
Genesis HealthCare System and Subsidiaries

**Consolidated Financial Report
with Additional Information
December 31, 2017**

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Independent Auditor's Report

To the Board of Directors
Genesis HealthCare System and Subsidiaries

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Genesis HealthCare System and Subsidiaries (the "System"), which comprise the consolidated balance sheet 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 accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of Genesis HealthCare Foundation, a controlled subsidiary, whose statements reflect total assets constituting 9 and 8 percent of consolidated total assets at December 31, 2017 and 2016, respectively, and total excess of revenue over expenses constituting 28 percent and 11 percent, respectively, of consolidated total excess of revenue over expenses for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Genesis HealthCare Foundation, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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. Genesis HealthCare Foundation was not audited under *Government Auditing Standards*.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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, based on our audits and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Genesis HealthCare System and Subsidiaries 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 accounting principles generally accepted in the United States of America.

To the Board of Directors
Genesis HealthCare System and Subsidiaries

Other Matters

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements of Genesis HealthCare System and Subsidiaries. The consolidating balance sheet and consolidating statement of operations and changes in unrestricted net assets are presented for the purpose of additional analysis and are not a required part of the consolidated financial statements.

The consolidating balance sheet and consolidating statement of operations and changes in unrestricted net assets are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, based on our audits and the report of other auditors for the 2017 Genesis HealthCare Foundation financial statements, the consolidating balance sheet and consolidating statement of operations and changes in unrestricted net assets are fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 13, 2018 on our consideration of Genesis HealthCare System and Subsidiaries' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Genesis HealthCare System and Subsidiaries' internal control over financial reporting and compliance.



March 13, 2018

Genesis HealthCare System and Subsidiaries

Consolidated Balance Sheet

December 31, 2017 and 2016

	2017	2016
Assets		
Current Assets		
Cash and cash equivalents	\$ 32,199,969	\$ 20,714,091
Accounts receivable (Note 4)	66,434,655	67,016,229
Estimated third-party payor settlements	-	5,128,705
Inventory	9,855,851	10,269,152
Other assets	9,320,152	9,860,196
Total current assets	117,810,627	112,988,373
Assets Limited as to Use (Note 7)	193,961,300	175,055,176
Property and Equipment - Net (Note 8)	308,339,694	315,269,296
Beneficial Interest in Perpetual Trusts	14,498,896	13,067,990
Other Assets		
Long-term investments	679,394	825,588
Other noncurrent assets	3,341,967	6,525,034
Total assets	\$ 638,631,878	\$ 623,731,457
Liabilities and Net Assets		
Current Liabilities		
Accounts payable	\$ 17,472,082	\$ 23,202,186
Current portion of long-term debt (Note 9)	3,755,000	3,575,000
Estimated third-party payor settlements	3,389,385	-
Accrued liabilities and other:		
Accrued compensation	27,522,315	26,325,650
Other accrued liabilities	7,134,456	6,712,202
Total current liabilities	59,273,238	59,815,038
Long-term Debt - Net of current portion (Note 9)	287,941,989	290,594,517
Other Liabilities		
Pension and other postretirement obligations (Note 14)	35,430,217	40,731,184
Deferred revenue	3,850,051	4,736,012
Accrued professional liability	6,855,707	6,607,703
Total liabilities	393,351,202	402,484,454
Net Assets		
Unrestricted:		
Net assets	224,509,472	201,557,270
Noncontrolling interest (Note 15)	818,395	1,147,428
Temporarily restricted	1,967,960	2,023,452
Permanently restricted	17,984,849	16,518,853
Total net assets	245,280,676	221,247,003
Total liabilities and net assets	\$ 638,631,878	\$ 623,731,457

Genesis HealthCare System and Subsidiaries

Consolidated Statement of Operations

Years Ended December 31, 2017 and 2016

	2017	2016
Unrestricted Revenue, Gains, and Other Support		
Net patient service revenue	\$ 458,028,353	\$ 454,829,135
Less provision for bad debts	<u>(15,311,728)</u>	<u>(18,148,231)</u>
Net patient service revenue less provision for bad debts	442,716,625	436,680,904
Pharmacy sales and other	<u>78,036,144</u>	<u>74,850,429</u>
Total unrestricted revenue, gains, and other support	520,752,769	511,531,333
Expenses		
Salaries and wages	207,822,211	205,561,506
Employee benefits and payroll taxes	51,488,624	54,207,832
Operating supplies and expenses	75,276,753	74,817,781
Professional services and consultant fees	21,040,555	17,810,704
Purchased services	44,108,237	41,028,515
Utilities	6,202,889	6,801,377
Repairs, rentals, insurance, and other	40,738,756	35,267,205
Pharmacy cost of goods sold	36,066,194	36,470,761
Depreciation	22,738,970	23,073,703
Interest expense	<u>14,564,170</u>	<u>14,927,896</u>
Total expenses	<u>520,047,359</u>	<u>509,967,280</u>
Operating Income	705,410	1,564,053
Other Income (Loss)		
Investment income (Note 7)	6,760,831	6,699,988
Unrealized gains on trading securities (Note 7)	12,436,937	303,682
Other	<u>(2,200,390)</u>	<u>(2,116,469)</u>
Total other income	<u>16,997,378</u>	<u>4,887,201</u>
Excess of Revenue Over Expenses	17,702,788	6,451,254
Capital Distributions	(411,999)	(326,767)
Pension-related Changes Other than Net Periodic Cost	4,473,538	(1,977,947)
Net Assets Released from Restriction for Capital Equipment	<u>858,842</u>	<u>3,669,901</u>
Increase in Unrestricted Net Assets	<u><u>\$ 22,623,169</u></u>	<u><u>\$ 7,816,441</u></u>

Genesis HealthCare System and Subsidiaries

Consolidated Statement of Changes in Net Assets

Years Ended December 31, 2017 and 2016

	2017	2016
Unrestricted Net Assets		
Excess of revenue over expenses	\$ 17,702,788	\$ 6,451,254
Pension-related changes other than net periodic cost	4,473,538	(1,977,947)
Capital distributions	(411,999)	(326,767)
Net assets released from restriction for capital equipment	858,842	3,669,901
Increase in unrestricted net assets	22,623,169	7,816,441
Temporarily Restricted		
Restricted contributions	803,350	1,360,377
Net assets released from restriction for capital equipment	(858,842)	(3,669,901)
Decrease in temporarily restricted net assets	(55,492)	(2,309,524)
Permanently Restricted - Net unrealized gain in fair value of perpetual trusts	1,465,996	178,380
Increase in Net Assets	24,033,673	5,685,297
Net Assets - Beginning of year	221,247,003	215,561,706
Net Assets - End of year	<u>\$ 245,280,676</u>	<u>\$ 221,247,003</u>

