

Christiana Care Health Services, Inc.

**Financial Statements
June 30, 2018 and 2017**

Christiana Care Health Services, Inc.

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June 30, 2018 and 2017

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Report of Independent Auditors

To the Board of Directors
of Christiana Care Health Services, Inc.

We have audited the accompanying financial statements of Christiana Care Health Services, Inc. ("Health Services"), which comprise the balance sheets as of June 30, 2018 and 2017, and the related statements of operations and changes in net assets, and of cash flows for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our 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, we consider internal control relevant to Health Services' preparation and fair presentation of the 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 Health Services' 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Health Services at June 30, 2018 and 2017, and the results of its operations, changes in its net assets, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

August 22, 2018

Christiana Care Health Services, Inc.
Balance Sheets
June 30, 2018 and 2017

	2018	2017
Assets		
Current assets		
Cash and cash equivalents	\$ 109,239,932	\$ 75,572,361
Short-term investments	184,648,494	182,606,435
Patient accounts receivable, net of allowance for doubtful accounts of \$27,972,026 in 2018 and \$21,698,219 in 2017	284,783,184	239,035,873
Other current assets	<u>65,797,001</u>	<u>65,199,888</u>
Total current assets	644,468,611	562,414,557
Assets limited as to use	31,431,438	67,490,424
Long-term investments	1,625,497,705	1,443,129,466
Property and equipment, net	902,263,865	845,454,264
Other assets	<u>29,204,296</u>	<u>30,168,814</u>
Total assets	<u>\$ 3,232,865,915</u>	<u>\$ 2,948,657,525</u>
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term debt	\$ 170,670,000	\$ 176,450,000
Accounts payable	69,035,430	57,035,750
Accrued salaries and professional fees	127,167,574	124,693,904
Estimated third-party payor settlements	7,117,510	9,751,038
Other accrued expenses and current liabilities	<u>58,676,986</u>	<u>46,466,019</u>
Total current liabilities	432,667,500	414,396,711
Long-term debt, net of current portion	77,887,244	80,004,888
Pension and postretirement benefits	77,321,618	73,036,235
Self insurance liabilities	33,323,924	24,580,305
Other liabilities	<u>33,675,835</u>	<u>25,824,661</u>
Total liabilities	<u>654,876,121</u>	<u>617,842,800</u>
Net assets		
Unrestricted	2,519,198,396	2,274,581,802
Temporarily restricted	29,596,700	28,856,381
Permanently restricted	<u>29,194,698</u>	<u>27,376,542</u>
Total net assets	<u>2,577,989,794</u>	<u>2,330,814,725</u>
Total liabilities and net assets	<u>\$ 3,232,865,915</u>	<u>\$ 2,948,657,525</u>

The accompanying notes are an integral part of these financial statements.

Christiana Care Health Services, Inc.
Statements of Operations and Changes in Net Assets
Years Ended June 30, 2018 and 2017

	2018	2017
Unrestricted operating revenues and other support		
Net patient service revenue	\$ 1,929,153,407	\$ 1,824,168,759
Provision for bad debts	<u>(50,250,831)</u>	<u>(48,439,495)</u>
Net patient service revenue less provision for bad debts	1,878,902,576	1,775,729,264
Other revenue	61,696,620	54,317,303
Net assets released from restrictions	<u>3,242,083</u>	<u>2,277,789</u>
	<u>1,943,841,279</u>	<u>1,832,324,356</u>
Operating expenses		
Salaries and employee benefits	1,133,632,267	1,075,428,232
Supplies and other expenses	600,528,185	526,480,490
Interest expense	3,700,129	4,329,815
Depreciation and amortization	<u>98,345,757</u>	<u>96,131,848</u>
	<u>1,836,206,338</u>	<u>1,702,370,385</u>
Operating gain	<u>107,634,941</u>	<u>129,953,971</u>
Nonoperating revenues, gains, and losses		
Investment income, gains, and losses	142,653,187	149,546,078
Other gains, net	<u>2,130,546</u>	<u>3,322,112</u>
Total nonoperating revenues, gains, and losses	<u>144,783,733</u>	<u>152,868,190</u>
Excess of revenues over expenses	<u>\$ 252,418,674</u>	<u>\$ 282,822,161</u>

The accompanying notes are an integral part of these financial statements.

Christiana Care Health Services, Inc.
Statement of Operations and Changes in Net Assets, continued
Years Ended June 30, 2018 and 2017

	2018	2017
Unrestricted net assets		
Excess of revenues over expenses	\$ 252,418,674	\$ 282,822,161
Net assets released from restrictions used for purchase of property and equipment	829,394	3,069,331
Other changes in pension and postretirement liabilities	(8,631,474)	78,838,864
Transfer from affiliate	-	1,900,000
Increase in unrestricted net assets	<u>244,616,594</u>	<u>366,630,356</u>
Temporarily restricted net assets		
Contributions	1,617,040	6,930,339
Investment income and gains	2,538,387	2,115,364
Change in interest in net assets of the System	656,369	(2,116,056)
Net assets released from restrictions	(4,071,477)	(5,347,120)
Increase in temporarily restricted net assets	<u>740,319</u>	<u>1,582,527</u>
Permanently restricted net assets		
Contributions	1,619,765	9,565,424
Change in interest in net assets of the System	(665,256)	(8,976,455)
Change in value of assets	253,357	533,902
Investment income and gains	610,290	114,745
Increase in permanently restricted net assets	<u>1,818,156</u>	<u>1,237,616</u>
Increase in net assets	247,175,069	369,450,499
Net assets		
Beginning of year	<u>2,330,814,725</u>	<u>1,961,364,226</u>
End of year	<u>\$ 2,577,989,794</u>	<u>\$ 2,330,814,725</u>

The accompanying notes are an integral part of these financial statements.

