



**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
AFFILIATES**

Consolidated Financial Statements

December 31, 2017 and 2016

(With Independent Auditors' Report Thereon)

**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
AFFILIATES**

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Independent Auditors' Report

The Board of Directors
Children's Hospital & Medical Center and
Affiliates Omaha, Nebraska:

We have audited the accompanying consolidated financial statements of Children's Hospital & Medical Center and Affiliates (the Company), 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 Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Children's Hospital & Medical Center and Affiliates as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.



Other Matters

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information included in exhibits 1 through 3 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Omaha, Nebraska
May 24, 2018

**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
AFFILIATES**

Consolidated Balance Sheets

December 31, 2017 and 2016

(Dollars in thousands)

Assets	2017	2016
Current assets:		
Cash and cash equivalents	\$ 68,619	32,296
Patient accounts receivable, net of allowance for doubtful accounts of \$3,868 and \$3,434 in 2017 and 2016, respectively	70,944	56,192
Current portion of pledges receivable	6,881	6,092
Other receivables	7,791	11,771
Prepaid expenses and other assets	15,841	11,782
Estimated third-party payor settlements	10,187	10,129
Total current assets	<u>180,263</u>	<u>128,262</u>
Restricted cash	5,011	7,467
Assets limited as to use	91,067	—
Pledges receivable, net of current portion	11,284	11,212
Long-term investments (including restricted investments of \$15,473 and \$11,769 in 2017 and 2016, respectively)	417,471	366,469
Property and equipment, net	229,197	232,198
Other assets	7,307	7,058
Total assets	<u>\$ 941,600</u>	<u>752,666</u>
Liabilities and Net Assets		
Current liabilities:		
Current portion of long-term debt	\$ 5,043	4,399
Trade accounts payable	19,188	17,562
Construction payables	2,597	517
Affiliate payables	1,385	1,247
Accrued salaries	25,477	22,646
Other accrued expenses	11,996	11,936
Total current liabilities	<u>65,686</u>	<u>58,307</u>
Long-term debt and other obligations, net of current portion	181,084	90,714
Other liabilities	8,524	8,631
Total liabilities	<u>255,294</u>	<u>157,652</u>
Net assets:		
Unrestricted	639,008	555,209
Noncontrolling interest	3,459	4,073
Total unrestricted net assets	<u>642,467</u>	<u>559,282</u>
Temporarily restricted	37,872	30,077
Permanently restricted	5,967	5,655
Total net assets	<u>686,306</u>	<u>595,014</u>
Total liabilities and net assets	<u>\$ 941,600</u>	<u>752,666</u>

See accompanying notes to consolidated financial statements.

**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
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Consolidated Statements of Operations

Years ended December 31, 2017 and 2016

(Dollars in thousands)

	2017	2016
Unrestricted revenue, gains, and other support:		
Net patient service revenue	\$ 418,234	383,646
Provision for bad debt	2,871	3,195
Net patient service revenue less provision for bad debt	415,363	380,451
Contributions for use in operations	4,569	4,495
Other revenue	13,551	11,731
Total unrestricted revenues, gains, and other support	433,483	396,677
Operating expenses:		
Salaries, wages, and agency staffing	180,037	162,863
Employee benefits	40,467	35,680
Supplies and pharmaceuticals	52,900	50,355
Outside services and professional fees	36,764	32,192
Other operating expenses	29,944	33,128
Depreciation and amortization	24,677	24,252
Affiliation support	14,154	12,271
Occupancy	10,920	10,462
Interest	3,808	4,645
Loss on sale of property and equipment	238	—
Total operating expenses	393,909	365,848
Operating income	39,574	30,829
Other income:		
Net investment income	41,253	25,736
Change in interest rate swap valuation	690	883
Other nonoperating income	166	166
Total other income, net	42,109	26,785
Excess of revenue, gains, and other support over expenses	81,683	57,614
Other changes in unrestricted net assets:		
Net assets released from restrictions used for property and equipment	1,502	2,039
Increase in unrestricted net assets	\$ 83,185	59,653

See accompanying notes to consolidated financial statements.

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Consolidated Statements of Changes in Net Assets

Years ended December 31, 2017 and 2016

(Dollars in thousands)

	2017	2016
Unrestricted net assets:		
Excess of revenue, gains, and other support over expenses	\$ 81,683	57,614
Net assets released from restrictions used for property and equipment	1,502	2,039
Increase in unrestricted net assets	83,185	59,653
Temporarily restricted net assets:		
Contributions restricted by donor	9,525	20,479
Investment income	152	113
Change in value of split-interest agreements	(236)	(83)
Net assets released from restrictions	(1,646)	(2,475)
Increase in temporarily restricted net assets	7,795	18,034
Permanently restricted net assets:		
Contributions restricted by donor	237	215
Change in value of split-interest agreements	75	61
Increase in permanently restricted net assets	312	276
Increase in net assets	91,292	77,963
Net assets, beginning of year	595,014	517,051
Net assets, end of year	\$ 686,306	595,014

See accompanying notes to consolidated financial statements.

**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
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Consolidated Statements of Cash Flows
Years ended December 31, 2017 and 2016
(Dollars in thousands)

	2017	2016
Cash flows from operating activities:		
Increase in net assets	\$ 91,292	77,963
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Change in interest rate swap valuation	(690)	(883)
Depreciation and amortization	24,677	24,252
Loss on sale of property and equipment	238	—
Realized and unrealized (gains) loss on investments, net	(31,346)	(19,029)
Change in value of split-interest agreements	161	22
Provision for bad debt	2,871	3,195
Restricted contributions and investment income, net	(9,914)	(20,807)
Amortization of debt issuance costs	21	—
Amortization of debt (premiums) and discounts, net	(293)	(37)
Changes in operating assets and liabilities:		
Patient accounts receivable	(17,623)	(9,813)
Other receivables	3,980	136
Prepaid expenses and other assets	(4,059)	(2,659)
Estimated third-party payor settlements	(58)	(4,085)
Other assets	(409)	(640)
Trade accounts payable	1,626	1,431
Affiliate payables	138	510
Accrued salaries	2,831	2,551
Other accrued expenses	60	2,437
Other liabilities	583	585
Net cash provided by operating activities	64,086	55,129
Cash flows from investing activities:		
Purchase of property and equipment	(24,513)	(63,408)
Proceeds from sale of property and equipment and land	5,216	—
Proceeds from sale of long-term investments	120,148	95,541
Purchases of long-term investments	(139,803)	(104,526)
Purchases of assets limited as to use	(91,067)	—
Proceeds from sale of short-term investments	—	4,350
Net cash used in investing activities	(130,019)	(68,043)
Cash flows from financing activities:		
Payments on long-term debt and other obligations	(62,389)	(4,351)
Issuance of long-term debt	154,061	—
Debt issuance costs incurred	(925)	—
Restricted contributions and investment income received	9,053	9,860
Net cash provided by financing activities	99,800	5,509
Net (decrease) increase in cash and cash equivalents	33,867	(7,405)
Cash and cash equivalents and restricted cash, beginning of year	39,763	47,168
Cash and cash equivalents and restricted cash, end of year	\$ 73,630	39,763
Supplemental disclosure of cash flow information:		
Cash paid for the year for interest	\$ 4,118	4,706
Non cash operating and investing activities:		
Purchases of property and equipment in accounts payable	\$ 788	—
Issuance of capital lease	538	—
Cash and cash equivalents	\$ 68,619	32,296
Restricted cash	5,011	7,467
Cash and cash equivalents and restricted cash, end of year	\$ 73,630	39,763