Genesis HealthCare System and Subsidiaries

Consolidated Statement of Cash Flows

Years Ended December 31, 2017 and 2016

	2017	2016
Cash Flows from Operating Activities		
Increase in net assets	\$ 24,033,673	\$ 5,685,297
Adjustments to reconcile increase in net assets to net cash and cash equivalents from operating activities:		
Depreciation and amortization	22,784,603	23,248,793
Unrealized gain on trading securities	(12,436,937)	(303,682)
Net realized gain on investments	(4,184,604)	(4,461,981)
Pension-related changes other than net periodic cost	(4,473,538)	1,977,947
Restricted contributions	(803,350)	(1,360,377)
Provision for bad debts	15,311,728	18,148,231
Net unrealized gain in fair value of perpetual trusts	(1,465,996)	(178,380)
Changes in operating assets and liabilities which (used) provided cash and cash equivalents:		
Accounts receivable	(14,730,154)	(23,400,627)
Inventory and other assets	4,136,412	566,600
Estimated third-party payor settlements	8,518,090	(1,150,945)
Accounts payable	(5,730,104)	(2,708,080)
Accrued compensation and other	1,618,919	5,168,858
Deferred revenue	(885,961)	(774,432)
Accrued professional liability and pension	(579,425)	1,254,837
Net cash and cash equivalents provided by operating activities	31,113,356	21,712,059
Cash Flows from Investing Activities		
Purchase of property and equipment	(15,914,527)	(16,045,536)
Proceeds from sale of property and equipment	105,159	694,862
Purchases of investments and assets limited as to use	(12,754,979)	(6,083,974)
Proceeds from sale of investments and assets limited as to use	10,651,680	4,871,332
Net cash and cash equivalents used in investing activities	(17,912,667)	(16,563,316)
Cash Flows from Financing Activities		
Principal payments on long-term debt	(3,575,000)	(3,400,000)
Proceeds from restricted contributions	803,350	1,360,377
(Payments to) proceeds from revolving credit loan	(1,250,000)	750,000
Proceeds from bond issuance	2,306,839	-
Net cash and cash equivalents used in financing activities	(1,714,811)	(1,289,623)
Net Increase in Cash and Cash Equivalents	11,485,878	3,859,120
Cash and Cash Equivalents - Beginning of year	20,714,091	16,854,971
Cash and Cash Equivalents - End of year	\$ 32,199,969	\$ 20,714,091
Supplemental Cash Flow Information - Cash paid for interest - Net of capitalized interest	\$ 14,608,000	\$ 14,852,000

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 1 - Nature of Business

Genesis HealthCare System (the "System") is a nonprofit corporation organized under the laws of the State of Ohio to provide and promote healthcare services.

Effective January 1, 1997, Bethesda Care System (Bethesda Care), an Ohio nonprofit corporation, signed an affiliation agreement (the "agreement") with Good Samaritan Medical Center of the Franciscan Sisters of Christian Charity (GSMC), an Ohio nonprofit corporation, and Franciscan Sisters of Christian Charity Sponsored Ministries, Inc., a Wisconsin nonstock nonprofit corporation (FSCCM), which is the sole corporate member of GSMC. The agreement provided for the creation of Genesis HealthCare System, of which Bethesda Care and FSCCM are 50 percent co-members. The agreement provides for the integration of GSMC and Bethesda Care operations under the System and shall be a community-based healthcare delivery system operating a Catholic community hospital and healthcare system.

The System is the sole corporate member of CareServe and its subsidiaries (CareServe) and Genesis HealthCare Foundation (the "Foundation"). In addition, the System owns 100 percent of the stock of CareLife, Inc. and its wholly owned subsidiaries. The System also has a 75 percent member interest in Community Ambulance Service (CAS).

All rights, titles, and interest of Bethesda Care and GSMC and their nonprofit and for-profit subsidiaries were transferred to the System on January 1, 1997, with the exception of legal title to certain real property comprising substantially all of Bethesda Hospital and GSMC's current campuses, and cash and investments totaling approximately \$5,710,000 for each member. Bethesda Care and GSMC have entered into a 70-year lease agreement to lease the nontransferred real property to the System for a nominal amount. Related debt of Bethesda Care and GSMC was transferred to the System effective January 1, 1997. During 2009, both Bethesda Care and GSMC provided member contributions and pledges of funding to the System that totaled \$10,200,000. This funding was completed in 2014.

During 2004, the System established Southeast Ohio Medical Insurance Company, Ltd. (SOMIC), a wholly owned captive insurance company incorporated in the Cayman Islands. Effective August 1, 2004, SOMIC began providing professional liability and related general liability insurance to the System and certain employed health professionals. SOMIC also provides professional liability and related general liability coverage to participating staff physicians.

During 2010, the System entered into a joint venture with an Ohio limited liability company (Alternate Solutions Healthcare Central, LLC) to form Zanesville Homecare Ventures, LLC (Genesis Homecare). The System assigned 100 percent of its membership interest to CareLife, Inc. Each member owns 50 percent of Zanesville Homecare Ventures, LLC. The operations of Genesis Homecare are accounted for using the equity method on CareLife, Inc.

During 2013, the System established Ohio Integrated Care Providers, LLC (OICP). OICP was developed to create a clinically integrated system to develop improved patient care and lower healthcare costs. As of December 31, 2017, OICP does not have any risk based contracts to provide these services.

The System paid approximately \$2,381,000 and \$1,954,000 in 2017 and 2016, respectively, to FSCCM for management and support services.

Note 2 - Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include all the accounts of the System, including all wholly owned subsidiaries and majority-owned entities. The noncontrolling interest in majority-owned entities on the December 31, 2017 and 2016 consolidated balance sheet represents a 25 percent outside membership interest in CAS. The System consolidated the balance sheets and statements of operations and changes in net assets of CAS. All material intercompany accounts and transactions have been eliminated in consolidation.

Note 2 - Significant Accounting Policies (Continued)

Cash and Cash Equivalents

Cash and cash equivalents include cash and highly liquid investments purchased with an original maturity of three months or less, excluding those amounts included in assets limited as to use.

Accounts Receivable

Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges. An allowance for contractual adjustments and interim payment advances is based on expected payment rates from payors based on current reimbursement methodologies. Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the System analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the System analyzes contractually due amounts and provides an allowance for contractual adjustments, which includes any patient responsibility deemed uncollectible.

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

Inventories

Inventories, which consist of medical and office supplies and pharmaceutical products, are stated at cost, determined on a first-in, first-out basis or market.

Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheet. Investments in partnerships and limited liability companies are reported using the equity method of accounting. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in excess of revenue over expenses unless the income or loss is restricted by donor or law.

The System invests much of its funds in the FSCCM pooled investment management program. The pooled investment management program primarily invests in cash and cash equivalents, marketable equity securities, corporate and government bonds, mutual funds, common collective funds, fund of funds hedge funds, real estate funds, and private equity funds. Earnings in the pooled investment program are allocated to the participants based upon each participant's weighted-average percentage of the pooled investment fund.

Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported on the consolidated balance sheet.

Note 2 - Significant Accounting Policies (Continued)

Beneficial Interest in Perpetual Trust

The Foundation is the beneficiary of certain funds held in trust by others, which represent resources neither in the possession nor under the control of the Foundation, but held in perpetuity and administered by outside trustees, with the Foundation deriving income from a portion of the assets held in such trusts. The Foundation's interest in perpetual trusts is recorded at the fair market value of the Foundation's interest in the trust and is recorded as an investment held for long-term purposes. The contribution revenue from perpetual trusts is an increase in permanently restricted net assets.

Cash distributions received by these perpetual trusts are reported as investment income in the accompanying consolidated statement of operations. The investment income is reported as increases in temporarily restricted or unrestricted net assets based upon the existence or absence of donor-imposed restrictions.

Changes in the fair market value of the Foundation's portion of the funds held in perpetual trusts are reported in the accompanying consolidated statement of operations as a net unrealized gain or loss in permanently restricted net assets.

Assets Limited as to Use

Assets limited as to use include assets designated by the board of directors for future capital improvement, assets held by trustees under indenture agreements, funds received by donors, and assets held for professional and other liability claims. The board retains control over assets held for future capital improvements and may, at its discretion, use them for other purposes.

Charity Care

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

Charity care is determined based on established policies, using patient income and assets to determine payment ability. The amount reflects the cost of free or discounted health services, net of contributions and other revenue received, as direct assistance for the provision of charity care. The estimated cost of providing charity services is based on a calculation which applies a ratio of cost to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the System's total operating expenses divided by gross patient service revenue. The System estimates that it provided approximately \$1,573,000 and \$1,368,000 of services to indigent patients during 2017 and 2016, respectively. The System recorded \$9,302,000 and \$9,317,000 in net distributions from the Ohio Medicaid HCAP program as revenue during 2017 and 2016, respectively, and it is estimated that approximately \$1,100,000 and \$2,100,000 of the total net distributions from the Ohio HCAP program related to HCAP and charity patients during 2017 and 2016, respectively.

