

Hutchinson Regional Medical Center, Inc.

Independent Auditor's Report and Consolidated Financial Statements

June 30, 2019 and 2018

Hutchinson Regional Medical Center, Inc.
June 30, 2019 and 2018

Contents

Independent Auditor’s Report.....1

Consolidated Financial Statements

Balance Sheets 3
Statements of Operations 4
Statements of Changes in Net Assets..... 5
Statements of Cash Flows 6
Notes to Consolidated Financial Statements..... 8

Supplementary Information

Consolidating Schedule – Balance Sheet..... 42
Consolidating Schedule – Statement of Operations..... 44
Consolidating Schedule – Statement of Changes in Net Assets 45

Independent Auditor's Report

Board of Directors
Hutchinson Regional Medical Center, Inc.
Hutchinson, Kansas

We have audited the accompanying consolidated financial statements of Hutchinson Regional Medical Center, Inc., which comprise the consolidated balance sheets as of June 30, 2019 and 2018, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Hutchinson Regional Medical Center, Inc. as of June 30, 2019 and 2018, and the results of its operations, the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in *Note 17* to the consolidated financial statements, in 2019, Hutchinson Regional Medical Center, Inc. adopted ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. Our opinion is not modified with respect to this matter.

Other Matter

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The Consolidating Schedule – Balance Sheet, Consolidating Schedule – Statement of Operations and Consolidating Schedule – Statement of Changes in Net Assets listed in the table of contents are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the 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, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

BKD, LLP

Wichita, Kansas
November 15, 2019

Hutchinson Regional Medical Center, Inc.
Consolidated Balance Sheets
June 30, 2019 and 2018

Assets

	<u>2019</u>	<u>2018</u>
Current Assets		
Cash and cash equivalents	\$ 25,104,764	\$ 23,080,570
Assets limited as to use, current	2,029,715	1,902,146
Funds held on deposit with the Hutchinson Regional Medical Foundation	7,352,127	6,930,640
Patient accounts receivable, net of 2018 allowance of \$25,116,791	33,045,913	31,723,444
Other receivables	1,528,154	1,853,579
Net investment in direct financing leases	1,265,713	1,191,934
Supplies	4,990,757	5,533,324
Prepaid expenses and other	<u>3,265,717</u>	<u>3,576,386</u>
Total current assets	<u>78,582,860</u>	<u>75,792,023</u>
Assets Limited As To Use		
Internally designated		
For capital improvements	26,242,276	25,002,472
For self-funded employee health, workers' compensation and professional liability insurance	6,679,450	6,499,872
Interests in net assets of foundations	<u>29,560,454</u>	<u>30,114,701</u>
	62,482,180	61,617,045
Less amount required to meet current obligations	<u>2,029,715</u>	<u>1,902,146</u>
	<u>60,452,465</u>	<u>59,714,899</u>
Property and Equipment, Net	<u>96,914,972</u>	<u>94,711,327</u>
Other Assets		
Net investment in direct financing leases	15,078,764	16,142,660
Long-term investments	62,222,367	71,641,642
Deposits	<u>24,456</u>	<u>24,465</u>
	<u>77,325,587</u>	<u>87,808,767</u>
Total assets	<u>\$ 313,275,884</u>	<u>\$ 318,027,016</u>

Liabilities and Net Assets

	<u>2019</u>	<u>2018</u>
Current Liabilities		
Outstanding checks in excess of bank balance	\$ -	\$ 59,566
Current maturities of long-term debt	815,000	785,000
Current maturities of capital lease obligations	58,559	57,831
Accounts payable	7,386,190	9,595,958
Accrued expenses	10,348,928	9,411,792
Deferred revenue	10,101	1,724
Estimated amounts due to third-party payers	<u>3,198,406</u>	<u>1,992,204</u>
 Total current liabilities	 21,817,184	 21,904,075
 Long-term Debt, Net	 34,650,122	 35,485,184
 Capital Lease Obligations	 <u>30,545</u>	 <u>90,643</u>
 Total liabilities	 <u>56,497,851</u>	 <u>57,479,902</u>
 Net Assets		
Without donor restrictions		
Undesignated	<u>228,616,515</u>	<u>231,728,115</u>
With donor restrictions		
Purpose restrictions	28,110,912	28,768,393
Perpetual in nature	<u>50,606</u>	<u>50,606</u>
	<u>28,161,518</u>	<u>28,818,999</u>
 Total net assets	 <u>256,778,033</u>	 <u>260,547,114</u>
 Total liabilities and net assets	 <u><u>\$ 313,275,884</u></u>	 <u><u>\$ 318,027,016</u></u>