See accompanying notes to consolidated financial statements.

CHILDREN'S HOSPITAL & MEDICAL CENTER AND AFFILIATES

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

(Dollars in thousands)

(1) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Children's Hospital & Medical Center (the Hospital) and its affiliates (collectively, the Company). The affiliates are Children's Physicians and Children's Hospital & Medical Center Foundation (the Foundation), both not-for-profit organizations; and Children's Health Network, a not-for-profit taxable corporation. Significant intercompany accounts and transactions have been eliminated in the consolidation.

The mission of the Hospital is to improve the life of every child through dedication to exceptional clinical care, research, education, and advocacy. The Hospital operates a 145-bed pediatric hospital, which includes seven surgical suites, a hybrid heart catheterization lab, a 33-bed Children's Ambulatory Recovery and Express Stay (CARES) unit, an outpatient surgery center, a heart transplant program and a fetal care center that focuses on the coordination of care for babies diagnosed with complex congenital defects before birth. Children's Specialty Pediatric Center offers 50+ outpatient specialty clinics, providing diagnostics, treatment, and therapy. In addition, Children's provides outpatient eating disorder services and a full array of pediatric home health care services to children and adolescents who have immediate or long-term health care needs, including home medical equipment rentals and sales, home health nursing, in-home private duty nursing and home infusion therapy services. The Hospital is home to the region's only Level IV Newborn Intensive Care Unit and the only dedicated pediatric emergency department with Level II Pediatric Trauma verification. The Hospital also provides specialty pediatric care services in communities across a five-state region.

Children's Physicians is a pediatric healthcare provider organization for Omaha and surrounding communities that owns and operates primary care pediatric clinics. The clinics also serve as resident training sites for pediatric residents. Children's Physicians has two voting members – Children's Hospital & Medical Center, a Nebraska not-for-profit corporation (two-thirds or majority voting membership) and Creighton University, a Nebraska not-for-profit corporation (one-third or noncontrolling voting membership). As of December 31, 2017, Children's Physicians operates 14 clinical sites. Creighton University's accumulated noncontrolling interest is recognized in the consolidated balance sheets as part of net assets.

The Foundation's purpose is to manage and distribute funds solicited from the public to further the mission and purpose of the Hospital.

Children's Health Network is a messenger model physician hospital organization composed of more than 434 general pediatricians, family practitioners, and pediatric specialists as well as Children's Hospital & Medical Center employed physicians and other providers committed to improving the health status of children.

In 2007, the Hospital entered into an Institutional Affiliation Agreement (IAA) with the Board of Regents of the University of Nebraska acting through the University of Nebraska Medical Center (UNMC), which provides 50% ownership of Nebraska Pediatric Practice (NPP) for each party. Under the terms of this agreement, the Hospital is responsible for funding any annual operating deficits incurred as a result of NPP operations (note 14) and is accounted for using the equity method as reflected in affiliation support in the consolidated statements of operations.

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(2) Summary of Significant Accounting Policies

(a) Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles 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. Significant items subject to such estimates and assumptions include the useful lives of fixed assets, allowances for doubtful accounts, contractual adjustments to revenue, investment valuation, and professional liability reserves and loss recoverables.

(b) Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with original maturities of three months or less that have not otherwise been classified as long-term assets due to a designation for long-term purposes.

(c) Restricted Cash

Restricted cash is cash and cash equivalents that are donor restricted or board designated for expenditures in the acquisition or construction of noncurrent assets.

(d) Allowance for Doubtful Accounts and Contractual Adjustments

Accounts receivable are reduced by an allowance for doubtful accounts and contractual adjustments. In evaluating patient accounts receivable by financial class, management regularly reviews an analysis of its historical collectibility trends along with an aging of accounts receivable. For receivables associated with services provided to patients, collectibility is determined based on a combination of historical trends and contractual agreements. For receivables associated with self-pay patients, including patients without insurance and patients with deductibles and copayments, management analyzes historical trends in each of its predetermined stages of collectibility and status of agreed-upon payment plans. The difference between the standard or negotiated discounted rates and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

(e) Investments and Investment Income

Investments in equity securities with readily determinable fair values and investments in debt securities are measured at fair value in the accompanying consolidated balance sheets. Alternative investments are valued at net asset value as a practical expedient to estimated fair values. The estimated values as determined by the respective fund's general manager and investment managers may differ significantly from the values that would have been used had ready markets existed. Real estate held in investments is valued based on contributed value at the time of donation.

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The Company has designated its investment portfolio as trading. Accordingly, unrealized gains and losses on investments are reported within excess of revenue, gains, and other support over expenses. The Company presents the purchase and investment of securities as an investing activity.

Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in the excess of revenue, gains, and other support over expenses, unless the income or loss is restricted by donor.

Periodically, the Company reviews its investment portfolio to determine whether any unrealized losses on securities are other than temporary. To determine whether impairment is other-than-temporary, the Company considers all information relevant to the collectability of the security, including past events and current conditions. Evidence considered in this assessment includes the reasons for the impairment, the severity, and duration of the impairment, and the general market condition in the geographic area or industry the investee operates in. The company recognized \$719 and \$0 other-than-temporary impairment loss in 2017 and 2016, respectively.