Property and Equipment

Property and equipment purchases are recorded at cost or at fair value if acquired by gift. Depreciation is computed principally using the straight-line method over the estimated useful lives of the assets. Costs of maintenance and repairs are charged to expense when incurred.

Professional and Other Liability Insurance

The System accrues an estimate of the ultimate expense, including litigation and settlement expense, for incidents of potential improper professional service and other liability claims occurring during the year as well as for those claims that have not been reported at year end.

December 31, 2017 and 2016

Note 2 - Significant Accounting Policies (Continued)

Classification of Net Assets

Net assets of the System are classified as permanently restricted, temporarily restricted, or unrestricted depending on the presence and characteristics of donor-imposed restrictions limiting the System's ability to use or dispose of contributed assets or the economic benefits embodied in those assets. Donor-imposed restrictions that expire with the passage of time or that can be removed by meeting certain requirements result in temporarily restricted net assets. Permanently restricted net assets result from donor-imposed restrictions that limit the use of net assets in perpetuity. Earnings, gains, and losses on restricted net assets are classified as unrestricted unless specifically restricted by the donor or by applicable state law.

Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactively calculated adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Management believes that it is in compliance with all applicable laws and regulations. Final determination of compliance of such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action, including fines, penalties, and exclusions from the Medicare and Medicaid programs.

The System 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 that do not qualify for charity care, the System recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). On the basis of historical experience, a significant portion of the System's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the System records a significant provision for bad debts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the period from these major payor sources in total was approximately \$458,028,000 and \$454,829,000 at December 31, 2017 and 2016, respectively. These amounts are made up of amounts from third-party payors of approximately \$449,635,000 and \$447,643,000 and amounts from self-pay payors of approximately \$8,393,000 and \$7,186,000 for the years ended December 31, 2017 and 2016, respectively.

Pharmacy Sales and Other Revenue

Revenue is primarily composed of retail pharmacy sales, home infusion services, durable medical equipment sales, revenue from electronic health records incentive payments, and hospital cafeteria sales.

Contributions

The System reports gifts of cash and other assets as 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 to unrestricted net assets and reported in the consolidated statement of changes in net assets as net assets released from restrictions.

Note 2 - Significant Accounting Policies (Continued)

The System reports gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. 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, the System reports the expiration of donor restrictions when the assets are placed in service.

Excess of Revenue Over Expenses

The consolidated statement of operations includes excess of revenue over expenses. Changes in unrestricted net assets, which are excluded from excess of revenue over expenses, consistent with industry practice, include net assets released from restrictions for the acquisition of long-lived assets, permanent transfers of assets to and from affiliates for other than goods and services, capital distributions to joint venture partners, and pension-related changes other than net periodic cost.

Use of Estimates

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

Tax Status

The System and its subsidiaries are tax-exempt organizations, except for CareLife; accordingly, no tax provision is reflected in the consolidated financial statements.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the System and to recognize a tax liability if the System has taken an uncertain position that more likely than not would not be sustained upon examination by the Internal Revenue Service or other applicable taxing authorities.

Sale Leaseback

The System has entered into sale-leaseback arrangements. Under the arrangements, the System sold property and leased it back. The leasebacks have been accounted for as operating leases. The gain on the transactions is deferred and recognized into income in proportion to rental expense over the term of the lease.

Subsequent Events

The consolidated financial statements and related disclosures include evaluation of events up through and including March 13, 2018, which is the date the consolidated financial statements were available to be issued.

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 2 - Significant Accounting Policies (Continued)

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) released Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which will supersede the current revenue recognition requirements in Topic 605, *Revenue Recognition*. The ASU is based on the principal that revenue is recognized to depict the transfer of goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new guidance will be effective for the System's year ending December 31, 2018. Management does not expect that this standard will have a significant impact on the System's main revenue stream. However, management has not completed its assessment on its revenue streams.

In February 2016, the Financial Accounting Standards Board issued ASU No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the System's year ending December 31, 2019 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The effect of applying the new lease guidance on the consolidated financial statements has not yet been determined.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. ASU No. 2016-14 requires significant changes to the financial reporting model of organizations that follow FASB not-for-profit rules, including changing from three classes of net assets to two classes: net assets with donor restrictions and net assets without donor restrictions. The ASU will also require changes in the way certain information is aggregated and reported by the System, including required disclosures about the liquidity and availability of resources. The new standard is effective for the System's year ending December 31, 2018 and thereafter, and must be applied on a retrospective basis. The System expects this standard to have an impact on the presentation of net assets and to result in enhanced disclosures related to liquidity and availability.

Note 3 - Cash in Excess of Insured Limits

The System and its subsidiaries maintain cash and investment balances at several financial institutions located in the vicinity of Zanesville, Ohio. Accounts at each institution are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per institution. As of December 31, 2017 and 2016, the System holds funds at various institutions in excess of insured limits.

Note 4 - Patient Accounts Receivable

The details of patient accounts receivable are set forth below:

	2017	2016
Patient accounts receivable	\$ 153,551,875	\$ 153,366,258
Less:		
Allowance of uncollectible accounts	8,890,839	10,343,833
Allowance for contractual adjustments	78,226,381	76,006,196
Net patient accounts receivable	<u>\$ 66,434,655</u>	<u>\$ 67,016,229</u>

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 4 - Patient Accounts Receivable (Continued)

The System grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The composition of receivables from patients and third-party payors was as follows:

	2017	2016
Medicare	35 %	38 %
Medicaid	19	19
Commercial insurance and HMOs	31	29
Self-pay	15	14
Total	100 %	100 %

Note 5 - Patient Service Revenue

Approximately 54 percent of the System's net patient service revenue is received from the Medicare and Medicaid programs. Subsidiaries of the System have agreements with third-party payors that provide for reimbursement at amounts different from established rates. A summary of the basis of reimbursement with these third-party payors is as follows:

- **Medicare**

Inpatient, acute-care, and rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Outpatient and home care services related to Medicare beneficiaries are reimbursed based on a prospectively determined amount per episode of care.

- **Medicaid**

Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Outpatient and physician services are reimbursed on an established fee-for-service methodology.

The Medicaid payment system in Ohio is a prospective one, whereby rates for the following state fiscal year beginning July 1 are based upon filed cost reports for the preceding calendar year. The continuity of this system is subject to the uncertainty of the fiscal health of the State of Ohio, which can directly impact future rates and the methodology currently in place. Any significant changes in rates, or the payment system itself, could have a material impact on the future Medicaid funding to providers.

- **Other Third-party Payors**

The System has also entered into agreements with certain commercial carriers, health maintenance organizations, and preferred provider organizations. The basis for reimbursement to the System under these agreements is discounts from established charges, prospectively determined rates per discharge, and prospectively determined daily rates.

- **Health Maintenance Organizations**

Services rendered to HMO beneficiaries are paid at predetermined rates or at a percentage of system charges.

Cost report settlements result from the adjustment of interim payments to final reimbursement under the Medicare and HMO programs that are subject to audit by fiscal intermediaries. 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.

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 6 - Community Benefit

In support of its mission, the System provides various health-related services, at a loss, to the indigent and other residents in its service area. The following is a summary of the System's community benefit expense:

	2017	2016
Community partnership programs (unaudited)	\$ 2,418,000	\$ 2,101,000
Donations/Contributions (unaudited)	354,000	354,000
Traditional charity care	1,573,000	1,368,000
Unpaid costs for government program patients (unaudited)	24,696,000	28,859,000
Total	<u>\$ 29,041,000</u>	<u>\$ 32,682,000</u>

Community Partnership Programs

Community partnership programs include programs provided to persons with inadequate healthcare resources or for other groups within the community that need special services and support. Examples include programs related to the poor, elderly, substance abuse, child abuse, and others with specific particular healthcare needs. They also include broader populations who benefit from health community initiatives such as health promotion, education, and health screening.

