                       | \$ 1,301                      | \$ 1,301   | \$ —  | \$ —                                      | \$ —                        |
| Domestic equity mutual funds                    | 108,050                       | 108,050  | —   | —   | —                           |
| International equity mutual funds               | 61,311                        | 61,311   | —   | —   | —                           |
| Domestic fixed income mutual funds              | 71,708                        | 71,708   | —   | —   | —                           |
| International fixed income mutual funds         | 11,972                        | 11,972   | —   | —   | —                           |
| Municipal bonds                                 | 1,966                         | —  | 1,966   | —   | —                           |
| Corporate bonds                                 | 2,194                         | —  | 2,194   | —   | —                           |
| Pooled investment and limited partnership funds | 54,890                        | —  | —   | —   | 54,890                      |
| Beneficial interest in perpetual trusts         | 17,715                        | —  | 17,715  | —   | —                           |
| <b>Liabilities</b>                              |                               |  |   |   |                             |
| Interest rate swap agreement                    | (22,337)                      | —  | (22,337)                                      | —   | —                           |

Following is a description of the valuation methodologies and inputs used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2017. There are no assets classified within Level 3 of the fair value hierarchy.

### Investments

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. There are no Level 3 securities.

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements Years Ended December 31, 2017 and 2016 (Dollar Amounts in Thousands)

The value of certain investments, classified as alternative investments, is determined using net asset value (or its equivalent) as a practical expedient. Investments for which the Corporation expects to have the ability to redeem its investments with the investee within 12 months after the reporting date are categorized as Level 2.

### ***Beneficial Interest in Perpetual Trusts***

Fair value is estimated at the present value of the future distributions expected to be received over the term of the agreement. Due to the nature of the valuation inputs, the interest is classified within Level 2 of the hierarchy.

### ***Interest Rate Swap Agreement***

The fair value is estimated using forward looking interest rate curves and discounted cash flows that are observable or that can be corroborated by observable market data and, therefore, are classified within Level 2 of the valuation hierarchy.

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying consolidated balance sheets at amounts other than fair value.

### **Note 18: The Fair Value Option**

As permitted by Topic 825, the Corporation has elected to measure pooled investment and limited partnership funds at fair value. Management has elected the fair value option for these items because they believe this provides a better matching of reported unrealized gains and losses on these investments to the periods in which the unrealized gains or losses occur.

See Note 4 for additional disclosures regarding fair value of each of the consolidated balance sheet line items listed in the preceding paragraph.

### ***Changes in Fair Value***

Changes in fair value for items for which the fair value option has been elected and the consolidated statements of operations and changes in unrestricted net assets (for nonoperating gains (losses) and other) section in which these unrealized losses on trading securities are reported are as follows:

|   | 2017   |  |                                   |
|---|--|--|-----------------------------------|
|   | Change in<br>Temporarily<br>Restricted<br>Net Assets | Change in<br>Permanently<br>Restricted<br>Net Assets | Total<br>Changes in Fair<br>Value |
| Assets limited as to use<br>Internally designated<br>Private equity and<br>other alternative<br>investments | \$ 3,907   | \$ _____   | \$ 3,907                          |

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

|   | 2016                            |  |  |                                   |
|---|---------------------------------|--|--|-----------------------------------|
|   | Nonoperating<br>Gains and Other | Change in<br>Temporarily<br>Restricted<br>Net Assets | Change in<br>Permanently<br>Restricted<br>Net Assets | Total<br>Changes in Fair<br>Value |
| Assets limited as to use<br>Internally designated<br>Private equity and<br>other alternative<br>investments | \$ 2,875                        | \$   | \$   | \$ 2,875                          |

Investment return for items for which the fair value option has been elected are measured at the actual interest income, dividend income and realized gains and losses associated with the investments and are included in nonoperating investment return in the accompanying consolidated statements of operations and changes in unrestricted net assets.