(f) Property and Equipment

Property and equipment acquisitions are recorded at cost or, if donated, at fair market value on the date of the gift. Depreciation is provided over the estimated useful life of each class of depreciable asset and are computed using the straight-line method based on the following useful lives:

Buildings and leasehold improvements	5–40 years
Equipment and furnishings	3–10 years

Equipment under capital lease obligations is stated at the present value of future minimum lease payments amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is presented with depreciation in the consolidated financial statements.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from the excess of revenue, gains, and other support over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(g) Assets Limited to Use

Assets limited to use represent investments limited for specific purposes, such as certain improvements to healthcare facilities and proceeds of debt issues deposited with a trustee and limited to use in accordance with the requirements of the master agreement.

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(h) Other Assets

Other assets include interests in split-interest agreements and deferred compensation assets. The Hospital and Foundation have been named the beneficiaries of irrevocable charitable remainder trust agreements in which each will receive certain funds upon termination of the trusts. Contribution revenue is recognized in the period in which the gift is established or when the Hospital or Foundation receives notice of the gift's existence. The contribution and associated receivable are recorded by discounting the future gift amount to its net present value. Adjustments to reflect the amortization of the discount rate and changes in actuarial assumptions are recognized as a temporarily or permanently restricted change in value of split-interest agreements.

The Foundation is also a beneficiary of perpetual trusts, and annually receives the income on the trusts' assets as earned in perpetuity. Contribution revenue is recognized in the period in which the trusts are established or when the Foundation receives notice of the trust's existence. The contributions and associated assets are recorded by discounting the future gift amount to its net present value.

The Hospital offers a 457b retirement plan. The Hospital maintains investment balances, within other assets, equal to the Hospital's total liability under this deferred compensation retirement plan. The investment balances related to the 457b retirement plan were \$3,690 and \$3,280 as of December 31, 2017 and 2016, respectively.

(i) Deferred Debt Issuance Costs

Financing and legal costs incurred in connection with the issuance of long-term debt are amortized over the term of the related debt using the effective interest rate method. Unamortized costs are presented on the consolidated balance sheets as a direct deduction of debt liabilities.

(j) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained in perpetuity. The Company applies the provisions of the Nebraska Uniform Prudent Management of Institutional Funds Act (the Act) in managing its endowment. The Company classifies as permanently restricted net assets (a) the original value of the gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Hospital in a manner consistent with the standard of prudence prescribed by the Act.

(k) Unrestricted Net Assets

Unrestricted net assets represent assets accumulated through the Company's operations that are not restricted by outside donors. This includes assets with a board designation or assets whose use is contractually limited, such as proceeds of debt issues deposited with a trustee and limited to use in accordance with the requirements of the master agreement. Board-designated unrestricted net assets

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are neither temporarily nor permanently restricted by donor stipulations, but rather designated by the board for specified purposes.

(l) Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. 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.

(m) Financial Assistance

The Hospital and Children's Physicians (collectively, the Healthcare Providers) provide care to patients who meet certain criteria under its financial assistance policy without charge or at amounts less than its established rates. Because the Healthcare Providers do not pursue collection of amounts determined to qualify for financial assistance, they are not reported in the consolidated statements of operations. The amount of cost for services and supplies furnished under the Company's financial assistance policy aggregated at \$3,634 and \$3,464 in 2017 and 2016, respectively, utilizing the ratio of costs to charges.

(n) Donor-Restricted Gifts

Unconditional promises to give cash and other assets to the Company are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value when the conditions have been substantially met. Intentions to give are not recorded until they become unconditional promises to give. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reflected as unrestricted contributions in the accompanying consolidated financial statements.

Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of the discounts is included in contribution revenue.

(o) Fair Value of Financial Instruments

The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. The Company determines fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements,

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the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

- Level 1 inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to the reporting entity at the measurement date
- Level 2 inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability
- Level 3 inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at measurement date

(p) *Derivative Instruments and Hedging Activities*

The Company accounts for derivatives and hedging by recognizing all derivative instruments as either assets or liabilities in the consolidated balance sheets at their respective fair values. Changes in the fair value of derivatives are recognized in other income.

The fair value of interest rate swaps is determined using pricing models developed based on the LIBOR swap rate and other observable market data.

(q) *Income Taxes*

All affiliated entities, with the exception of Children's Health Network, have been recognized as not-for-profit corporations by the Internal Revenue Service as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. Children's Health Network is a not-for-profit taxable corporation that has net taxable operating losses and, therefore, has no tax liability. The United States is the major tax jurisdiction for the Company and 2014 is the earliest tax year subject to examination.

The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. During 2017 and 2016, the Company did not record any amounts related to uncertain tax positions or any accrued interest and penalties.

H.R. 1, originally known as the Tax Cuts and Jobs Act (the Act), was signed into law on December 22, 2017. The Act contains various provisions affecting both for-profit and not-for-profit entities. Tax-exempt entities are impacted in part by the inclusion of a new excise tax on excess compensation for covered employees, changes to unrelated business income, as well as their ability to advance refund bonds. In addition, tax-exempt entities may be impacted through certain for-profit subsidiaries and/or joint ventures based on the Act's provisions for tax rates, measurement of deferred taxes as well as other limitations on deductions. The Act's provisions may also impact donor incentives for charitable giving. Management is currently assessing the overall impact of the Act and its impact on the financial statements.

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(r) Excess of Revenue, Gains, and Other Support over Expenses

The performance indicator is the excess of revenue, gains, and other support over expenses. Changes in unrestricted net assets that are excluded from excess of revenue, gains, and other support over expenses, consistent with industry practice, include contributions of long-lived assets (including assets acquired using contributions that by donor restriction were to be used for purposes of acquiring such assets) and other net asset transfers.

(s) Estimated Malpractice Costs

The provision for estimated medical malpractice claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported.

(t) Reclassifications

Certain reclassifications have been made to the prior year consolidated financial statements to conform to the current year presentation. These reclassifications have not changed the results of operations of the prior period.

(u) New Accounting Pronouncements

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. ASU 2016-14 will change the way not-for profit entities, including healthcare entities, report net asset classes, expenses, and liquidity in their financial statements. The new guidance is effective for annual financial statements issued for fiscal years beginning after December 15, 2017, and requires retrospective application in the year of adoption. The Company will adopt the new standard as of January 1, 2018. The company is continuing to evaluate the effects the adoption of this standard will have on its financial statements and financial disclosures.