Donations/Contributions

Donations/Contributions include cash and in-kind donations that are made on behalf of the poor and needy to community agencies and to special funds for charitable activities as well as resources contributed directly to programs, organizations, and foundations for efforts on behalf of the poor and disadvantaged.

Traditional Charity Care

Traditional charity care covers services provided to persons who cannot afford to pay. The amount reflects the cost of free or discounted health services, net of contributions and other revenue received, as direct assistance for the provision of charity care. Charity care is determined based on established policies, using patient income and assets to determine payment ability.

Unpaid Costs for Government Program Patients

The System is a licensed Medicare and Medicaid provider with approximately 77 percent of its patient base qualifying for one of these two programs. At present, the reimbursement rates for both programs do not fully cover the cost of provider care to these patients. This represents the estimated shortfall created when a facility receives payments below the costs of treating Medicare and Medicaid beneficiaries.

Note 7 - Assets Limited as to Use

The detail of investments is summarized as follows:

	2017	2016
Assets limited as to use:		
By board of directors for future capital improvements	\$ 110,700,274	\$ 96,525,820
Funds held in trust for payment of debt service	27,681,477	27,488,802
Funds received from donors	39,040,156	35,097,118
Funds held for professional and other liability claims	16,539,393	15,943,436
Total assets limited as to use	<u>\$ 193,961,300</u>	<u>\$ 175,055,176</u>

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 7 - Assets Limited as to Use (Continued)

Investments consist of the following:

	2017	2016
Cash equivalents	\$ 27,786,806	\$ 10,729,532
U.S. government obligations	-	17,770,413
Alternative investments	12,451,425	12,358,067
Marketable equity securities	5,028,614	5,393,108
Mutual funds	36,933,581	31,217,636
Real estate	1,060,600	1,060,600
Investment in FSCCM pooled investment management program	110,700,274	96,525,820
Total	<u>\$ 193,961,300</u>	<u>\$ 175,055,176</u>

Investment income and gains are composed of the following:

	2017	2016
Investment income	\$ 2,576,227	\$ 2,238,007
Net realized gains on sales of investments	4,184,604	4,461,981
Unrealized investment gains	12,436,937	303,682
Total	<u>\$ 19,197,768</u>	<u>\$ 7,003,670</u>

Note 8 - Property and Equipment

Cost of property and equipment and depreciable lives are summarized as follows:

	2017	2016	Depreciable Life - Years
Land and land improvements	\$ 21,743,998	\$ 22,223,091	10-15
Buildings and fixed equipment	247,678,797	254,626,980	7-50
Major movable and minor equipment	217,582,926	213,418,974	3-13
Construction in progress	4,694,319	1,622,823	-
Total cost	491,700,040	491,891,868	
Less accumulated depreciation	183,360,346	176,622,572	
Net property and equipment	<u>\$ 308,339,694</u>	<u>\$ 315,269,296</u>	

Genesis HealthCare System and Subsidiaries

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Note 9 - Long-term Debt

Long-term debt is as follows:

	2017	2016
Muskingum County, Ohio Hospital Facilities Revenue Bonds, Series 2013, dated May 9, 2013, due on February 15, 2048, maturing in various amounts through 2048, with interest due semiannually, interest rates ranging from 4.0 percent to 5.0 percent	\$ 288,025,000	\$ 291,600,000
Genesis HealthCare System revolving credit loan payable to various banks carrying an interest rate equal to LIBOR, plus an applicable margin (3.31 percent at December 31, 2017), expiring on May 9, 2019 with principal payments due by expiration and interest payments due monthly	6,000,000	7,250,000
Perry County, Ohio Hospital Facilities Revenue Bonds, Series 2017, dated September 1, 2017, due on September 1, 2037, maturing in various amounts through 2037, with interest due monthly, interest rates initially 65.001 percent * one-month LIBOR rate + 1.46 percent (2.34 percent at December 31, 2017)	2,306,839	-
Unamortized bond discount	(307,685)	(317,800)
Unamortized debt issuance costs	(4,327,165)	(4,362,683)
Long-term debt less unamortized bond discount and debt issuance costs	291,696,989	294,169,517
Less current portion	3,755,000	3,575,000
Long-term portion	<u>\$ 287,941,989</u>	<u>\$ 290,594,517</u>

In May 2013, the County of Muskingum, Ohio issued \$295,000,000 of tax-exempt bonds on behalf of the Obligated Group. The bonds were issued to finance the construction of an addition and the related renovations of one of the System's hospital campuses (Bethesda) and refinance outstanding debt.

Also in May 2013, in conjunction with the issuance of the Series 2013 bonds, the System entered into a revolving credit facility with PNC Bank, N.A. and The Huntington National Bank. PNC Bank, N.A. holds 65 percent of the outstanding balance and The Huntington National Bank holds the remaining 35 percent. The maximum borrowing capacity is \$20,000,000. The System has the ability to choose an interest rate based upon a selection of various market rates at the time the revolving credit loans are drawn upon. At December 31, 2017, there had been \$6,000,000 drawn against the revolving credit.

In September 2017, the County of Perry, Ohio issued \$10,000,000 of tax-exempt bonds on behalf of the Obligated Group. The bonds were issued to purchase and finance the construction of the Genesis Perry County Medical Center along with furnishing the Center. Interest-only payments are required monthly on the bonds through February 2019.

In 2017, the System paid interest of \$14,580,000, of which \$15,000 was capitalized. In 2016, the System paid interest of \$14,928,000, of which none was capitalized.

The System formed an obligated group to accomplish common financing plans. The obligated group is governed by a master agreement and is composed of Genesis HealthCare System, CareServe, CareLife, Inc. and Subsidiaries, Ohio Integrated Care Providers, and the Genesis HealthCare Foundation (collectively, the "Obligated Group"). Each member of the Obligated Group is jointly and severally obligated with respect to substantially all of the debt for the System.

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 9 - Long-term Debt (Continued)

The terms of the debt require the Obligated Group to, among other things, comply with certain financial ratios, restrict additional encumbrances, maintain rates sufficient to meet debt service requirements, and maintain specified net assets.

The affiliation agreement (described in Note 1) also established a credit enhancement and line of credit agreement. In addition, the credit enhancement and line of credit agreement provide that the System could loan or provide credit support to FSCCM up to certain specified limits. Such loans cannot exceed 25 percent of the debt capacity of the System, as defined in the affiliation agreement, and interest is payable based on the Dow Jones Bond Averages, 20 Bond Taxable Index. FSCCM does not anticipate exercising the line of credit in 2017. In lieu of borrowing amounts from the System, FSCCM has the option to seek credit enhancement from the System. The System shall have the option to become a member of FSCCM's obligated group with respect to the proposed borrowing, provide a contractual guarantee with respect to the proposed borrowing, or pay to FSCCM credit enhancement payments with respect to such proposed borrowing for the difference between the credit rating obtained with and without the System as a member of the FSCCM obligated group. No loans or credit support were provided to FSCCM by the System in 2017 or 2016.

Minimum principal payments on long-term debt to maturity as of December 31, 2017 are as follows:

2018	\$	3,755,000
2019		9,950,000
2020		4,155,000
2021		4,365,000
2022		6,896,839
Thereafter		267,210,000
Less unamortized bond discount		(307,685)
Less unamortized debt issuance costs		<u>(4,327,165)</u>
Total	\$	<u>291,696,989</u>

Note 10 - Operating Leases

The System is obligated under various operating leases. Total rent expense under these leases was approximately \$9,541,000 and \$9,350,000 for the years ended December 31, 2017 and 2016, respectively. Future lease payments include additional operating lease costs based on the sale-leaseback agreement into which the System entered during 2010.