Hutchinson Regional Medical Center, Inc.
Consolidated Statements of Operations
Years Ended June 30, 2019 and 2018

	2019	2018
Unrestricted Revenues, Gains and Other Support		
Net patient service revenue		\$ 162,674,213
Provision for uncollectible accounts		25,224,131
Net patient service revenue less provision for uncollectible accounts	\$ 142,717,904	137,450,082
Electronic health records incentive	-	35,491
Other	9,101,960	7,466,991
Net assets released from restriction used for operations	5,617	1,903
Total unrestricted revenues, gains and other support	151,825,481	144,954,467
Expenses and Losses		
Salaries and wages	61,770,055	58,131,099
Employee benefits	18,616,975	15,674,877
Purchased services, supplies and other	69,656,069	67,471,527
Depreciation	11,259,710	8,425,113
Income tax expense	91,200	46,000
Interest	1,645,851	140,719
Total expenses and losses	163,039,860	149,889,335
Operating Loss	(11,214,379)	(4,934,868)
Other Income (Expense)		
Investment return, net	5,271,709	5,754,484
Contributions received	762,800	335,526
Insurance recoveries	-	89,132
Other	56,270	(330,929)
Total other income	6,090,779	5,848,213
Excess (Deficiency) of Revenues Over Expenses	(5,123,600)	913,345
Net assets released from restriction used for purchase of property and equipment	2,012,000	4,000,000
Increase (Decrease) in Net Assets Without Donor Restrictions	\$ (3,111,600)	\$ 4,913,345

Hutchinson Regional Medical Center, Inc.
Consolidated Statements of Changes in Net Assets
Years Ended June 30, 2019 and 2018

	2019	2018
Net Assets Without Donor Restrictions		
Excess (deficiency) of revenues over expenses	\$ (5,123,600)	\$ 913,345
Net assets released from restriction used for purchase of property and equipment	2,012,000	4,000,000
Increase (decrease) in net assets without donor restrictions	(3,111,600)	4,913,345
Net Assets With Donor Restrictions		
Investment return, net	4,239	3,318
Contributions received	2,012,000	4,024,702
Change in interests in net assets of foundations	(656,103)	(1,939,548)
Net assets released from restrictions used for operations	(5,617)	(1,903)
Net assets released from restrictions used for purchase of property and equipment	(2,012,000)	(4,000,000)
Decrease in net assets with donor restrictions	(657,481)	(1,913,431)
Change in Net Assets	(3,769,081)	2,999,914
Net Assets, Beginning of Year	260,547,114	257,547,200
Net Assets, End of Year	\$ 256,778,033	\$ 260,547,114

Hutchinson Regional Medical Center, Inc.
Consolidated Statements of Cash Flows
Years Ended June 30, 2019 and 2018

	2019	2018
Operating Activities		
Change in net assets	\$ (3,769,081)	\$ 2,999,914
Items not requiring (providing) operating cash flow		
Loss on disposal of property and equipment	846	175,429
Depreciation	11,259,710	8,425,113
Amortization of bond issuance costs and bond premium	(20,062)	(20,043)
Provision for uncollectible accounts	-	25,224,131
Restricted contributions and investment income	(2,016,239)	(4,028,020)
Net assets released from restriction used for purchase of property and equipment	(2,012,000)	(4,000,000)
Net realized and unrealized gains on trading securities	(2,550,705)	(3,554,916)
Change in interests in net assets of foundations	656,103	1,939,548
Changes in		
Patient accounts receivable	(1,322,469)	(22,916,561)
Other receivables	325,425	(656,912)
Supplies	542,567	(441,893)
Prepaid expenses and other	310,678	(605,551)
Estimated amounts due from and to third-party payers	1,206,202	1,173,767
Accounts payable	(827,339)	1,215,643
Accrued expenses	937,136	399,019
Other liabilities	8,377	(1,247)
	<u>2,729,149</u>	<u>5,327,421</u>
Net cash provided by operating activities		
Investing Activities		
Purchase of investments	(1,419,382)	(1,937,674)
Proceeds from disposition of investments	11,868,124	16,748,581
Change in funds held on deposit with the Hutchinson Regional Medical Foundation	(421,487)	(537,090)
Purchase of property and equipment	(14,879,785)	(38,203,704)
Proceeds from disposal of property and equipment	33,155	130,636
Principal payments received on leases	1,265,047	1,197,521
Direct financing leases funded	(274,930)	(42,170)
Proceeds from disposition of leased assets	-	2,225
	<u>(3,829,258)</u>	<u>(22,641,675)</u>
Net cash used in investing activities		