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update ASU 2016-02, *Leases* (Topic 842), (ASU 2016-02). ASU 2016-02 requires the lessee to recognize assets and liabilities for leases with lease terms of more than 12 months. For leases with a term of 12 months or less, the Company is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. Further, the lease standard requires a finance lease to recognize both interest expense and amortization expense related to the right of use asset. Operating leases generally recognize the associated expense on a straight-line basis. ASU 2016-02 requires the Company to adopt the standard using a modified retrospective approach and adoption beginning on January 1, 2019. The Company is currently evaluating the impact that ASU 2016-02 will have on its financial position, results of operations, and cash flows.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*. ASU 2014-09 provides a single model for recognizing revenue arising from contracts with customers and supersedes current revenue recognition guidance. This ASU requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of goods or services and will replace existing revenue recognition guidance in U.S. GAAP when it becomes effective. This ASU became effective for the Company on January 1, 2018. As a practical expedient, the Company applied the revenue guidance to a portfolio of contracts with similar characteristics. While the adoption of ASU 2014-09 will impact

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certain disclosures, it will not materially impact the financial position, result of operations or cash flows of the Company. There was no cumulative effect of a change in accounting principal recorded related to the adoption of ASU 2014-09 on January 1, 2018.

(3) Net Patient Service Revenue

The Healthcare Providers have agreements with third-party payors that provide for payments at amounts different from their established rates.

The Healthcare Providers have entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment under these agreements consists primarily of discounts from established charges.

Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. Outpatient Medicaid services are reimbursed based on a percentage rate representing the discounted average ratio of cost to charges. The Hospital also receives a Disproportionate Share Payment annually from the State of Nebraska Department of Health and Human Services.

Physician clinic services are paid based on fee schedule amounts. The following sets forth the Healthcare Providers' patient service revenue at its established rates and related revenue deductions for the years ended December 31, 2017 and 2016:

	2017	2016
Patient service revenue:		
Hospital:		
Inpatient services	\$ 362,270	311,292
Outpatient services	347,164	314,407
Children's Physicians	66,414	60,782
Total patient service revenue	775,848	686,481
Deductions, including provision for bad debts of \$2,871 and \$3,195 in 2017, and 2016, respectively	360,485	306,030
Patient service revenue, net of deductions	\$ 415,363	380,451

Net patient service revenue from the Medicaid program accounted for approximately 29% of the Healthcare Providers' net patient service revenue for the years ended December 31, 2017 and 2016, respectively.

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Patient service revenue, net of adjustments, recognized in 2017 and 2016 from major payor sources is as follows:

	<u>2017</u>	<u>2016</u>
Medicaid	\$ 121,414	109,518
Commercial insurance and other third-party payors	287,378	265,554
Patient (self-pay)	<u>6,571</u>	<u>5,379</u>
Patient service revenue, net of deductions	<u>\$ 415,363</u>	<u>380,451</u>

(4) Pledges Receivable

The Company has received certain pledges to support operations and other designated purposes. Pledges receivable consist of the following as of December 31:

	<u>2017</u>	<u>2016</u>
Rainbow House Redevelopment	\$ 930	2,054
Dr. C. C. & Mabel L. Criss Heart Center	627	915
Changing Lives Together capital campaign	16,889	14,290
Other	<u>427</u>	<u>698</u>
	18,873	17,957
Less:		
Unamortized discount	516	441
Allowance for uncollectibles	<u>192</u>	<u>212</u>
Net pledges receivable	<u>\$ 18,165</u>	<u>17,304</u>
Amounts due in:		
Less than one year	\$ 6,881	6,092
One to five years	<u>11,992</u>	<u>11,865</u>
	18,873	17,957
Less unamortized discounts and allowances	<u>708</u>	<u>653</u>
Net pledges receivable	<u>\$ 18,165</u>	<u>17,304</u>

Pledges receivable were discounted utilizing interest rates ranging from 1.43% to 1.84%.

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(5) Investments

The composition of investments and assets limited to use at December 31, 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
At fair value:		
Cash and cash equivalents	\$ 33,120	63,571
Corporate and municipal bonds	267,085	96,212
Common and preferred stocks	28,879	30,209
Mutual funds	115,899	114,268
	<u>444,983</u>	<u>304,260</u>
At net asset value:		
Investment in partnerships	63,552	62,206
At cost:		
Real estate held for resale	3	3
Total	<u>\$ 508,538</u>	<u>366,469</u>

All investment income and realized and unrealized gains and losses related to investment transactions are included in investment income in the consolidated statements of operations.

Investment income is comprised of the following for the years ended December 31, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Other-than-temporary impairment	\$ (719)	—
Dividend and interest income	9,907	6,707
Net realized gains	13,133	11,167
Net unrealized gains	18,932	7,862
Total investment income	<u>\$ 41,253</u>	<u>25,736</u>

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For investments in partnerships, the Company used the net asset value reported by the underlying fund as a practical expedient to estimate the fair value of the investment. Below is a summary of investments accounted for at net asset value:

	<u>2017</u>	<u>2016</u>	Redemption frequency (if currently eligible)	Redemption notice period
Absolute return (a)	\$ 47,658	45,808	Quarterly/annually Life of investment	45–90 days
Private equity/venture capital funds (b)	7,330	5,508	Life of investment	Life of investment
Real assets (c)	723	1,171	Life of investment	Life of investment
Domestic equity (d)	<u>7,841</u>	<u>9,719</u>	Quarterly/annually	60 days
	<u>\$ 63,552</u>	<u>62,206</u>		

- (a) This category includes investments in funds that invest primarily in event-driven investments, which seek to exploit situations in which announced or anticipated events create inefficiencies in valuations of securities (hedging using multiple strategies such as merger arbitrage, restructuring, exchange offers, distressed debt, credit, options and other derivatives, and initial public offerings). At December 31, 2017, \$3,036 of this category is locked-up for the life of the investment.
- (b) This category includes seven partnerships. Six partnerships invest primarily in private equities related to the oil and gas sectors predominately in North America. The seventh partnership in this category invests in growth-oriented equities across a broad variety of sectors. At December 31, 2017, there were unfunded commitments of \$2,537 related to this category. It is estimated that the underlying assets of the fund will be liquidated over the next 2 to 8 years.
- (c) This category includes investments in funds that invest in a geographically diverse portfolio of real estate investments, principally industrial, office, residential, and retail properties. The term of each partnership is 10 years from the date of when substantially all capital commitments are invested. It is estimated that the underlying assets of the fund will be liquidated over the next 2 to 10 years.
- (d) This category invests in funds that primarily invest in U.S. common stocks. Those included in this category pursue a long-short strategy. Lockup period ranges from 12 to 36 months from the original subscription period. Redemption dates range between June 30, 2018 and December 31, 2018.