Christiana Care Health Services, Inc.
Notes to Financial Statements
June 30, 2018 and 2017

	2018	2017
Cash flows from operating activities		
Change in net assets	\$ 247,175,069	\$ 369,450,499
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Net realized and unrealized gains on investments	(118,182,100)	(127,677,897)
Depreciation and amortization	98,345,757	96,131,848
Provision for bad debts	50,250,831	48,439,495
Transfer (from) affiliate	-	(1,900,000)
Change in interest in net assets of the System	8,887	11,092,511
Restricted contributions and investment income received	(3,795,127)	(17,601,901)
Other changes in pension and postretirement benefits	8,631,474	(78,838,864)
(Increase) decrease in		
Patient accounts receivable	(95,998,142)	(53,766,399)
Other current assets	(597,113)	(8,456,955)
Other assets	955,631	(3,233,983)
Increase (decrease) in		
Accounts payable, accrued salaries, and other accrued expenses	14,661,110	25,164,593
Estimated third-party payor settlements	(2,633,528)	(812,241)
Pension and postretirement benefits	(4,123,967)	(55,394,679)
Self insurance liabilities	8,743,619	(8,664,802)
Other liabilities	7,964,268	(12,472,090)
Net cash provided by operating activities	<u>211,406,669</u>	<u>181,459,135</u>
Cash flows from investing activities		
Purchase of property and equipment, net	(143,540,949)	(120,323,071)
Proceeds from sale of investments and assets limited as to use	848,500,359	849,444,718
Purchase of investments and assets limited as to use	(878,669,572)	(956,235,577)
Net cash (used in) investing activities	<u>(173,710,162)</u>	<u>(227,113,930)</u>
Cash flows from financing activities		
Repayment of long-term debt	(7,945,000)	(7,735,000)
Securities lending	120,937	(133,423)
Restricted contributions and investment income received	3,795,127	17,601,901
Transfer from affiliate	-	1,900,000
Net cash (used in) provided by financing activities	<u>(4,028,936)</u>	<u>11,633,478</u>
Net increase (decrease) in cash and cash equivalents	33,667,571	(34,021,316)
Cash and cash equivalents		
Beginning of year	<u>75,572,361</u>	<u>109,593,677</u>
End of year	<u>\$ 109,239,932</u>	<u>\$ 75,572,361</u>
Supplemental disclosure of cash flow information		
Cash paid for interest, net of amounts capitalized	\$ 3,777,861	\$ 4,398,372
Accrued property and equipment acquisitions	\$ 11,680,145	\$ 2,336,987

Christiana Care Health Services, Inc.

Notes to Financial Statements

June 30, 2018 and 2017

1. Description of the Organization

Christiana Care Health Services, Inc. (“Health Services”), a Delaware not-for-profit corporation, owns and operates: Christiana Hospital, Wilmington Hospital, Eugene duPont Preventive Medicine and Rehabilitation Institute, a free-standing emergency department, a physician network, residency training programs, and numerous ambulatory and physician office locations. Health Services’ primary activity is to provide healthcare services to the residents of Delaware and the surrounding counties in Maryland, Pennsylvania, and New Jersey.

Health Services is an affiliate of Christiana Care Health System, Inc. (the “System”). The System is the parent organization of Health Services, Christiana Care Health Initiatives (“Health Initiatives”), Christiana Care Home Health and Community Services, Inc. (“CCHHCS”) and Christiana Care Health Plans, Inc. (“Health Plans”).

2. Summary of Significant Accounting Policies

Basis of Accounting

Health Services’ financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America.

Basis of Presentation

Health Services reports its net assets by classifying net assets into three categories in accordance with the existence or absence of donor imposed restrictions. A description of these categories is as follows:

Permanently restricted net assets include gifts, trusts, pledges, income, and gains that are required by donor imposed restrictions to be permanently retained. Investment return derived from permanently restricted net assets may be spent for general or specific purposes in accordance to donor imposed restrictions, based on the amounts appropriated for expenditure annually by the Board of Directors.

Temporarily restricted net assets include gifts, pledges, income, and gains for which donor imposed restrictions have not yet been met. Such restrictions are purpose restrictions imposed by donors, which are normally released upon the incurrence of expenditures that fulfill those donor specified purposes.

Unrestricted net assets are neither permanently restricted nor temporarily restricted by donor imposed stipulations.

Use of Estimates

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

Christiana Care Health Services, Inc.
Notes to Financial Statements
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Net Patient Service Revenue and Patient Accounts Receivable

Health Services has agreements with third-party payors that provide for payments to Health Services at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per-diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes 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.

Health Services recognizes patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients who do not qualify for charity care (Self-Pay), Health Services recognizes revenue based on established rates, subject to certain discounts as determined by Health Services. An estimated provision for bad debts is recorded that results in net patient service revenue being reported at the net amount expected to be received. Health Services has determined that patient service revenue is primarily recorded prior to assessing the patient's ability to pay and as such, the entire provision for bad debts related to patient revenue is recorded as a deduction from patient service revenue in the accompanying statements of operations. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), for the years ended June 30, 2018 and 2017 from these two payor sources are as follows:

	2018	2017
Third-Party Payors	96.7 %	96.6 %
Self-Pay	3.3 %	3.4 %
	<u>100.0 %</u>	<u>100.0 %</u>

Revenue from the Medicare and Medicaid programs accounted for approximately 34% and 14%, respectively, of Health Services' net patient service revenue for the year ended June 30, 2018 and 34% and 15%, respectively, for the year ended June 30, 2017. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The 2018 and 2017 net patient service revenue increased \$1,346,964 and \$855,272, respectively, because of tentative settlements, final settlements, and final appeals for years that are no longer subject to audits, reviews, and investigations, as well as other changes in estimates.

Christiana Care Health Services, Inc.
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Patient accounts receivable are reduced by an allowance for doubtful accounts. The allowance for doubtful accounts is based upon management's assessment of historical and expected net collections considering historical business and economic conditions, trends in healthcare coverage, major payor sources, and other collection indicators. Periodically throughout the year, management assesses the adequacy of the allowance for doubtful accounts based upon historical write-off experience by payor category. The results of this review are then used to make modifications to the provision for bad debts to establish an appropriate allowance for doubtful accounts. No significant modifications were made to the methodology for the provision of doubtful accounts for fiscal years 2018 and 2017. After satisfaction of amounts due from insurance and reasonable efforts to collect from the patient have been exhausted Health Services follows established guidelines for placing certain past-due balances with collection agencies, subject to terms and certain restrictions on collection efforts as determined by Health Services. Accounts receivable are written off after collection efforts have been followed in accordance with Health Services' policy.

For patient accounts receivable associated with self-pay patients, which includes patients that fail to make payment for services rendered or insured patients who fail to remit co-payments and deductibles as required under the applicable health insurance arrangement, Health Services records an estimated provision for bad debts in the year of service.

Charity Care

Health Services provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because Health Services does not pursue collections of amounts determined to qualify as charity care, they are not reported as revenue.