The following is a schedule of future minimum lease payments under operating leases that have initial or remaining lease terms in excess of one year:

<u>Years Ending</u>	<u>Amount</u>
2018	\$ 6,928,452
2019	6,241,720
2020	6,014,879
2021	5,128,637
2022	4,973,940
Thereafter	<u>10,039,447</u>
Total	<u>\$ 39,327,075</u>

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 11 - Professional Liability Insurance

Effective August 1, 2004, the System, through SOMIC, maintains a policy of self-insuring its professional liability risks for individual losses up to specified amounts per claim. In addition, the self-insurance plan has specified annual aggregate limits. The System carries commercial insurance coverage for incidents which would exceed coverages specified by the self-insurance program on a claims-made basis.

Because of the nature of its operations, the System is at all times subject to pending and threatened legal actions which arise in the normal course of its activities.

Malpractice and general patient liability claims for incidents which may give rise to litigation have been asserted against the System and attending physicians with insurance coverage provided by SOMIC by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. There are also known incidents that have occurred through December 31, 2017 that may result in the assertion of additional claims. There may be other claims from unreported incidents arising from services provided to patients. The reserve for medical malpractice includes amounts for claims and related legal expenses for these unreported incidents. In 2017 and 2016, the reserve was actuarially determined by combining industry data and the System's historical experience. Accrued malpractice losses have been discounted at 2.00 percent, and in management's opinion, provide an adequate reserve for loss contingencies.

The System established a trust for the purpose of setting aside assets based on actuarial funding recommendations for claims incurred prior to August 1, 2004. Under the trust agreement, the trust assets can only be used for payment of malpractice losses, related expenses, and the cost of administering the trust.

Note 12 - Functional Expenses

The System provides diversified healthcare services to residents in the southeastern Ohio area. Expenses related to providing these services for the years ended December 31, 2017 and 2016 are approximately as follows:

	2017	2016
Healthcare services	\$ 398,382,000	\$ 383,325,000
General and administrative	121,665,000	126,642,000
Total	<u>\$ 520,047,000</u>	<u>\$ 509,967,000</u>

Note 13 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the consolidated financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the System has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. The Level 2 inputs include quoted prices for similar assets and liabilities in active markets and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 13 - Fair Value Measurements (Continued)

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The System's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

The System's policy is to recognize transfers between levels of the fair value hierarchy as of the beginning of the reporting period. For the years ended December 31, 2017 and 2016, there were no transfers between levels.

The following tables present information about the System's assets, held directly by the System, excluding its investment in the pooled investment program, measured at fair value on a recurring basis at December 31, 2017 and 2016, and the valuation techniques used by the System to determine those fair values.

	Assets Measured at Fair Value on a Recurring Basis at December 31, 2017				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Other Significant Unobservable Inputs (Level 3)	Investments Valued at Net Asset Value	Balance at December 31, 2017
Assets					
Marketable equity securities:					
Growth equities	\$ 3,146,848	\$ -	\$ -	\$ -	\$ 3,146,848
Value equities	1,881,766	-	-	-	1,881,766
Real estate	-	1,060,600	-	-	1,060,600
Mutual funds:					
Index funds	5,420,911	-	-	-	5,420,911
Value funds	2,448,720	-	-	-	2,448,720
Global equity funds	3,308,446	-	-	-	3,308,446
International funds	5,012,517	-	-	-	5,012,517
Emerging markets	1,451,760	-	-	-	1,451,760
Master limited partnerships	667,983	-	-	-	667,983
Mortgages	1,237,264	-	-	-	1,237,264
Global infrastructure	421,341	-	-	-	421,341
TIPS	2,367,160	-	-	-	2,367,160
Fixed-income funds	14,597,479	-	-	-	14,597,479
Beneficial interest in perpetual trusts	-	-	14,498,896	-	14,498,896
Investments valued at net asset value	-	-	-	12,451,425	12,451,425
Total assets	\$ 41,962,195	\$ 1,060,600	\$ 14,498,896	\$ 12,451,425	\$ 69,973,116

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 13 - Fair Value Measurements (Continued)

	Assets Measured at Fair Value on a Recurring Basis at December 31, 2016				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Investments Valued at Net Asset Value	Balance at December 31, 2016
Assets					
Assets limited as to use - U.S. government obligations:					
Federal home loan	\$ -	\$ 9,007,200	\$ -	\$ -	\$ 9,007,200
FNMA	-	8,763,213	-	-	8,763,213
Marketable equity securities:					
Growth equities	4,313,843	-	-	-	4,313,843
Value equities	1,079,265	-	-	-	1,079,265
Real estate	-	1,060,600	-	-	1,060,600
Mutual funds:					
Index funds	3,089,185	-	-	-	3,089,185
Value funds	2,138,626	-	-	-	2,138,626
Global equity funds	2,876,181	-	-	-	2,876,181
International funds	5,251,560	-	-	-	5,251,560
Emerging markets	1,079,647	-	-	-	1,079,647
Master limited partnerships	724,573	-	-	-	724,573
Mortgages	1,191,559	-	-	-	1,191,559
Global infrastructure	371,376	-	-	-	371,376
TIPS	988,167	-	-	-	988,167
Fixed-income funds	13,506,762	-	-	-	13,506,762
Beneficial interest in perpetual trusts	-	-	13,067,990	-	13,067,990
Investments valued at net asset value	-	-	-	12,358,067	12,358,067
Total assets	\$ 36,610,744	\$ 18,831,013	\$ 13,067,990	\$ 12,358,067	\$ 80,867,814

The fair value of the Level 2 securities as of December 31, 2017 and 2016 was determined primarily on quoted prices from the System's custodian bank and administrators of the funds.

As described in Note 2, the System participates in FSCCM's pooled investment program. As of December 31, 2017 and 2016, the System has \$110,700,274 and \$96,525,820, respectively, of investments at market value in the pool. The fair value of the investments in the pooled investment program is determined based on Level 3 inputs, estimated based on the System's percentage share of ownership, based on original value of contributions. There are no restrictions on redemption from the pooled investment management program for the System.

The underlying investments in the pool program are composed of assets with valuation techniques that result in 71 percent as Level 1, 8 percent as Level 2, and the remaining amounts comprised of assets valued at net asset value, which are excluded from the fair value reporting hierarchy as of December 31, 2017. At December 31, 2016, the investments in the pool program were composed of 74 percent Level 1, 21 percent Level 2, and the remaining amounts were composed of assets valued at net asset value, which are excluded from the fair value hierarchy.

The details of the fair value and unfunded commitments are described at length in the financial statements of FSCCM. The System's pro rata share of unfunded commitments is approximately \$2,729,000 and \$4,032,000 at December 31, 2017 and 2016, respectively.

There were no withdrawals or deposits during both 2017 and 2016. The total allocation of pooled earnings was \$14,174,453 and \$6,151,023 in 2017 and 2016, respectively.

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 13 - Fair Value Measurements (Continued)

The following table sets forth a summary of the changes in the fair value of the System's Level 3 assets at December 31, 2017 and 2016:

	Fair Value at January 1, 2017	Net Purchases and Issuances (Sales and Settlements)	Total Realized and Unrealized Gains	Net Transfers Into (Out of) Level 3	Fair Value at December 31, 2017
Level 3 Investments - Beneficial interest in perpetual trusts	\$ 13,067,990	\$ -	\$ 1,430,906	\$ -	\$ 14,498,896

	Fair Value at January 1, 2016	Net Purchases and Issuances (Sales and Settlements)	Total Realized and Unrealized Losses	Net Transfers Into (Out of) Level 3	Fair Value at December 31, 2016
Level 3 Investments - Beneficial interest in perpetual trusts	\$ 12,912,160	\$ -	\$ 155,830	\$ -	\$ 13,067,990

Investments in Entities that Calculate Net Asset Value per Share

The System holds shares or interests in investment companies at year end whereby the fair value of the investment held is estimated based on the net asset value per share (or its equivalent) of the investment companies as a practical expedient.