Due to the nature of the investments held by the funds, changes in market conditions, and the economic environment may significantly impact the net asset value of the funds and, consequently, the fair value of the Company's interests in the funds. Although a secondary market exists for these investments, it is not active and individual transactions are typically not observable. When transactions do occur in this limited secondary market, they may occur at discounts to the reported net asset value. It is, therefore, reasonably

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possible that if the Company were to sell these investments in the secondary market, a buyer may require a discount to the reported net asset value, and the discount could be significant.

The Company has designated certain investment funds to be used for specified purposes as of December 31, 2017 and 2016. These board designations include the Pediatric Enrichment Fund with \$40,813 and \$42,631 as of December 31, 2017 and 2016, respectively, and \$10,000 each year to support the UNMC affiliation agreement and a reserve fund held by trustee for the Series 2008B Bonds with \$788 and \$7,182, respectively.

(6) Property and Equipment

Property and equipment as of December 31, 2017 and 2016 consisted of the following:

	<u>2017</u>	<u>2016</u>
Land	\$ 19,381	21,173
Building and leasehold improvements	271,004	270,888
Equipment and furnishings	119,849	118,533
Construction in progress	<u>18,513</u>	<u>3,015</u>
	428,747	413,609
Less accumulated depreciation and amortization	<u>199,550</u>	<u>181,411</u>
	<u>\$ 229,197</u>	<u>232,198</u>

Depreciation expense for the years ended December 31, 2017 and 2016 amounted to \$24,677 and \$24,252, respectively. The Company capitalized \$2,446 and \$0 of interest cost during the years ended December 31, 2017 and 2016, respectively.

(7) Other Assets

Other assets consist of the following as of December 31, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Interest in charitable remainder and perpetual trusts	\$ 3,618	3,778
Investments held for deferred compensation	<u>3,689</u>	<u>3,280</u>
	<u>\$ 7,307</u>	<u>7,058</u>

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(8) Long-Term Debt

Long-term debt as of December 31, 2017 and 2016 consisted of the following:

	2017	2016
Health Facilities Revenue Refunding Bonds, Series 2008A, variable interest, 1.75% at December 31, 2017, principal maturing in varying annual amounts commencing August 15, 2019, final maturity August 15, 2032	\$ 34,870	34,870
Health Facilities Revenue Refunding Bonds, Series 2008B, defeased in August 2017, redeemed in September 2017	—	34,960
Health Facilities Revenue Refunding Bonds, Series 2014, fixed interest, 3.01% at December 31, 2017, principal maturing in varying annual amounts commencing August 15, 2018, final maturity August 15, 2030	18,945	19,260
Health Facilities Revenue Refunding Bonds, Series 2017, fixed interest, 4.55% at December 31, 2017, principal maturing in varying annual amounts commencing November 15, 2027, final maturity November 15, 2047	95,530	—
Health Facilities Revenue Refunding Bonds, Series 2017B, fixed interest, 2.15% at December 31, 2017, principal maturing in varying annual amounts commencing August 15, 2018, final maturity August 15, 2030	26,885	—
Mortgage note payable, interest at 9.49%, principal and interest due quarterly through 2027, secured by the related property	5,355	5,676
Capital lease obligation, principal paid in varying amounts through June 2017	—	163
Capital lease obligation, 4.5% interest at December 31, 2017, principal paid in varying amounts through 2020	454	—
	182,039	94,929
Net unamortized premium on 2017 Bonds	4,992	184
Less debt issuance costs	904	—
Less current portion	5,043	4,399
Long-term debt and other obligations, net of current portion	\$ 181,084	90,714

The overall effective-interest rate on the Series 2008A, 2008B, 2014, 2017, and 2017B Bonds was 3.71% for 2017. The Series 2014 Bonds have a fixed rate of 3.01%. The Series 2017 Bonds have fixed rates with

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a minimum rate of 3.25% and a maximum rate of 5.00%. The Series 2017B Bonds have a fixed interest rate at 2.15%.

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

	<u>Long-term debt</u>	<u>Capital lease obligation</u>
Year ending December 31:		
2018	\$ 4,867	176
2019	4,832	199
2020	5,000	79
2021	5,182	—
2022	5,382	—
Thereafter	<u>156,322</u>	<u>—</u>
Total	<u>\$ 181,585</u>	<u>454</u>

On August 12, 2008, \$34,870 of Health Facilities Revenue Refunding Bonds, Series 2008A and \$65,000 of Health Facilities Revenue Refunding Bonds, Series 2008B were issued by the Hospital Authority No. 2 of Douglas County, Nebraska pursuant to the Master Trust Indenture and Loan Agreement between the Hospital and Foundation (Obligated Group) and First National Bank of Omaha, Nebraska (Master Trustee). The Series 2008 Bonds are the joint and several obligations of the Hospital and Foundation. The Series 2008B Bonds were issued at various fixed interest rates. The 2008B Bonds were defeased in August 2017 and redeemed in September 2017.

On March 1, 2017, The Hospital issued a \$95,530 tax-exempt bond through Hospital Authority No. 2 of Douglas County, Nebraska pursuant to the Master Trust Indenture and Loan Agreement between the Hospital and Foundation (Obligated Group) and First National Bank of Omaha, Nebraska (Master Trustee). Series Bonds were made up of a combination of Serial and Term bonds with a final maturity of November 15, 2047. The Series 2017 Bonds were issued at various fixed interest rates. The Hospital deposited the bond proceeds to a construction fund invested in corporate and municipal bonds. The fund is presented as assets limited as to use on the Consolidated Balance Sheets. The bond proceeds and additional funds will be used to pay for committed expenditures to improve healthcare facilities and construct the Tower Project (collectively, the Project) (note 9).

On September 2017, the Hospital issued a \$26,885 tax exempt bond Series 2017B through Hospital Authority No. 2 of Douglas County, Nebraska Health Facilities Revenue Refunding Bonds. Proceeds were used to pay the line of credit taken to redeem the Series 2008B bonds. The Series 2017B Bonds were issued at a fixed interest rate of 2.15%, and have a final maturity of August 15, 2030.

The Hospital has entered into an interest rate swap agreement with Piper Jaffray Financial Products Inc. and Morgan Stanley Capital Services, Inc. with original notional value of \$34,720. The Hospital has accounted for derivatives and hedging activities in accordance with ASC Topic 815, *Derivatives and*

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Hedging, which requires that the derivatives be recorded at fair value in the consolidated financial statements and the change in the derivative's fair value is recognized currently in earnings unless specific hedge accounting criteria are met. The Hospital has not met the requirements for hedge accounting, and accordingly, the change in the value of the swap is reflected in other income in the consolidated statements of operations.