Hutchinson Regional Medical Center, Inc.
Consolidated Statements of Cash Flows (Continued)
Years Ended June 30, 2019 and 2018

	2019	2018
Financing Activities		
Outstanding checks in excess of bank balance	\$ (59,566)	\$ 59,566
Proceeds from restricted contributions and investment income	2,016,239	4,028,020
Principal payments on long-term debt	(785,000)	(720,000)
Principal payments on capital lease obligations	(59,370)	(52,408)
Net assets released from restrictions used for purchase of property and equipment	2,012,000	4,000,000
Net cash provided by financing activities	3,124,303	7,315,178
Increase (Decrease) in Cash and Cash Equivalents	2,024,194	(9,999,076)
Cash and Cash Equivalents, Beginning of Year	23,080,570	33,079,646
Cash and Cash Equivalents, End of Year	\$ 25,104,764	\$ 23,080,570
Supplemental Cash Flows Information		
Purchases of property and equipment in accounts payable	\$ 328,841	\$ 2,618,536
Interest paid (net of amount capitalized)	\$ 1,665,913	\$ 160,762
Income taxes paid	\$ 201,780	\$ 240,000

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

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

Nature of Operations

Hutchinson Regional Medical Center, Inc. (Medical Center) is a Kansas not-for-profit membership corporation organized for the purpose of owning and operating a health care facility located in Hutchinson, Kansas. The Medical Center is the sole member or sole shareholder of the following corporations:

Not-for-profit

Horizons Mental Health Center, Inc. (HMHC)

Main Line, Inc. (Main Line)

Hospice of Reno County, Inc. (HoRC)

For profit

Hutchinson Health Care Services, Inc. (HHCSI)

Hutchinson Regional Medical Foundation (Foundation), a related party, is a not-for-profit organization whose mission and principal activities are to benefit and support the Medical Center and its not-for-profit, tax-exempt affiliates. Affiliates of the Medical Center that qualify to receive funding are HMHC and HoRC. The Foundation's revenues and other support are derived principally from donor contributions and investment income.

Principles of Consolidation

The consolidated financial statements of Hutchinson Regional Medical Center, Inc. (Healthcare System) include the accounts of the Medical Center and its wholly-owned or controlled corporate entities. All of the corporate entities in the Healthcare System were organized under the laws of the State of Kansas and are under common control and management. Significant intercompany accounts and transactions have been eliminated.

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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents

The Healthcare System considers all liquid investments with original maturities of three months or less to be cash equivalents, except for assets limited as to use by either Board designation or other arrangements. At June 30, 2019 and 2018, cash equivalents consisted primarily of money market accounts with brokers and certificates of deposit.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

At June 30, 2019, the Healthcare System's cash accounts, including assets limited as to use by either Board designation or other arrangements, exceeded federally insured limits by approximately \$34,830,000.

Assets Limited As To Use

Assets limited as to use include (1) assets set aside by the Board of Directors (Board) for future capital improvements over which the Board retains control and may at its discretion subsequently use for other purposes, (2) assets set aside by the Board under self-insurance arrangements for employee health, workers' compensation and professional liability insurance, and (3) beneficial interest in net assets of the Foundation and Hutchinson Community Foundation (HCF). Amounts required to meet current liabilities of the Healthcare System are included in current assets. Investments held within assets limited as to use are trading securities.

Funds Held on Deposit with the Hutchinson Regional Medical Foundation

Funds held on deposit are managed by the Foundation in a pooled investment account in order to maximize investment returns. The Foundation has agreed to pay interest on these funds at the Foundation's average rate of return on its pooled investment portfolio. The funds are due on demand without any limitations on withdrawals. Interest in the Foundation investment pool is valued based on estimates of the net asset value of the investment pool as provided by the Foundation.

Patient Accounts Receivable

Patient accounts receivable reflects the outstanding amount of consideration to which the Healthcare System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payers (including health insurers and government programs) and others. As a service to the patient, the Healthcare System bills third-party payers directly and bills the patient when the patient's responsibility for co-pays, coinsurance and deductibles is determined. Patient accounts receivable are due in full when billed.