Investments Held at December 31, 2017

	Fair Value
Private equity (1)	\$ 1,218,822
Multistrategy hedge fund (2)	2,558,486
Long and short equities hedge fund (3)	6,355,652
Private real estate (4)	327,922
Event-driven hedge fund (5)	1,990,543
Total	<u>\$ 12,451,425</u>

Investments Held at December 31, 2016

	Fair Value
Private equity (1)	\$ 1,440,737
Multistrategy hedge fund (2)	2,336,600
Long and short equities hedge fund (3)	5,937,264
Private real estate (4)	552,452
Event-driven hedge fund (5)	2,091,014
Total	<u>\$ 12,358,067</u>

(1) Private equity funds broadly diversified across managers, investment stages, geography, industry sectors, and company size

(2) Multistrategy hedge funds with broadly diversified multi-advisor, multistrategy fund of hedge funds utilizing a proprietary portfolio construction methodology that combined a top-down strategy allocation process with comprehensive manager selection, due diligence, and risk management

(3) Long and short equities hedge funds are fund of funds with long/short focus. The managers employed by the funds are fundamentally driven, bottoms-up, research-intensive stock pickers who use very little, if any, leverage.

(4) Private real estate funds that invest in private real estate broadly classified as core, value-added, and opportunistic

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 13 - Fair Value Measurements (Continued)

(5) Event-driven hedge funds are seeking stable returns and appreciation, independent of returns of the overall equity and debt markets by using a variety of strategies but principally employing event-driven strategies.

Note 14 - Pension and Other Postretirement Benefit Plans

The System maintains a defined benefit pension plan covering substantially all its employees who have completed one year of continuous service as defined by the plan. Benefits paid under the plan are based generally on employees' years of service and compensation levels during employment. The plan requires annual contributions that are sufficient to meet the minimum funding standards of the Employee Retirement Income Security Act of 1974 and the Internal Revenue Code of 1986.

Effective April 8, 2009, new employees are no longer eligible to participate in the defined benefit plan, but will be eligible to participate in a defined contribution plan in which substantially all employees are eligible. The contributions are based on an employer's matching contribution of an employee's contribution up to a maximum of 60 percent of an employee's 5 percent contribution to the employee plan, based on years of service. For the years ended December 31, 2017 and 2016, the amount of retirement expense for the defined contribution plan was approximately \$1,996,000 and \$2,004,000, respectively.

The defined benefit plan was amended in 2011. As a result of the amendment, contributions to the plan for participants that were 50 years old and older as of June 30, 2011 were reduced as follows based on years of service:

- Up to five years of service were reduced from 2.25 percent to 2 percent.
- 5-10 years of service were reduced from 3 percent to 2 percent.
- 10 years of service or greater were reduced from 4 percent to 3 percent.

For participants that were under the age of 50 as of June 30, 2011, benefits were frozen but interest would continue to accrue on the frozen balance.

Obligations and Funded Status

	Pension Benefits	
	2017	2016
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 103,582,641	\$ 101,131,981
Service cost	520,611	584,563
Interest cost	4,283,483	4,444,030
Actuarial loss	2,347,383	2,875,487
Benefits paid	(5,112,904)	(5,453,420)
Projected benefit obligation at end of year	105,621,214	103,582,641
Change in plan assets:		
Fair value of plan assets at beginning of year	64,130,807	65,071,244
Actual return on plan assets	9,465,587	3,396,632
Employer contributions	3,496,952	1,116,351
Benefits paid	(5,112,904)	(5,453,420)
Fair value of plan assets at end of year	71,980,442	64,130,807
Funded status at end of year	\$ (33,640,772)	\$ (39,451,834)

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 14 - Pension and Other Postretirement Benefit Plans (Continued)

Included in unrestricted net assets at December 31, 2017 and 2016 are the following amounts that have not yet been recognized in net periodic pension cost:

	Pension Benefits	
	2017	2016
Net loss	\$ 28,815,718	\$ 33,297,664
Prior service cost	(23,105)	(53,504)
Total included in net assets not yet recognized in net periodic benefit cost	<u>\$ 28,792,613</u>	<u>\$ 33,244,160</u>

The accumulated benefit obligation for all defined benefit pension plans was \$105,591,146 and \$103,545,526 at December 31, 2017 and 2016, respectively.

Components of Net Periodic Benefit Cost

	2017	2016
Service cost	\$ 520,611	\$ 584,563
Interest cost	4,283,483	4,444,030
Expected return on plan assets	(5,113,087)	(4,925,305)
Recognized prior service credit	(30,399)	(30,399)
Recognized actuarial loss	2,476,829	2,467,942
Net periodic benefit cost	<u>\$ 2,137,437</u>	<u>\$ 2,540,831</u>

The estimated net loss and prior service cost for the defined benefit pension plans that will be amortized into net periodic benefit cost over the next fiscal year is \$3,023,432.

Assumptions

Weighted-average Assumptions Used to Determine Benefit Obligations at December 31

	Pension Benefits	
	2017	2016
Discount rate	4.00 %	4.25 %
Rate of compensation increase	3.00	3.00

Weighted-average Assumptions Used to Determine Net Periodic Benefit Cost for Years Ended December 31

	Pension Benefits	
	2017	2016
Discount rate	4.25 %	4.50 %
Increase in future compensation levels	3.00	3.00
Expected rate of return on plan assets	7.50	7.50

The overall expected rate of return on plan assets represents a weighted-average composite rate based on the historical rates of returns of the respective asset classes adjusted for anticipated market movements.

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 14 - Pension and Other Postretirement Benefit Plans (Continued)

Pension Plan Assets

The goals of the pension plan investment program are to fully fund the obligation to pay retirement benefits in accordance with the plan documents and to provide returns that, along with appropriate funding from the System, maintain an asset/liability ratio that is in compliance with all applicable laws and regulations and assures timely payment of retirement benefits.

The System's overall investment strategy is to achieve a mix of approximately 55 percent equity, 25 percent of investments in fixed income, and 20 percent in alternative investments, with a wide diversification of asset types, fund strategies, and fund managers.

Equity securities primarily include investments in large-cap and mid-cap companies primarily located in the United States and international equities, along with mutual funds. Fixed-income securities include asset management investments that invest in corporate bonds of companies from diversified industries, mortgage-backed securities, and U.S. Treasuries. Alternative investments include investments in fund-of-funds hedge funds, real estate funds, and private equity funds that follow several different strategies.