The amount and terms of the swap agreements are as follows:

Series	Outstanding amount of swap	Interest rate
2008A	\$ 28,220	3.655 %

The following items related to the interest rate swap are included in the consolidated financial statements:

	2017	2016
Statements of operations:		
Swap interest – operating expenses	\$ 843	1,009
Change in fair value of swap transaction	690	883
Balance sheets:		
Interest rate swap – other liabilities	\$ 4,363	5,053
Accrued interest payable – current liabilities	60	77

(9) Commitments

The Company is in the process of constructing the Tower Project with an estimated total cost of \$385,000 and expected completion date of June 2021. Total construction costs included in the accompanying consolidated balance sheets as of December 31, 2017 and 2016 is \$14,254 and \$897, respectively. The Tower Project will be funded through the use of bond proceeds, existing investments, and future obligations.

(10) Operating Leases

The Company leases two floors in the north tower of the Nebraska Methodist Hospital facility. The lease includes helistop and parking access. The initial term of the lease expires May 31, 2021 and requires the Company to pay both a shell and a facility services lease rate.

The Company also leases various equipment and other building spaces for operations under various noncancelable operating lease arrangements that expire between January 2018 and December 2027 and require varying minimum annual rentals. Several of the building leases also require the payment of property taxes and normal maintenance on the properties.

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The total minimum rental and facility services commitments at December 31, 2017 are as follows:

	Building and equipment rental commitments	Facility services commitments
2018	\$ 4,734	1,036
2019	3,184	1,045
2020	2,825	1,055
2021	1,622	1,064
2022	624	447
Due thereafter	1,426	—

Total rental expense included in the accompanying consolidated statements of operations for the years ended December 31, 2017 and 2016 is \$6,349 and \$6,335, respectively.

(11) Temporarily and Permanently Restricted Net Assets

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

	2017	2016
Changing Lives Together Capital Campaign	\$ 30,639	21,463
Carolyn Scott Rainbow House	884	1,937
Specialty Pediatric Center	254	250
Charitable Remainder Trust	2,784	3,022
Dr. C.C. & Mabel L. Criss Heart Center	1,572	1,529
Other	1,739	1,876
Total	<u>\$ 37,872</u>	<u>30,077</u>

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Permanently restricted net assets include endowment funds, which are to be held in perpetuity, and perpetual trusts. The income is expendable for the identified activity:

	2017	2016
Changing Lives Together Capital Campaign	\$ 493	265
Carolyn Scott Rainbow House	1,023	1,023
William Fleming Endowed Chair in Cardiothoracic Surgery	640	640
Barbara W. and Ronald W. Shafer Endowed Chair in Orthopedics	1,009	1,009
Other	2,802	2,718
	\$ 5,967	5,655

Realized and unrealized gains and losses on investment transactions related to restricted investments are included in temporarily restricted net assets and released from restrictions in accordance with the Foundation's spending policy and donor stipulation. Change in value of split-interest agreements is reflected in the appropriate net asset classifications.

(12) Professional Liability Insurance

The Company carries a professional liability policy that provides \$1,000 of coverage for injuries per claim and \$3,000 aggregate, with a deductible of \$25 per claim and \$125 aggregate. This policy expires on August 1, 2018. Claims made prior to such date were insured. The Company also carries a physician professional liability policy that provides \$1,000 of coverage for injuries per claim and \$3,000 aggregate, with a deductible of \$10 per claim and no aggregate. In addition, the Company carries an umbrella excess liability policy (hospital professional and physician professional) that also provides \$25,000 per claim and aggregate coverage. These policies provide coverage on a claims-made basis, covering incidents that occurred subsequent to the retroactive date stated in the policy and first reported to the insurance company while the coverage is in force. In the event the Company should elect not to purchase insurance from the present carrier and fails to purchase the appropriate extended reporting endorsement, any unreported claims that occurred during the policy year may not be recoverable from the carrier.

The Company has provided for claims, including estimates of the ultimate costs of both reported claims and claims incurred but not reported at year-end. Management is presently not aware of any unasserted general and professional liability claims that would have a material adverse impact on the accompanying consolidated financial statements.

(13) Workers' Compensation Agreement

The Company has established a self-insured workers' compensation program that provides coverage for workers' compensation claims for the Company. An aggregate retention policy is provided through a commercial insurance company, which provides coverage up to the state of Nebraska's statutory requirements and the employer's liability up to \$1,000. The responsibility for the initial \$450 on each claim

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resides with the Company, subject to an aggregate retention limit of \$3,634. The Company has provided for claim payments, including estimates of the ultimate costs for both reported claims and claims incurred but not reported at year-end.

(14) Transactions with Affiliates

As discussed in note 1, Creighton University has a noncontrolling interest in Children's Physicians. For financial reporting purposes, the assets, liabilities, and operations of Children's Physicians are consolidated in the accompanying consolidated financial statements. Creighton University's 33% interest in Children's Physicians is reported as a noncontrolling interest in net assets on the consolidated balance sheets and the income or loss therefrom is included in other operating revenue in the consolidated statements of operations and changes in net assets. The noncontrolling interest related to excess of revenue over expenses was \$(614) and \$41 for the years ended December 31, 2017 and 2016, respectively.

The following is a summary of transactions between Creighton University and Children's Physicians, related to market rates or costs incurred, as reflected in the accompanying consolidated financial statements at December 31:

	2017	2016
Consolidated balance sheets:		
Payable for operating, overhead, and physician labor costs	\$ 1,385	1,247
Consolidated statements of operations:		
Operating and overhead expenses	\$ 150	264
Physician labor costs	5,318	5,481

As described in note 1, the Hospital and the Board of Regents of the University of Nebraska, acting on behalf of UNMC, entered into a members' agreement, on June 30, 2008, as the only members of NPP. Under the terms of this agreement, the Hospital is responsible for funding any annual operating deficit incurred as a result of NPP operations.