Other Revenue

Other revenue consists of research, rental, intercompany, and other miscellaneous non-patient related revenue.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid instruments with original maturities of three months or less. At June 30, 2018 and 2017, Health Services had cash balances in financial institutions which exceed federal depository insurance limits. Management believes that the credit risk related to these deposits is minimal.

Inventories

Inventories are stated at the lower of cost (determined by the first-in, first-out method) or market (defined as net realizable value).

Christiana Care Health Services, Inc.

Notes to Financial Statements

June 30, 2018 and 2017

Investments and Assets Limited as to Use

Investments and assets limited as to use are measured at fair value in the balance sheets based on the methodology described in Note 3. Managed funds represent subscriptions in funds-of-funds utilized to diversify the portfolio of Health Services. As a practical expedient, Health Services estimates the fair value of managed funds using the reported net asset value (NAV). Health Services has assessed factors such as the managed funds' compliance with fair value reporting standards, price transparencies and valuation procedures, the ability to redeem at NAV at the measurement date, and existence of redemption restrictions at the measurement dates. Health Services is required to provide written notice of at least 90 calendar days prior to a calendar quarter-end to redeem managed funds. There are no lock-up provisions. Investment income or loss (consisting of realized and unrealized gains and losses on investments, interest, and dividends) are included in the excess of revenues over expenses unless the income or loss is restricted by donor.

Assets limited as to use include designated assets set aside by Health Services' Board of Directors ("Board"). During 2018, the Board removed the designation on assets previously set aside by the Board to support the Cancer Center. As a result of this action, these assets are classified as unrestricted long-term investments in the June 30, 2018 balance sheet. Additionally, in 2018, the Board designated \$5 million to support the Center for Translational Cancer Research (CTCR) at the Helen F. Graham Cancer Center, and these assets are classified as assets limited as to use in the June 30, 2018 balance sheet.

Investments classified as current in the balance sheets are for amounts required to meet the current portion of long-term debt.

Health Services classifies investments as trading securities. Investment income or loss generated by trading securities is classified within nonoperating revenues, gains, and losses within the statement of operations and changes in net assets. Health Services considers the activity of the investment portfolio and the associated cash receipts and cash purchases resulting from purchases and sales of investments classified as trading securities as an investing activity and classifies this activity accordingly within the statements of cash flows.

Property, Equipment, and Depreciation

Property and equipment acquisitions are recorded at cost. Expenditures which substantially increase the useful lives of existing assets are capitalized. Routine maintenance and repairs are expensed as incurred. Depreciation is computed using the straight-line method based on the following estimated useful lives: Buildings and building improvements 5-40 years, equipment 3-20 years. Gains and losses from retirement or disposition of fixed assets are recognized in the statement of operations as nonoperating activity. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted contributions at fair value as of the date of the gift, and are excluded from the excess of revenues 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.

Christiana Care Health Services, Inc.
Notes to Financial Statements
June 30, 2018 and 2017

Securities Lending

Health Services engages in securities lending whereby certain securities in its portfolio are loaned to other parties generally for a short period of time. Health Services receives collateral equal to 100% of the market value of securities borrowed. Health Services records the fair value of the collateral received as a component of both other current assets and other current liabilities as Health Services is obligated to return the collateral upon the return of the borrowed securities. Other current assets and liabilities include \$151,139 and \$30,202 of collateral investments at June 30, 2018 and 2017, respectively.

Bond Issuance Costs

Bond Issuance costs are recorded as a direct deduction from long-term debt and represent the cost of issuing long-term debt. Such costs are being amortized over the life of the applicable indebtedness using the interest method.

Interest in the System

Health Services records an interest in certain net assets of the System resulting from temporarily and permanently restricted contributions that were solicited and held by the System for the ultimate benefit of Health Services. An interest in the net assets of the System is recorded within other assets in the balance sheet. Changes in the value of the interest in the net assets of the System is recorded as a change in temporarily and permanently restricted net assets. In fiscal year 2017, Health System transferred endowments to Health Services as they supported the activities within Health Services resulting in a reduction of the interest in the System. The interest in the System as of June 30, 2018 is \$6,035,345.

Investments Held in Trust

Health Services is entitled to beneficial interests in perpetual trusts at various percentages, which are maintained by outside trustees. Health Services' share of the market value of the trusts are recorded in permanently restricted net assets. The change in value of assets is also recorded as permanently restricted. The periodic income distributions received from the trustees are recorded as increases in unrestricted or temporarily restricted net assets, based on the donors' intentions.

Excess of Revenue Over Expenses

The statement of operations includes excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets), and other changes in pension and postretirement liabilities.

Donor-Restricted Contributions

Unconditional promises to give cash and other assets to Health Services are reported at fair value at the date the promise is received. The contributions 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 statement of operations as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements.

Christiana Care Health Services, Inc.

Notes to Financial Statements

June 30, 2018 and 2017

Compensated Paid Leave

Health Services records a liability in accrued salaries and professional fees for amounts due to employees for future paid leave which are attributable to services performed in the current and prior periods.

Tax Status

Health Services is a Delaware nonprofit corporation and has been recognized as tax-exempt pursuant to Section 501(c) (3) of the Internal Revenue Code.

Subsequent Events

Health Services has performed an evaluation of subsequent events through August 22, 2018, which is the date the financial statements were considered widely distributed. There were no events that require adjustment to the audited financial statements or disclosure in the notes to the audited financial statements.

Accounting Pronouncements not yet Adopted

In May 2014, the FASB issued a standard on *Revenue from Contracts with Customers*. This standard implements a single framework for recognition of all revenue earned from customers. This framework ensures that entities appropriately reflect the consideration to which they expect to be entitled in exchange for goods and services by allocating transaction price to identified performance obligations and recognizing revenue as performance obligations are satisfied. Qualitative and quantitative disclosures are required to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The standard is effective for fiscal year 2019, and Health Services is evaluating the impact this will have on its financial statements.

In February 2016, the FASB issued a standard on *Leases*. This standard requires lessees to recognize assets and liabilities for the rights and obligations created by leases with terms in excess of 12 months. The recognition, measurement, and presentation of expenses and cash flows arising from a lease will primarily depend on its classification as a finance or operating lease. The accounting by lessors remains largely unchanged. This standard is effective for fiscal years beginning after December 15, 2018 (fiscal year 2020 for Health Services). Health Services is evaluating the impact this will have on its financial statements.