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

	Fair Value Measurements at December 31, 2017				Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Investments in Limited Partnerships Valued at Net Asset Value	
Mutual funds:					
Value funds	\$ 3,824,716	\$ -	\$ -	\$ -	\$ 3,824,716
Non-U.S. funds	11,357,983	-	-	-	11,357,983
Emerging market funds	3,639,951	-	-	-	3,639,951
S&P Index funds	7,641,721	-	-	-	7,641,721
Fixed-income investments	4,461,143	-	-	-	4,461,143
Money market funds	1,358,375	-	-	-	1,358,375
Bonds and notes:					
Federal Home Loan Mortgage bonds	-	8,951,077	-	-	8,951,077
Corporate bonds	-	3,660,654	-	-	3,660,654
Common stock	7,010,214	-	-	-	7,010,214
Comingled funds	-	13,473,580	-	-	13,473,580
Investments in limited partnerships valued at net asset value:					
Equity and credit market hedge fund (2)	-	-	-	5,429,700	5,429,700
Private equity funds (3)	-	-	-	590,502	590,502
Real estate funds (4)	-	-	-	580,826	580,826
Total	\$ 39,294,103	\$ 26,085,311	\$ -	\$ 6,601,028	\$ 71,980,442

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 14 - Pension and Other Postretirement Benefit Plans (Continued)

	Fair Value Measurements at December 31, 2016				Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Investments in Limited Partnerships Valued at Net Asset Value	
Mutual funds:					
Value funds	\$ 3,276,969	\$ -	\$ -	\$ -	\$ 3,276,969
Non-U.S. funds	8,493,829	-	-	-	8,493,829
Emerging market funds	2,445,305	-	-	-	2,445,305
S&P Index funds	6,312,870	-	-	-	6,312,870
Fixed-income investments	4,053,627	-	-	-	4,053,627
Money market funds	2,479,858	-	-	-	2,479,858
Bonds and notes:					
Federal Home Loan Mortgage bonds	-	7,523,045	-	-	7,523,045
Corporate bonds	-	3,826,825	-	-	3,826,825
Common stock	5,354,071	-	-	-	5,354,071
Comingled funds	-	6,629,563	-	-	6,629,563
Investments in limited partnerships valued at net asset value:					
Long and short equities hedge fund (1)	-	-	-	7,888,610	7,888,610
Equity and credit market hedge fund (2)	-	-	-	4,165,900	4,165,900
Private equity funds (3)	-	-	-	766,057	766,057
Real estate funds (4)	-	-	-	914,278	914,278
Total	\$ 32,416,529	\$ 17,979,433	\$ -	\$ 13,734,845	\$ 64,130,807

(1) Long and short equities hedge fund - A fund of funds with long/short focus. The managers employed by the fund are fundamentally driven, bottoms-up, research-intensive stock pickers who use very little, if any, leverage.

(2) Equity and credit market hedge fund - A fund of funds with a mix of directional and nondirectional strategies that include equity long/short, event-driven, relative-value, and global asset allocation. The managers seek equity-like returns that will capture opportunities in up markets while preserving capital in more difficult markets.

(3) Three private equity funds broadly diversified across managers, investment stages, geography, industry sectors, and company size.

(4) Investment in private property funds broadly classified as core, value-added, and opportunistic.

The tables above present information about the pension and postretirement benefit plan assets measured at fair value at December 31, 2017 and 2016 and the valuation techniques used by the System to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the System has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The System's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each plan asset.

Genesis HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2017 and 2016

Note 14 - Pension and Other Postretirement Benefit Plans (Continued)

Cash Flow

Contributions

The System expects to contribute \$3,150,000 to its pension plan in 2018.

Estimated Future Benefit Payments

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

Years Ending December 31	Pension Benefits
2018	\$ 5,125,383
2019	5,389,960
2020	5,446,814
2021	5,924,664
2022	6,009,518
2023-2027	32,181,234

Note 15 - Changes in Consolidated Unrestricted Net Assets Attributable to the System and the Noncontrolling Interest

The changes in consolidated unrestricted net assets attributable to the System and the noncontrolling interest were as follows:

	Controlling Interest	Noncontrolling Interest	Total
Balance at December 31, 2015	\$ 193,513,040	\$ 1,375,217	\$ 194,888,257
Excess of revenue over expenses	6,352,276	98,978	6,451,254
Capital distributions	-	(326,767)	(326,767)
Pension-related changes other than net periodic cost	(1,977,947)	-	(1,977,947)
Net assets released from restriction for capital equipment	3,669,901	-	3,669,901
Balance at December 31, 2016	201,557,270	1,147,428	202,704,698
Excess of revenue over expenses	17,619,822	82,966	17,702,788
Capital distributions	-	(411,999)	(411,999)
Pension-related changes other than net periodic cost	4,473,538	-	4,473,538
Net assets released from restriction for capital equipment	858,842	-	858,842
Balance at December 31, 2017	<u>\$ 224,509,472</u>	<u>\$ 818,395</u>	<u>\$ 225,327,867</u>

Additional Information

Genesis HealthCare System and Subsidiaries

Consolidating Balance Sheet

December 31, 2017

	Genesis HealthCare System	CareServe	CareLife, Inc. and Subsidiaries	Genesis HealthCare Foundation	Obligated Eliminating Entries	Total Obligated Group	Community Ambulance Service	Southeast Ohio Medical Insurance Company, Ltd.	Eliminating Entries	Total
Assets										
Current Assets										
Cash and cash equivalents	\$ 19,615,570	\$ 261,640	\$ 10,561,697	\$ 522,318	\$ -	\$ 30,961,225	\$ 1,180,753	\$ 57,991	\$ -	\$ 32,199,969
Accounts receivable	54,653,655	(15,000)	11,266,064	-	-	65,904,719	529,936	1,188,799	(1,188,799)	66,434,655
Inventory	5,402,928	-	4,452,923	-	-	9,855,851	-	-	-	9,855,851
Other assets	25,079,085	60,203	4,052,401	2,262,676	(12,206,990)	19,247,375	274,954	12,883	(10,215,060)	9,320,152
Total current assets	104,751,238	306,843	30,333,085	2,784,994	(12,206,990)	125,969,170	1,985,643	1,259,673	(11,403,859)	117,810,627
Assets Limited as to Use	135,633,920	1,211,358	412,495	39,040,157	-	176,297,930	1,123,977	16,539,393	-	193,961,300
Property and Equipment - Net	301,449,225	-	5,720,612	162,359	-	307,332,196	1,007,498	-	-	308,339,694
Beneficial Interest in Perpetual Trusts	-	-	-	14,498,896	-	14,498,896	-	-	-	14,498,896
Other Assets										
Long-term investments	3,273,954	-	346,862	-	-	3,620,816	-	-	(2,941,422)	679,394
Other noncurrent assets	3,099,034	-	100,000	142,933	-	3,341,967	-	-	-	3,341,967
Total assets	<u>\$ 548,207,371</u>	<u>\$ 1,518,201</u>	<u>\$ 36,913,054</u>	<u>\$ 56,629,339</u>	<u>\$ (12,206,990)</u>	<u>\$ 631,060,975</u>	<u>\$ 4,117,118</u>	<u>\$ 17,799,066</u>	<u>\$ (14,345,281)</u>	<u>\$ 638,631,878</u>

Genesis HealthCare System and Subsidiaries

Consolidating Balance Sheet (Continued)