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The following is a summary of transactions between NPP, UNMC, and the Company, related to market rates or costs incurred, as reflected in the accompanying consolidated financial statements:

	2017	2016
Consolidated balance sheets:		
Receivable for billing fees, clinical support, and occupancy	\$ 3,063	8,370
Prepaid tax levy reserve	8,054	6,204
Payable for operating loss shortfall, net	(2,190)	(3,067)
	\$ 8,927	11,507
Consolidated statements of operations:		
Support for billing fees, clinical support, and occupancy	\$ (26,231)	(24,462)
Practice support costs	40,386	36,733
	\$ 14,155	12,271

(15) Defined-Contribution Plan

The Hospital and Children's Physicians offer defined-contribution retirement plans covering substantially all of their employees. Contributions and related retirement plan expense totaled \$9,759 and \$8,490 for the years ended December 31, 2017 and 2016, respectively. The Hospital's contributions include a payroll match and a basic year-end contribution, as defined by the Plan. Children's Physician's contributions included a payroll match and a year-end discretionary contribution, as defined by the Plan. The Children's Physician's plan was terminated at the end of 2017 and participants were made eligible for the Hospital plan.

(16) Concentrations of Credit Risk

The Company grants credits without collateral to its patients, most of whom are local residents of Nebraska and western Iowa and are insured under third-party payor agreements. The mix of gross patient receivables from patients and third-party payors at December 31, 2017 and 2016 are as follows:

	2017	2016
Medicaid	49 %	46 %
Commercial insurance and other third-party payors	43	42
Patients	8	12
	100 %	100 %

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December 31, 2017 and 2016

(Dollars in thousands)

(17) Commitments and Contingencies

(a) Laws and Regulations

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursements for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government healthcare programs, together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Management believes that the Company is in compliance with government laws and regulations as they apply to the areas of fraud and abuse. While no regulatory inquiries have been made that are expected to have a material effect on the Company's consolidated financial statements, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

(b) Line of Credit

The Company has entered into an unsecured revolving line of credit in the amount of \$10,000. At December 31, 2017 or 2016, the Company had not borrowed on this line.

(18) Functional Expenses

The Company provides general healthcare and other services to residents within its geographical location. Expenses included in the accompanying consolidated statements of operations as they relate to provision of these services are as follows:

	<u>2017</u>	<u>2016</u>
Health care services	\$ 344,644	318,692
Fundraising	2,997	2,958
General and administrative	46,268	44,197
	<u>\$ 393,909</u>	<u>365,848</u>

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(19) Fair Value Measurements

ASC Topic 820, *Fair Value Measurements*, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives this highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest-level input that is significant to the fair value measurement in its entirety. The following tables present assets and liabilities that are measured at fair value on a recurring basis (including items that are required to be measured at fair value and items for which the fair value option has been elected) at December 31, 2017 and 2016:

Fair value measurements at December 31, 2017				
	Level 1	Level 2	Level 3	Total
Financial assets:				
Money market funds	\$ 78,872	—	—	78,872
Repurchase agreements	517	—	—	517
Fixed income securities	—	267,085	—	267,085
Domestic mutual funds	62,794	—	—	62,794
International mutual funds	53,105	—	—	53,105
Domestic – individual stocks	28,879	—	—	28,879
Deferred compensation assets				
Money market funds	224	—	—	224
Domestic equity funds	2,708	—	—	2,708
International equity funds	249	—	—	249
Fixed income funds	509	—	—	509
Investments measured at net asset value ¹	—	—	—	63,552
	\$ 227,857	267,085	—	558,494
Financial liabilities:				
Interest rate swap	\$ —	4,363	—	4,363
Deferred compensation	3,690	—	—	3,690
Total	\$ 3,690	4,363	—	8,053

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Fair value measurements at December 31, 2016					
		Level 1	Level 2	Level 3	Total
Financial assets:					
Money market funds	\$	62,168	—	—	62,168
Repurchase agreements		516	—	—	516
Fixed income securities		—	96,212	—	96,212
Domestic mutual funds		63,940	—	—	63,940
International mutual funds		50,328	—	—	50,328
Domestic – individual stocks		29,726	—	—	29,726
International – individual stocks		483	—	—	483
Deferred compensation assets:					
Money market funds		208	—	—	208
Domestic equity funds		2,551	—	—	2,551
International equity funds		172	—	—	172
Fixed income funds		349	—	—	349
Investments measured at net asset value ¹		—	—	—	62,206
	\$	210,441	96,212	—	368,859
Financial liabilities:					
Interest rate swap	\$	—	5,053	—	5,053
Deferred compensation		3,280	—	—	3,280
Total	\$	3,280	5,053	—	8,333

1 Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.

(20) Subsequent Events

The Company has reviewed subsequent events through May 24, 2018, the date the financial statements were issued, noting no subsequent events to disclose.

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Consolidating Balance Sheet

December 31, 2017

(Dollars in thousands)

Assets	Children's Hospital	Children's Physicians	Children's Hospital Foundation	Children's Health Network	Eliminations	Consolidated
Current assets:						
Cash and cash equivalents	\$ 50,224	11,580	6,815	—	—	68,619
Patient accounts receivable, net of allowance for doubtful accounts	68,793	2,151	—	—	—	70,944
Current portion of pledges receivable	—	—	6,881	—	—	6,881
Affiliate receivables	2,386	226	—	—	(2,612)	—
Other receivables	4,547	318	2,926	—	—	7,791
Prepaid expenses and other assets	14,889	944	8	—	—	15,841
Estimated third-party payor settlements	10,187	—	—	—	—	10,187
Total current assets	151,026	15,219	16,630	—	(2,612)	180,263
Restricted cash	—	—	5,011	—	—	5,011
Assets limited to use	91,067	—	—	—	—	91,067
Pledges receivable	—	—	11,284	—	—	11,284
Long-term investments (including restricted investments)	55,936	—	371,912	—	(10,377)	417,471
Property and equipment, net	226,315	2,841	41	—	—	229,197
Interest in Foundation	404,546	—	—	—	(404,546)	—
Other assets	6,476	—	831	—	—	7,307
Total assets	\$ 935,366	18,060	405,709	—	(417,535)	941,600

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Consolidating Balance Sheet

December 31, 2017

(Dollars in thousands)

Liabilities and Net Assets	Children's Hospital	Children's Physicians	Children's Hospital Foundation	Children's Health Network	Eliminations	Consolidated
Current liabilities:						
Current portion of long-term debt	\$ 5,043	—	—	—	—	5,043
Trade accounts payable	17,493	1,695	—	—	—	19,188
Construction payables	2,597	—	—	—	—	2,597
Affiliate payables	—	3,630	367	—	(2,612)	1,385
Accrued salaries	23,722	1,755	—	—	—	25,477
Other accrued expenses	10,852	603	541	—	—	11,996
Total current liabilities	59,707	7,683	908	—	(2,612)	65,686
Long-term debt and other obligations, net of current portion	181,084	—	—	—	—	181,084
Other liabilities	8,269	—	255	—	—	8,524
Total liabilities	249,060	7,683	1,163	—	(2,612)	255,294
Net assets:						
Unrestricted	639,008	10,377	363,492	—	(373,869)	639,008
Noncontrolling interest	3,459	—	—	—	—	3,459
Total unrestricted net assets	642,467	10,377	363,492	—	(373,869)	642,467
Temporarily restricted	37,872	—	35,087	—	(35,087)	37,872
Permanently restricted	5,967	—	5,967	—	(5,967)	5,967
Total net assets	686,306	10,377	404,546	—	(414,923)	686,306
Total liabilities and net assets	\$ 935,366	18,060	405,709	—	(417,535)	941,600

See accompanying independent auditors' report.