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*. This standard intends to make certain improvements to the current reporting requirements for not-for-profit entities. This standard sets forth changes to net asset classification requirements and the information presented about a non-for-profit entity's liquidity, financial performance, and cash flows. ASU 2016-14 is effective for the Health Services for annual reporting periods beginning after December 15, 2017. Health Services is currently evaluating the impact that ASU 2016-14 will have on its consolidated financial statements and will adopt the provisions upon the effective date.

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In March 2017, the FASB issued a standard on *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. Presently, net benefit cost is reported as an employee cost within excess of revenue over expenses from operations (or capitalized into assets when appropriate). This standard requires the bifurcation of net benefit cost, as follows: service cost will continue to be reported in employee benefits, while the remaining components of net benefit cost will be reported in nonoperating revenue, gains, and losses. This standard is effective for fiscal years beginning after December 15, 2018 or fiscal year 2020 for Health Services, and early adoption is permitted. Health Services has elected to adopt this new standard beginning on July 1, 2018. There is no impact to the excess of revenues over expenses.

In June 2018, the FASB issued a standard on *Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made*. The new guidance shifts the accounting for revenue recognition for most federal grants from an exchange model to the contribution accounting model. The new guidance provides an enhanced framework for determining whether a contribution is conditional or unconditional, which is important for the timing of revenue recognition. The standard is effective for fiscal year 2019, and Health Services is evaluating the impact this will have on its financial statements. At this time, Health Services does not expect the timing of revenue recognition to change significantly as a result because most federal grants are awarded on a cost reimbursement basis, where revenue is triggered by incurring reimbursable costs.

Reclassifications

Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation.

3. Investments, Assets Limited as to Use, and Investment Income

The composition of investments and assets limited as to use at June 30, 2018 and 2017 is set forth in the following table. Investments and assets limited to use are stated at fair value.

	2018	2017
Short-term investments	<u>\$ 184,648,494</u>	<u>\$ 182,606,435</u>
Assets limited as to use		
Internally designated by Board of Directors		
Infant mortality	14,537,698	14,836,765
Harrington VIP/VICP fund	11,648,345	12,182,714
Translational Cancer Research	5,245,395	-
Cancer program	-	40,470,945
Total assets limited as to use	<u>31,431,438</u>	<u>67,490,424</u>
Long-term investments		
Unrestricted	1,572,828,480	1,392,934,223
Temporarily restricted	23,755,578	23,673,956
Permanently restricted	28,913,647	26,521,287
Total long-term investments	<u>1,625,497,705</u>	<u>1,443,129,466</u>
Total investments and assets limited as to use	<u>\$ 1,841,577,637</u>	<u>\$ 1,693,226,325</u>

Christiana Care Health Services, Inc.
Notes to Financial Statements
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Within the statement of operations, investment income is comprised of the following:

	Year Ended June 30,	
	2018	2017
Interest and dividend income	\$ 27,467,614	\$ 21,868,181
Net realized gains	26,815,554	41,404,735
Change in net unrealized gains	88,370,019	86,273,162
	<u>\$ 142,653,187</u>	<u>149,546,078</u>

Investment income is net of investment fees of \$5,210,638 and \$4,085,405 in 2018 and 2017, respectively.

The unrealized gains and losses in temporary and permanently restricted investments are \$2,168,491 and \$1,133,676 in 2018 and 2017, respectively. The realized gains and losses in temporary and permanently restricted investments are \$574,680 and \$575,141 in 2018 and 2017, respectively.

Health Services adheres to applicable accounting guidance for fair value measurements and defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

Health Services applies the following fair value hierarchy:

- Level 1 Quoted prices in active markets for identical assets or liabilities. Level 1 assets include money market funds, debt and equity securities that are traded in an active exchange market, as well as certain U.S. Treasury and other U.S. Governments and agency securities that are highly liquid and are actively traded in over-the-counter markets.
- Level 2 Observable inputs other than Level 1 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 same term of the assets or liabilities. Level 2 assets include equity and debt securities with quoted prices that are traded less frequently than exchange-traded instruments whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.
- 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. Level 3 assets include investments held in trust by others whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

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Transfers between leveled assets are based on the actual date of the event which caused the transfer. As of June 30, 2018 and 2017 there were no transfers between Level 1, 2, and 3. The following table presents the financial instruments carried at fair value as of June 30, 2018 in accordance with the fair value hierarchy:

	Level 1	Level 2	Level 3	Total
Investments and assets limited as to use				
Money market funds	\$238,358,406	\$ -	\$ -	\$ 238,358,406
U.S. Government and agency securities	115,276,954	-	-	115,276,954
Corporate and other debt securities	-	464,224,546	-	464,224,546
Equity securities	606,428,857	371,156,679	-	977,585,536
Investments held in trust by others	-	-	8,497,095	8,497,095
Total investments and assets limited as to use	<u>960,064,217</u>	<u>835,381,225</u>	<u>8,497,095</u>	<u>1,803,942,537</u>
Total assets at fair value	<u>\$960,064,217</u>	<u>\$835,381,225</u>	<u>\$8,497,095</u>	<u>\$1,803,942,537</u>
Equity managed funds measured at net asset value				<u>37,635,100</u>
Total assets at fair value				<u>\$1,841,577,637</u>

The following table illustrates the change in Level 3 assets:

	Investments Held by Others
Fair value June 30, 2017	\$ 7,821,873
Contribution	421,865
Change in value of assets	<u>253,357</u>
Fair value June 30, 2018	<u>\$ 8,497,095</u>

The following table presents the financial instruments carried at fair value as of June 30, 2017 in accordance with the fair value hierarchy:

	Level 1	Level 2	Level 3	Total
Investments and assets limited as to use				
Money market funds	\$ 232,734,577	\$ -	\$ -	\$ 232,734,577
U.S. Government and agency securities	90,521,377	6,196,247	-	96,717,624
Corporate and other debt securities	-	449,896,883	-	449,896,883
Equity securities	507,106,277	265,453,469	-	772,559,746
Investments held in trust by others	-	-	7,821,873	7,821,873
Total investments and assets limited as to use	<u>830,362,231</u>	<u>721,546,599</u>	<u>7,821,873</u>	<u>1,559,730,703</u>
Total assets at fair value	<u>\$ 830,362,231</u>	<u>\$ 721,546,599</u>	<u>\$ 7,821,873</u>	<u>\$ 1,559,730,703</u>
Equity managed funds measured at net asset value				<u>133,495,622</u>
Total assets at fair value				<u>\$ 1,693,226,325</u>