December 31, 2017

	Genesis HealthCare System	CareServe	CareLife, Inc. and Subsidiaries	Genesis HealthCare Foundation	Obligated Eliminating Entries	Total Obligated Group	Community Ambulance Service	Southeast Ohio Medical Insurance Company, Ltd.	Eliminating Entries	Total
Liabilities and Net Assets										
Current Liabilities										
Accounts payable	\$ 11,181,090	\$ 1	\$ 5,750,389	\$ 24,523	\$ -	\$ 16,956,003	\$ 115,606	\$ 757,877	\$ (357,404)	\$ 17,472,082
Current portion of long-term debt	3,755,000	-	-	-	-	3,755,000	-	-	-	3,755,000
Estimated third-party payor settlements	3,389,385	-	-	-	-	3,389,385	-	-	-	3,389,385
Accrued liabilities and other:										
Accrued compensation	17,763,626	802	9,457,465	-	-	27,221,893	300,422	-	-	27,522,315
Other accrued liabilities	9,204,715	61,354	9,122,906	-	(12,206,990)	6,181,985	273,737	11,725,189	(11,046,455)	7,134,456
Total current liabilities	45,293,816	62,157	24,330,760	24,523	(12,206,990)	57,504,266	689,765	12,483,066	(11,403,859)	59,273,238
Long-term Debt - Net of current portion	287,941,989	-	-	-	-	287,941,989	-	-	-	287,941,989
Other Liabilities										
Pension and other postretirement obligations	35,430,217	-	-	-	-	35,430,217	-	-	-	35,430,217
Deferred revenue	3,850,051	-	-	-	-	3,850,051	-	-	-	3,850,051
Accrued professional liability	1,659,707	-	-	-	-	1,659,707	-	5,196,000	-	6,855,707
Total liabilities	374,175,780	62,157	24,330,760	24,523	(12,206,990)	386,386,230	689,765	17,679,066	(11,403,859)	393,351,202
Net Assets										
Unrestricted:										
Net assets	174,031,591	1,456,044	12,582,294	36,652,007	-	224,721,936	2,608,958	120,000	(2,941,422)	224,509,472
Noncontrolling interest	-	-	-	-	-	-	818,395	-	-	818,395
Temporarily restricted	-	-	-	1,967,960	-	1,967,960	-	-	-	1,967,960
Permanently restricted	-	-	-	17,984,849	-	17,984,849	-	-	-	17,984,849
Total net assets	174,031,591	1,456,044	12,582,294	56,604,816	-	244,674,745	3,427,353	120,000	(2,941,422)	245,280,676
Total liabilities and net assets	<u>\$ 548,207,371</u>	<u>\$ 1,518,201</u>	<u>\$ 36,913,054</u>	<u>\$ 56,629,339</u>	<u>\$ (12,206,990)</u>	<u>\$ 631,060,975</u>	<u>\$ 4,117,118</u>	<u>\$ 17,799,066</u>	<u>\$ (14,345,281)</u>	<u>\$ 638,631,878</u>

Genesis HealthCare System and Subsidiaries

Consolidating Statement of Operations and Changes in Unrestricted Net Assets

Year Ended December 31, 2017

	Genesis HealthCare System	CareServe	CareLife, Inc. and Subsidiaries	Genesis HealthCare Foundation	Obligated Eliminating Entries	Total Obligated Group	Community Ambulance Service	Southeast Ohio Medical Insurance Company, Ltd.	Eliminating Entries	Total
Unrestricted Revenue, Gains, and Other Support										
Net patient service revenue	\$ 390,680,265	\$ -	\$ 62,497,558	\$ -	\$ -	\$ 453,177,823	\$ 4,850,530	\$ -	\$ -	\$ 458,028,353
Less provision for bad debts	(11,045,110)	-	(4,018,009)	-	-	(15,063,119)	(248,609)	-	-	(15,311,728)
Net patient service revenue less provision for bad debts	379,635,155	-	58,479,549	-	-	438,114,704	4,601,921	-	-	442,716,625
Pharmacy sales and other	18,810,836	572,897	63,418,975	1,023,082	(6,822,536)	77,003,254	971,645	1,205,376	(1,144,131)	78,036,144
Total unrestricted revenue, gains, and other support	398,445,991	572,897	121,898,524	1,023,082	(6,822,536)	515,117,958	5,573,566	1,205,376	(1,144,131)	520,752,769
Expenses										
Salaries and wages	122,747,809	466,747	81,809,730	233,227	-	205,257,513	2,564,698	-	-	207,822,211
Employee benefits and payroll taxes	42,471,258	70,332	8,146,692	-	-	50,688,282	800,342	-	-	51,488,624
Operating supplies and expenses	72,498,248	1,925	3,572,556	9,917	(1,129,690)	74,952,956	323,797	-	-	75,276,753
Professional services and consultant fees	15,884,849	-	5,137,206	-	-	21,022,055	18,500	-	-	21,040,555
Purchased services	35,341,526	25,588	9,771,645	174,540	(1,071,368)	44,241,931	612,982	148,556	(895,232)	44,108,237
Utilities	4,775,385	8,236	1,316,354	3,089	-	6,103,064	94,666	5,159	-	6,202,889
Repairs, rentals, insurance, and other	29,380,150	33,211	8,864,747	760,644	-	39,038,752	648,343	1,051,661	-	40,738,756
Pharmacy cost of goods sold	-	-	40,686,573	-	(4,621,478)	36,065,095	1,099	-	-	36,066,194
Depreciation	21,441,991	1,146	933,850	9,506	-	22,386,493	352,477	-	-	22,738,970
Interest expense	14,562,458	-	1,712	-	-	14,564,170	-	-	-	14,564,170
Total expenses	359,103,674	607,185	160,241,065	1,190,923	(6,822,536)	514,320,311	5,416,904	1,205,376	(895,232)	520,047,359
Operating Income (Loss)	39,342,317	(34,288)	(38,342,541)	(167,841)	-	797,647	156,662	-	(248,899)	705,410
Other Income (Loss)										
Investment income	4,954,681	56,033	7,559	1,682,006	-	6,700,279	60,552	-	-	6,760,831
Unrealized gains on trading securities	8,836,183	99,074	45,258	3,373,056	-	12,353,571	83,366	-	-	12,436,937
Other	(2,228,702)	-	(2,973)	-	-	(2,231,675)	31,285	-	-	(2,200,390)
Total other income	11,562,162	155,107	49,844	5,055,062	-	16,822,175	175,203	-	-	16,997,378
Excess of Revenue Over (Under) Expenses	50,904,479	120,819	(38,292,697)	4,887,221	-	17,619,822	331,865	-	(248,899)	17,702,788
Capital Distributions	-	-	-	-	-	-	(1,648,000)	-	1,236,001	(411,999)
Transfer (to) from Affiliate	(38,177,652)	-	40,268,671	(2,091,019)	-	-	-	-	-	-
Pension-related Changes Other than Net Periodic Cost	4,473,538	-	-	-	-	4,473,538	-	-	-	4,473,538

Genesis HealthCare System and Subsidiaries

Consolidating Statement of Operations and Changes in Unrestricted Net Assets (Continued)

Year Ended December 31, 2017

	Genesis HealthCare System	CareServe	CareLife, Inc. and Subsidiaries	Genesis HealthCare Foundation	Obligated Eliminating Entries	Total Obligated Group	Community Ambulance Service	Southeast Ohio Medical Insurance Company, Ltd.	Eliminating Entries	Total
Net Assets Released from Restriction for Capital Equipment	\$ -	\$ -	\$ -	\$ 858,842	\$ -	\$ 858,842	\$ -	\$ -	\$ -	\$ 858,842
Increase (Decrease) in Unrestricted Net Assets	<u>\$ 17,200,365</u>	<u>\$ 120,819</u>	<u>\$ 1,975,974</u>	<u>\$ 3,655,044</u>	<u>\$ -</u>	<u>\$ 22,952,202</u>	<u>\$ (1,316,135)</u>	<u>\$ -</u>	<u>\$ 987,102</u>	<u>\$ 22,623,169</u>

Report on Internal Control Over Financial
Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements
Performed in Accordance with *Government
Auditing Standards*

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Independent Auditor's Report

To Management and the Board of Directors
Genesis HealthCare System and Subsidiaries

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Genesis HealthCare System and Subsidiaries (the "System"), which comprise the consolidated balance sheet as of December 31, 2017 and the related consolidated statements of operations, changes in net assets, and cash flows for the year then ended, and the related notes to the consolidated financial statements and have issued our report thereon dated March 13, 2018. Our report includes a reference to other auditors who audited the financial statements of Genesis HealthCare Foundation, as described in our report on the Genesis HealthCare System and Subsidiaries' consolidated financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of Genesis HealthCare Foundation were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

To Management and the Board of Directors
Genesis HealthCare System and Subsidiaries

Purpose of this Report

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

Plante & Moran, PLLC

March 13, 2018