**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
AFFILIATES**

Consolidating Statement of Operations

Year ended December 31, 2017

(Dollars in thousands)

	Children's Hospital	Children's Physicians	Children's Hospital Foundation	Children's Health Network	Eliminations	Consolidated
Unrestricted revenue, gains, and other support:						
Net patient service revenue	\$ 375,524	42,710	—	—	—	418,234
Provision for bad debt	2,495	376	—	—	—	2,871
Net patient service revenue, less provision for bad debt	373,029	42,334	—	—	—	415,363
Contributions for use in operations	2,235	51	4,569	—	(2,286)	4,569
Other revenue	16,661	1,702	—	6	(4,818)	13,551
Equity in income of Children's Physicians	(1,841)	—	—	—	1,841	—
Equity in income of Children's Health Network	(244)	—	—	—	244	—
Total unrestricted revenue, gains, and other support	389,840	44,087	4,569	6	(5,019)	433,483
Operating expenses:						
Salaries, wages, and agency staffing	152,428	26,093	1,285	231	—	180,037
Employee benefits	35,407	4,762	279	19	—	40,467
Supplies and pharmaceuticals	44,660	8,209	31	—	—	52,900
Outside services and professional fees	35,520	4,367	1,199	—	(4,322)	36,764
Other operating expenses	26,279	2,292	3,659	—	(2,286)	29,944
Depreciation and amortization	24,259	406	12	—	—	24,677
Affiliation support	16,511	(2,357)	—	—	—	14,154
Occupancy	9,233	2,144	39	—	(496)	10,920
Interest	3,787	—	21	—	—	3,808
Loss on sale of property and equipment	226	12	—	—	—	238
Beneficial interest in Foundation	1,956	—	—	—	(1,956)	—
Total operating expenses	350,266	45,928	6,525	250	(9,060)	393,909
Operating income (loss)	39,574	(1,841)	(1,956)	(244)	4,041	39,574
Other income:						
Net investment income	178	—	41,075	—	—	41,253
Change in fair value of swap transaction	690	—	—	—	—	690
Change in beneficial interest in net assets of Foundation	41,075	—	—	—	(41,075)	—
Other nonoperating income	166	—	—	—	—	166
Total other income, net	42,109	—	41,075	—	(41,075)	42,109
Excess of revenue, gains, and other support over expenses	81,683	(1,841)	39,119	(244)	(37,034)	81,683
Other changes in unrestricted net assets:						
Net assets released from restrictions for use in operations	—	—	1,502	—	—	1,502
Net asset transfers	(11,395)	—	11,151	244	—	—
Change in beneficial interest in net assets of Foundation	12,897	—	—	—	(12,897)	—
Total other changes in unrestricted net assets	1,502	—	12,653	244	(12,897)	1,502
Increase (decrease) in unrestricted net assets	\$ 83,185	(1,841)	51,772	—	(49,931)	83,185

See accompanying independent auditors' report.

**CHILDREN'S HOSPITAL & MEDICAL CENTER AND
AFFILIATES**

Consolidating Statement of Changes in Net Assets

Year ended December 31, 2017

(Dollars in thousands)

	<u>Children's Hospital</u>	<u>Children's Physicians</u>	<u>Children's Hospital Foundation</u>	<u>Children's Health Network</u>	<u>Eliminations</u>	<u>Consolidated</u>
Unrestricted net assets:						
Excess of revenue, gains, and other support over (under) expenses	\$ 81,683	(1,841)	39,119	(244)	(37,034)	81,683
Net assets released from restricted for property and equipment	—	—	1,502	—	—	1,502
Change in beneficial interest in net assets of Foundation	12,897	—	—	—	(12,897)	—
Net asset transfers	<u>(11,395)</u>	<u>—</u>	<u>11,151</u>	<u>244</u>	<u>—</u>	<u>—</u>
Increase in unrestricted net assets	<u>83,185</u>	<u>(1,841)</u>	<u>51,772</u>	<u>—</u>	<u>(49,931)</u>	<u>83,185</u>
Temporarily restricted net assets:						
Contributions restricted by donor	—	—	9,525	—	—	9,525
Investment income	—	—	152	—	—	152
Change in beneficial interest in net assets of Foundation	8,031	—	—	—	(8,031)	—
Change in value of split-interest agreements	(236)	—	—	—	—	(236)
Net assets released from restrictions	<u>—</u>	<u>—</u>	<u>(1,646)</u>	<u>—</u>	<u>—</u>	<u>(1,646)</u>
Increase in temporarily restricted net assets	<u>7,795</u>	<u>—</u>	<u>8,031</u>	<u>—</u>	<u>(8,031)</u>	<u>7,795</u>
Permanently restricted net assets:						
Contributions restricted by donor	—	—	237	—	—	237
Change in beneficial interest in net assets of Foundation	312	—	—	—	(312)	—
Change in value of split-interest agreements	<u>—</u>	<u>—</u>	<u>75</u>	<u>—</u>	<u>—</u>	<u>75</u>
Increase in permanently restricted net assets	<u>312</u>	<u>—</u>	<u>312</u>	<u>—</u>	<u>(312)</u>	<u>312</u>
Increase in net assets	91,292	(1,841)	60,115	—	(58,274)	91,292
Net assets, beginning of year	<u>595,014</u>	<u>12,218</u>	<u>344,431</u>	<u>—</u>	<u>(356,649)</u>	<u>595,014</u>
Net assets, end of year	<u>\$ 686,306</u>	<u>10,377</u>	<u>404,546</u>	<u>—</u>	<u>(414,923)</u>	<u>686,306</u>

See accompanying independent auditors' report.