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The following table illustrates the change in Level 3 assets:

	Investments Held by Others
Fair value June 30, 2016	\$ 7,287,971
Change in value of assets	<u>533,902</u>
Fair value June 30, 2017	<u>\$ 7,821,873</u>

4. Property and Equipment

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

	2018	2017
Land and land improvements	\$ 69,016,752	\$ 68,630,387
Buildings and building improvements	1,191,321,509	1,148,953,021
Equipment	<u>689,498,716</u>	<u>647,090,684</u>
	1,949,836,977	1,864,674,092
Accumulated depreciation	<u>(1,183,800,072)</u>	<u>(1,087,989,005)</u>
	766,036,905	776,685,087
Construction-in-progress	<u>136,226,960</u>	<u>68,769,177</u>
	<u>\$ 902,263,865</u>	<u>\$ 845,454,264</u>

Included within buildings and building improvements are leasehold improvement costs of \$6,537,783 and \$6,474,325 in 2018 and 2017, respectively. Depreciation expense amounted to \$98,411,492 and \$96,083,213 in 2018 and 2017, respectively. In 2018 and 2017, Health Services incurred total interest costs of \$5,678,414 and \$5,142,084, respectively, of which \$2,091,376 in 2018 and \$812,269 in 2017 has been capitalized. At June 30, 2018 construction contracts of \$223,819,929 exist primarily for various expansion and other facility improvements. The remaining commitment on these contracts was \$141,776,269.

5. Other Current Assets and Other Assets

Other Current Assets at June 30, 2018 and 2017 consist of the following:

	2018	2017
Inventories	\$ 27,443,400	\$ 23,441,424
Prepaid expenses	17,016,122	22,819,553
Other	<u>21,337,479</u>	<u>18,938,911</u>
	<u>\$ 65,797,001</u>	<u>\$ 65,199,888</u>

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Other Assets at June 30, 2018 and 2017 consist of the following:

	2018	2017
Interest in the System	\$ 6,035,345	\$ 6,044,232
Goodwill	1,015,805	1,015,805
Other receivables	15,804,982	13,869,263
Other	6,348,164	9,239,514
	<u>\$ 29,204,296</u>	<u>\$ 30,168,814</u>

6. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at June 30, 2018 and 2017:

	2018	2017
Health care services	\$ 3,378,955	\$ 3,420,274
Purchases of buildings and equipment	10,851,152	7,727,899
Education, research, and other operational needs	15,366,593	17,708,208
	<u>\$ 29,596,700</u>	<u>\$ 28,856,381</u>

Permanently restricted net assets consist of the following at June 30, 2018 and 2017:

	2018	2017
Investments held in perpetuity	\$ 20,697,603	\$ 19,554,669
Investments held in trust by others	8,497,095	7,821,873
	<u>\$ 29,194,698</u>	<u>\$ 27,376,542</u>

7. Endowments

Health Services' endowment consists of twenty-two individual donor restricted endowment funds and three board-designated endowment funds for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. The net assets associated with endowment funds including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor imposed restrictions. In accordance with Health Services' endowment spending policy, annual distributions are 5% of the fiscal year-end value of the endowment pool calculated on a 36-month trailing average of the market value.

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Health Services has interpreted the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”) as requiring the preservation of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Health Services classifies as permanently restricted net assets, (a) the original value of 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 on an annual basis by the Board of Directors of Health Services in a manner consistent with the standard of prudence prescribed by UPMIFA.

Endowment net asset composition by type of fund as of June 30, 2018 and 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	2018			
Endowment funds				
Donor-restricted	\$ -	\$ 17,193,094	\$ 20,507,603	\$ 37,700,697
Board-designated	<u>31,431,438</u>	<u>-</u>	<u>-</u>	<u>31,431,438</u>
Total endowment funds	<u>\$ 31,431,438</u>	<u>\$ 17,193,094</u>	<u>\$ 20,507,603</u>	<u>\$ 69,132,135</u>

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	2017			
Endowment funds				
Donor-restricted	\$ -	\$ 16,547,193	\$ 18,699,413	\$ 35,246,606
Board-designated	<u>67,490,424</u>	<u>-</u>	<u>-</u>	<u>67,490,424</u>
Total endowment funds	<u>\$ 67,490,424</u>	<u>\$ 16,547,193</u>	<u>\$ 18,699,413</u>	<u>\$ 102,737,030</u>

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Changes in endowment net assets for the year ended June 30, 2018 and 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, June 30, 2017	\$ 67,490,424	\$ 16,547,193	\$ 18,699,413	\$ 102,737,030
Investment income	4,028,872	2,538,387	610,290	7,177,549
Contributions	-	-	1,197,900	1,197,900
Removal of board-designation	(39,129,436)	-	-	(39,129,436)
Appropriation of endowment assets for expenditure	(958,422)	(1,892,486)	-	(2,850,908)
Endowment net assets, June 30, 2018	<u>\$ 31,431,438</u>	<u>\$ 17,193,094</u>	<u>\$ 20,507,603</u>	<u>\$ 69,132,135</u>

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, June 30, 2016	\$ 64,037,334	\$ 11,828,040	\$ 9,019,244	\$ 84,884,618
Investment income	4,366,968	2,115,364	114,745	6,597,077
Contributions	-	1,878,212	9,565,424	11,443,636
Transfer to endowment	-	1,114,429	-	1,114,429
Appropriation of endowment assets for expenditure	(913,878)	(388,852)	-	(1,302,730)
Endowment net assets, June 30, 2017	<u>\$ 67,490,424</u>	<u>\$ 16,547,193</u>	<u>\$ 18,699,413</u>	<u>\$ 102,737,030</u>

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

	2018	2017
Temporarily restricted net assets		
Restricted for health care services	\$ 3,206,507	\$ 3,193,614
Restricted for purchases of building and maintenance	7,223,183	7,234,757
Restricted for education, research, and other operational needs	6,763,404	6,118,822
Total temporarily restricted net assets	<u>\$ 17,193,094</u>	<u>\$ 16,547,193</u>
Permanently restricted net assets		
Restricted for salary support	\$ 11,197,414	\$ 9,797,123
Restricted for education, research, and other operational needs	9,310,189	8,902,290
Total permanently restricted net assets	<u>\$ 20,507,603</u>	<u>\$ 18,699,413</u>

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Endowment Funds with Deficits

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts (deficit). When donor-restricted endowment deficits exist, they are classified as a reduction of unrestricted net assets. There were no deficits of this nature reported in unrestricted net assets as of June 30, 2018 and June 30, 2017.