### Note 19: Significant Estimates and Concentrations

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

#### **Allowance for Net Patient Service Revenue Adjustments**

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

#### **Malpractice Claims**

Estimates related to the accrual for medical malpractice claims are described in Notes 1 and 8.

#### **Litigation**

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

# Blanchard Valley Health System and Subsidiaries

## Notes to Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

(Dollar Amounts in Thousands)

### ***Pension Benefit Obligations***

The Corporation has a noncontributory defined benefit pension plan whereby it agrees to provide certain postretirement benefits to eligible employees. The benefit obligation is the actuarial present value of all benefits attributed to service rendered prior to the valuation date based on the projected unit credit cost method. It is reasonably possible that events could occur that would change the estimated amount of this liability materially in the near term.

### **Note 20: Subsequent Events**

Subsequent events have been evaluated through April 24, 2018, which is the date the consolidated financial statements were issued.

### **Note 21: Future Changes in Accounting Principles**

#### ***Presentation of Financial Statements for Not-for-Profit Entities***

The Financial Accounting Standards Board recently issued Accounting Standards Update (ASU) No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*, which changes requirements for financial statements and notes of all not-for-profit (NFP) entities and is effective for fiscal years beginning after December 15, 2017.

A summary of the changes by financial statement area most relevant to the Corporation are as follows:

#### Balance Sheet:

- The balance sheet will distinguish between two new classes of net assets - those with donor-imposed restrictions and those without. This is a change from the previously required three classes of net assets - unrestricted, temporarily restricted and permanently restricted.

#### Statement of Operations:

- Expenses are reported by both nature and function in one location.
- Investment income is shown net of external and direct internal investment expenses. Disclosure of the expenses netted against investment income is no longer required.

#### Notes to the Financial Statements:

- Enhanced quantitative and qualitative disclosures provide additional information useful in assessing liquidity and cash flows available to meet operating expenses for one-year from the date of the statement of financial position.
- Amounts and purposes of governing Board designations and appropriations as of the end of the period are disclosed.

# **Blanchard Valley Health System and Subsidiaries**

## **Notes to Consolidated Financial Statements**

**Years Ended December 31, 2017 and 2016**

(Dollar Amounts in Thousands)

The Corporation is in the process of evaluating the impact the amendment will have on the consolidated financial statements.

### ***Revenue Recognition***

The Financial Accounting Standards Board amended its standards related to revenue recognition. This amendment replaces all existing revenue recognition guidance and provides a single, comprehensive revenue recognition model for all contracts with customers. The guidance provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include capitalization of certain contract costs, consideration of the time value of money in the transaction price and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. The amendment also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in those judgments and assets recognized from costs incurred to fulfill a contract. The standard allows either full or modified retrospective adoption effective for annual periods beginning after December 15, 2017, for not-for-profits that are conduit debt obligors, and any interim periods within annual reporting periods that begin after December 15, 2018, for not-for-profits that are conduit debt obligors. The Corporation is in the process of evaluating the impact the amendment will have on the consolidated financial statements.

### ***Accounting for Leases***

The Financial Accounting Standards Board amended its standard related to the accounting for leases. Under the new standard, lessees will now be required to recognize substantially all leases on the balance sheet as both a right-of-use asset and a liability. The standard has two types of leases for income statement recognition purposes: operating leases and finance leases. Operating leases will result in the recognition of a single lease expense on a straight-line basis over the lease term similar to the treatment for operating leases under existing standards. Finance leases will result in an accelerated expense similar to the accounting for capital leases under existing standards. The determination of lease classification as operating or finance will be done in a manner similar to existing standards. The new standard also contains amended guidance regarding the identification of embedded leases in service contracts and the identification of lease and nonlease components in an arrangement. The new standard is effective for annual periods beginning after December 15, 2018 for not-for-profits that are conduit debt obligors, and any interim periods within annual reporting periods that begin after December 15, 2018, for not-for-profits that are conduit debt obligors. The Corporation is evaluating the impact the standard will have on the consolidated financial statements.