Strategies Employed for Achieving Investment Objectives

To achieve its long-term rate of return objectives, Health Services relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends). Health Services targets a diversified asset allocation that places greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

8. Debt

Health Services debt at June 30, 2018 and 2017 consisted of the following:

	Interest Rates	Final Maturity	2018	2017
Series 2010 Revenue Bonds				
2010A	4.00% to 5.00%	2040	\$ 57,640,000	\$ 57,640,000
2010B	variable	2040	69,925,000	72,490,000
2010C	variable	2040	23,305,000	24,165,000
2010D	2.44%	2020	6,350,000	8,365,000
2010E	3.01%	2025	16,660,000	16,760,000
Series 2008 Revenue Bonds				
2008A	variable	2038	51,735,000	53,395,000
2008B	variable	2038	<u>23,540,000</u>	<u>24,285,000</u>
			249,155,000	257,100,000
Unamortized premium			794,962	860,697
Debt issuance costs			(1,392,718)	(1,505,809)
Current maturities			(2,165,000)	(2,115,000)
Long-term variable rate debt classified as current			<u>(168,505,000)</u>	<u>(174,335,000)</u>
			<u>\$ 77,887,244</u>	<u>\$ 80,004,888</u>

In 2010, Health Services issued \$73,000,000 aggregate principal amount of Series 2010A fixed rate revenue bonds, \$75,000,000 aggregate principal amount of Series 2010B variable rate revenue bonds, \$25,000,000 aggregate principal amount of Series 2010C variable rate revenue bonds, \$10,335,000 aggregate principal amount of Series 2010D fixed rate revenue bonds, and \$16,860,000 aggregate principal amount of Series 2010E fixed rate revenue bonds through the Delaware Health Facilities Authority (DHFA). The proceeds were used to fund various capital projects and capital expenditures.

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The 2010B Bonds and 2010C Bonds bear interest at a variable rate as determined by a remarketing agent, reset on a weekly and monthly basis, respectively. At the time of the bond issuance, interest was assumed at a rate of 2.71% annually for both the 2010B Bonds and the 2010C Bonds. During 2018 and 2017, respectively, interest rates ranged from 0.76% to 1.85% and 0.38% to 0.95% for the 2010B bonds and from 0.85% to 1.72% and 0.44% to 0.95% for the 2010C Bonds.

In 2008, Health Services issued \$55,000,000 aggregate principal of Series 2008A variable rate revenue bonds and \$25,000,000 aggregate principal of Series 2008B variable rate revenue bonds through the DHFA. The proceeds were used for the repayment of a short term loan and to acquire land. The Series 2008A Bonds bear interest at a variable rate, as determined by a remarketing agent, reset on a daily basis. The Series 2008B Bonds bear interest at a variable rate, as determined by a remarketing agent, reset on a weekly basis. At the time of the bond issuance, interest was assumed at a rate of 3.50% annually for both the 2008A Bonds and the 2008B bonds. During 2018 and 2017, respectively, the rates for the Series 2008 Bonds ranged from 0.58% to 1.93% and 0.27% to 0.97%.

Health Services is obligated to purchase any Series 2010B Bonds, Series 2010C Bonds, and Series 2008 Bonds not remarketed. The Series 2010B Bonds, Series 2010C Bonds, and Series 2008 Bonds are classified as a current liability on the June 30, 2018 and June 30, 2017 balance sheets. In the event the Series 2010B Bonds, Series 2010C Bonds, and Series 2008 Bonds are not remarketed, Health Services would use available cash and investments to meet the obligations. Assuming the remarketing of the Series 2010B Bonds, Series 2010C Bonds and Series 2008 Bonds, scheduled maturities are as follows:

2019	\$ 8,150,000
2020	8,360,000
2021	8,580,000
2022	8,805,000
2023	9,050,000
Thereafter	<u>206,210,000</u>
	<u>\$ 249,155,000</u>

9. Interest Rate Swap Agreement

In conjunction with the issuance of the Series 2008 Bonds, Health Services entered into an interest rate swap agreement for a notional amount of \$25,000,000 with a financial institution to reduce Health Services' overall interest expense. Under the interest rate swap agreement, Health Services receives payments from the financial institution in the amount of 67% of one month LIBOR. In exchange, Health Services will pay the financial institution a fixed rate. The fair value of the interest rate swap represented a liability of \$1,012,012 and \$2,064,941 at June 30, 2018 and 2017, respectively, recorded within other liabilities. The change in the fair value of the interest rate swap of \$1,052,929 is recorded as a component of other gains, net within the statements of operations.

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10. Commitments and Contingencies

Leases

Health Services has various leases for office facilities and other equipment under cancelable and noncancelable operating leases, with initial terms in excess of one year, and a capital lease. Total related lease expense amounted to \$11,379,653 and \$10,943,600 in 2018 and 2017, respectively.

Future minimum lease payments under the capital lease and noncancelable operating leases are as follows:

	<u>Capital</u>	<u>Operating</u>
2019	\$ 1,374,220	\$ 9,046,010
2020	1,403,077	5,037,371
2021	1,433,216	3,937,988
2022	1,463,997	2,979,665
2023	1,495,418	2,523,933
Thereafter	1,528,123	1,879,962

Litigation

Health Services is a defendant in several matters of litigation, all in the ordinary course of conducting business. Management believes the ultimate outcome of these matters will not have a material effect on Health Services' financial position or results of operations.

Commitments

In fiscal 2017, Health Services entered a seven-year agreement with a vendor to provide healthcare IT software and solutions. Payments under this commitment will total \$163,674,466. At June 30, 2018, the remaining commitment is \$131,391,468, of which \$23,837,042 will be paid in fiscal 2019.

11. Employee Benefit Plans

Pension Plans

Health Services sponsors a noncontributory defined benefit pension plan covering substantially all eligible employees hired on or before August 13, 2006. Employees hired after that date are participants in a defined contribution plan. Contributions to the pension plan are based on the minimum amount required by the Employee Retirement Income Security Act of 1974.

Retirement benefits are paid based principally on years of service and salary. Pension plan assets consist primarily of corporate bonds, notes, U.S. government obligations, and common stocks.

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Postretirement Benefits

Health Services provides postretirement health care benefits to eligible employees and their dependents. The following table sets forth the components of the benefit obligations, plan assets, and funding status of the plan based on actuarial valuations performed as of June 30, 2018 and June 30, 2017:

	Pension Benefits		Postretirement Benefits	
	2018	2017	2018	2017
Change in benefit obligation				
Benefit obligation at beginning of year	\$ 882,968,089	\$ 959,323,114	\$ 76,834,173	\$ 85,327,331
Service cost	30,212,493	34,591,994	1,229,544	1,443,777
Interest cost	31,056,222	30,349,515	2,716,401	2,706,488
Actuarial (gain)	(34,578,994)	(78,844,755)	(3,528,723)	(9,031,547)
Retiree contributions	-	-	456,101	332,118
Benefits paid	(60,813,902)	(62,451,779)	(3,317,904)	(3,943,994)
Benefit obligation at end of year	<u>\$ 848,843,908</u>	<u>\$ 882,968,089</u>	<u>\$ 74,389,592</u>	<u>\$ 76,834,173</u>
Change in Plan assets				
Fair value of Plan assets at beginning of year	\$ 885,413,440	\$ 833,582,730	\$ -	\$ -
Actual return on Plan assets (net of expenses)	(14,207,718)	21,482,489	-	-
Employer contributions	31,500,000	92,800,000	2,861,803	3,611,876
Retiree contributions	-	-	456,101	332,118
Benefits paid	(60,813,902)	(62,451,779)	(3,317,904)	(3,943,994)
Fair value of Plan assets at end of year	<u>\$ 841,891,820</u>	<u>\$ 885,413,440</u>	<u>\$ -</u>	<u>\$ -</u>
Reconciliation of funded status to net amount recognized in the balance sheet				
Amounts recorded as accrued liabilities				
Funded status	(6,952,088)	\$ 2,445,351	\$ (74,389,592)	\$ (76,834,173)
Noncurrent Asset	-	2,445,351	-	-
Current liabilities	-	-	(4,020,061)	(3,797,937)
Noncurrent liabilities	(6,952,088)	-	(70,369,531)	(73,036,236)
Accrued liability	(6,952,088)	-	(74,389,592)	(76,834,173)
Amounts recorded within unrestricted net assets				
Unrecognized prior service (credit)	-	-	(23,026,134)	(29,056,496)
Unassigned actuarial loss	162,353,110	155,419,504	8,720,113	13,052,607
Net amount recognized at year end	<u>\$ 155,401,022</u>	<u>\$ 157,864,855</u>	<u>\$ (88,695,613)</u>	<u>\$ (92,838,062)</u>
Accumulated benefit obligation	<u>\$ 734,739,342</u>	<u>\$ 758,953,577</u>	<u>\$ -</u>	<u>\$ -</u>

	Pension Benefits		Postretirement Benefits	
	2018	2017	2018	2017
Weighted-average assumptions used to determine benefit obligations at June 30				
Discount rate	4.000 %	3.625 %	4.000 %	3.625 %
Rate of compensation increase	3.000 %	3.000 %		

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	Pension Benefits		Postretirement Benefits	
	2018	2017	2018	2017
Components of net periodic benefit cost				
Service cost	\$ 30,212,493	\$ 34,591,994	\$ 1,229,544	\$ 1,443,777
Interest cost	31,056,222	30,349,515	2,716,401	2,706,488
Expected return on plan assets	(35,862,938)	(44,197,103)	-	-
Amortization of prior service (credit)	-	-	(6,030,362)	(6,144,095)
Recognized actuarial loss	8,558,056	17,614,199	803,771	2,207,072
Net periodic benefit cost	<u>33,963,833</u>	<u>38,358,605</u>	<u>(1,280,646)</u>	<u>213,242</u>
Other changes in pension liability recognized in unrestricted net assets				
Net actuarial loss (gain)	15,491,662	(56,130,141)	(3,528,723)	(9,031,547)
Amortization of (gain)	(8,558,056)	(17,614,199)	(803,771)	(2,207,072)
Amortization of prior service credit	-	-	6,030,362	6,144,095
Total recognized in unrestricted net assets	<u>6,933,606</u>	<u>(73,744,340)</u>	<u>1,697,868</u>	<u>(5,094,524)</u>
Total recognized in net benefit cost and unrestricted net assets	<u>\$ 40,897,439</u>	<u>\$ (35,385,735)</u>	<u>\$ 417,222</u>	<u>\$ (4,881,282)</u>

	Pension Benefits		Postretirement Benefits	
	2018	2017	2018	2017
Weighted-average assumptions used to determine net periodic benefit cost at beginning of fiscal year				
Discount rate	3.625 %	3.250 %	3.625 %	3.250 %
Expected return on plan assets	4.250 %	5.750 %	-	-
Rate of compensation increase	3.000 %	3.000 %	-	-

Health Services expects to recognize \$5,400,194 of loss amortization, no prior service cost amortization and no amortization of transition asset or obligation as components of net pension cost during the year ending June 30, 2019, and expects to recognize \$198,321 of loss amortization, \$(5,996,389) of prior service (credit) amortization and no amortization of transition asset or obligation as components of net postretirement benefit cost during the year ending June 30, 2019.

The expected rate of return on plan assets assumption was developed based on historical returns for the major asset classes. This review also considered both current market conditions and projected future contributions.

Health Services utilizes published long-term high quality corporate bond indices to determine the discount rate at measurement date. Where commonly available, Health Services considers indices of various durations to reflect the timing of future benefit payments.

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Plan Assets

Pension plan weighted target and actual average asset allocations at June 30, 2018 and June 30, 2017 by asset category are as follows:

Asset Category	2018	2017
Fixed income	100 %	100 %
	<u>100 %</u>	<u>100 %</u>

The investment policy incorporates a liability-driven investment approach that focuses on the funded status of the Plan and seeks to match the duration of the assets with that of the liabilities. As such, the investment portfolio allocation is comprised of 100% long duration fixed income securities. The Plan's financial condition is monitored on an ongoing basis by means of an annual funding review, an annual independent actuarial valuation, and quarterly investment portfolio reviews.

The following table represents the Plan's financial instruments as of June 30, 2018, measured at fair value on a recurring basis using the fair value hierarchy defined in Note 3:

	Level 1	Level 2	Level 3	Total
Money market funds	\$ 22,690,992	\$ -	\$ -	\$ 22,690,992
U.S. Government and agency securities	196,010,677	21,575,554	-	217,586,231
Corporate and other debt securities	-	601,610,020	-	601,610,020
Equity securities	4,577	-	-	4,577
Total assets at fair value	<u>\$ 218,706,246</u>	<u>\$ 623,185,574</u>	<u>\$ -</u>	<u>\$ 841,891,820</u>

Money market funds	\$ 16,449,988	\$ -	\$ -	\$ 16,449,988
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The following table represents the Plan's financial instruments as of June 30, 2017, measured at fair value on a recurring basis using the fair value hierarchy defined in Note 3:

Money market funds	\$ 16,449,988	\$ -	\$ -	\$ 16,449,988
U.S. Government and agency securities	206,686,718	8,244,332	-	214,931,050
Corporate and other debt securities	-	654,027,109	-	654,027,109
Equity securities	5,293	-	-	5,293
Total assets at fair value	<u>\$ 223,141,999</u>	<u>\$ 662,271,441</u>	<u>\$ -</u>	<u>\$ 885,413,440</u>

Contributions

During Fiscal 2018, Health Services contributed \$31,500,000 to the pension plan in advance of the expected September, 2018 required contribution. Health Services expects to contribute approximately \$31,500,000 to the pension plan and \$4,020,061 to the postretirement benefit plan during the fiscal year ending June 30, 2019. The actual pension plan contribution may be higher or lower depending on interest rates, pension plan asset values, and legislated funding requirements.

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Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits	Postretirement Benefits
2019	\$ 51,593,355	\$ 4,020,061
2020	51,669,003	4,188,369
2021	54,301,629	4,186,002
2022	56,989,735	4,376,916
2023	58,744,420	4,523,697
2024 - 2028	316,227,855	23,982,640

The annual rate of increase assumed in the per capita cost of covered health care benefits was 6.75% and 7.50% for the Pre 65 and Post 64 participants, respectively, for June 30, 2018; the rates are assumed to decrease gradually to 5% for the fiscal year 2025 and remain at that level thereafter.

	1-Percentage Point Increase	1-Percentage Point Decrease
Effect on total service and interest cost	\$ 41,722	\$ (38,817)
Effect on postretirement benefit obligation	522,614	(489,430)

Defined Contribution Retirement Plan

Health Services sponsors a defined contribution retirement plan for all employees hired after August 13, 2006. Under the plan, Health Services contributes a percent of compensation quarterly based on an employee's years of vesting service. The employees vest in the employer contributions over a three-year period beginning on the employee's hire date. The expense incurred by Health Services for the year ended June 30, 2018 and June 30, 2017 was \$15,388,540 and \$13,405,530, respectively.

Deferred Compensation Plan

Health Services maintains a Tax-Deferred Annuity Plan for all employees. Under the plan, Health Services accumulates employee contributions which are transferred to and invested by various trustees. Health Services contributes 50% of the employee contributions up to a maximum of 3% of an employee's salary. Contributions for the year ended June 30, 2018 and 2017 were \$16,494,256 and \$15,502,467, respectively.

12. Self-Insurance Liabilities

Health Services maintains self-insurance programs for medical malpractice and worker's compensation claims. The medical malpractice program provides for a self insured retention of \$3,500,000 per claim and \$14,000,000 annual aggregate. The limit of excess coverage is \$60,000,000 per year for the System and its subsidiaries.

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Actuarially determined accruals for asserted and unasserted medical malpractice and worker's compensation claims at June 30, 2018 and 2017 amounted to \$49,839,192 and \$38,769,144, respectively. This liability represents the undiscounted estimated value of malpractice and worker's compensation claims that will be settled in the future based on anticipated payout patterns. The current portion of the accruals of \$16,515,268 and \$14,188,839 at June 30, 2018 and 2017, respectively, is recorded as a component of other accrued expenses and current liabilities on the balance sheets. Total expense incurred for medical malpractice and worker's compensation costs was \$29,205,140 in 2018 and \$6,083,271 in 2017 due to a growth in the medical malpractice liability.

13. Charity Care, Government Discounts, and Provision for Bad Debts

Health Services provides services to patients who meet the criteria of its charity service policy without charge or at amounts less than the established rates. Criteria for charity care considers the patient's family income, net worth, and other factors. Direct and indirect costs for these services amounted to \$22.6 million and \$15.6 million in 2018 and 2017, respectively. The costs of providing charity care services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients.

In addition to charity services, the Medicaid program reimburses Health Services for services at amounts that are substantially less than the cost to provide such services. The difference between the cost to provide those services and the reimbursement from the Medicaid program was approximately \$38.7 million and \$35.0 million in 2018 and 2017, respectively.

Health Services also records a provision for bad debts, which represents management's estimate of patient accounts receivable that will not be collected even though the patient does not meet the charity care criteria. The provision for bad debts was \$50,250,831 and \$48,439,495 in 2018 and 2017, respectively.

14. Related Party Transactions

Health Services has provided certain administrative, professional, and technical services to the System, Health Initiatives, and CCHHCS, totaling \$6,136,652 and \$4,570,776 for the years ended June 30, 2018 and 2017, respectively. Included within other current assets are amounts due from affiliates of \$7,606,979 and \$4,169,287 at June 30, 2018 and 2017, respectively.

Included in long-term investments are funds held for the benefit of CCHHCS in the amount of \$10,318,078 and \$9,212,834 at June 30, 2018 and 2017, respectively. A corresponding amount due to CCHHCS is recorded within other liabilities at June 30, 2018 and 2017.

Health Services recorded transfers from and to affiliated organizations representing cash in the amount of \$0 and \$1,900,000 during the fiscal years ended June 30, 2018 and 2017, respectively. These transfers are recorded as a component of other changes in unrestricted net assets and are excluded from the excess of revenues over expenses.

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15. Concentrations of Credit Risk

Health Services grants credit without collateral to its patients, most of whom are local residents and insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2018 and 2017 was as follows:

	2018	2017
Commercial payors	45 %	42 %
Medicaid	21	20
Medicare	20	26
Patients	14	12
	<u>100 %</u>	<u>100 %</u>

16. Functional Expenses

Health Services provides health care services to residents within its geographic location. Expenses related to providing these services are as follows:

	2018	2017
Health care services	\$ 1,586,956,018	\$ 1,488,789,937
General and administrative	<u>249,250,320</u>	<u>213,580,448</u>
	<u>\$ 1,836,206,338</u>	<u>\$ 1,702,370,385</u>