Net Investment in Direct Financing Leases

Main Line leases substantially all of its assets to local physician groups or other related health care entities. It has also constructed buildings and acquired equipment, most which are leased. The majority of the leases are accounted for as direct financing leases and are based upon the original cost of the asset.

Net investment in direct financing leases are reported at their outstanding unpaid principal balances. Interest income is accrued on the unpaid principal balance. Main Line charges off leases when collection of interest or principal becomes doubtful. There were no leases charged off during the years ended June 30, 2019 and 2018.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Supplies

The Healthcare System states supply inventories at the lower of cost, determined using the first-in, first-out method, or net realizable value.

Interests in Net Assets of Foundations

The Healthcare System and the Foundation are financially interrelated organizations. The Foundation seeks private support for and holds net assets on behalf of the Healthcare System. The Healthcare System accounts for its interest in the net assets of the Foundation (Interest) in a manner similar to the equity method. Changes in the Interest are included in change in net assets. Transfers of assets between the Foundation and the Healthcare System are recognized as increases or decreases in the Interest.

The Healthcare System is also the beneficiary of funds held by HCF. The Healthcare System recognizes as an asset its interest in the net assets held by HCF for the benefit of the Healthcare System and adjusts this interest for changes in the net assets held by HCF occurring during the reporting period.

Property and Equipment

Property and equipment acquisitions are recorded at cost and are depreciated using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives.

The estimated useful lives for each major depreciable classification of property and equipment are as follows:

Land improvements	4-20 years
Buildings	5-40 years
Equipment	3-15 years
Leasehold improvements	4-12 years

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

The Healthcare System capitalizes interest costs as a component of construction in progress, based on interest costs of borrowing specifically for the project, net of interest earned on investments acquired with the proceeds of the borrowing. Total interest capitalized and incurred was:

	2019	2018
Total interest expense incurred on borrowings for project	\$ 248,240	\$ 1,640,516
Interest income from investment of proceeds of borrowings for project	(26,896)	(44,551)
Net interest cost capitalized	\$ 221,344	\$ 1,595,965
Interest capitalized	\$ 221,344	\$ 1,595,965
Interest charged to expense	1,645,851	140,719
Total interest incurred	\$ 1,867,195	\$ 1,736,684

Long-lived Asset Impairment

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

No asset impairment was recognized for the years ended June 30, 2019 and 2018.

Equity Investments

The Healthcare System measures equity securities, other than investments that qualify for the equity method of accounting, at fair value with changes recognized within other income (expense) in the accompanying consolidated statements of operations. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method. Investments, other than investments that qualify for the equity method of accounting, are trading securities.

Transfers Between Fair Value Hierarchy Levels

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

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Debt Issuance Costs

Debt issuance costs represent costs incurred in connection with the issuance of long-term debt. The Healthcare System records these costs as direct deductions from the related debt. Such costs are being amortized over the term of the respective debt using the straight-line method and are included as a component of interest expense.

Debt Premium

The Healthcare System records debt premiums as direct additions to the related debt. Such premiums are being amortized over the term of the respective debt using the straight-line method and are included as a component of interest expense.

Net Assets

Net assets, revenues, gains and losses are classified based on the existence or absence of donor restrictions. Net assets without donor restrictions are available for use in general operations and not subject to donor restrictions. The governing board has designated, from net assets without donor restrictions, net assets for future capital improvements and for future self-funded employee health, workers' compensation and professional liability insurance claims. Net assets with donor restrictions are subject to donor restrictions. Some restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity.

Patient Service Revenue

Patient service revenue is recognized as the Healthcare System satisfies performance obligations under its contracts with patients. Patient service revenue is reported at the estimated transaction price or amount that reflects the consideration to which the Healthcare System expects to be entitled in exchange for providing patient care. The Healthcare System determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payers, discounts provided to uninsured patients in accordance with the Healthcare System's policies and implicit price concessions provided to uninsured patients.

The Healthcare System determines its estimates of explicit price concessions which represent adjustments and discounts based on contractual agreements, its discount policies and historical experience by payer groups. The Healthcare System determines its estimate of implicit price concessions based on its historical collection experience by classes of patients. The estimated amounts also include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews and investigations by third-party payers.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Charity Care

The Healthcare System provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Healthcare System does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as patient service revenue. The Healthcare System's direct and indirect costs for services and supplies furnished under the Healthcare System's charity care policy totaled approximately \$798,000 and \$848,000 in 2019 and 2018, respectively. Costs were calculated using the overall cost-to-charge ratio from the June 30, 2018 and 2017, filed Medicare cost reports, respectively. The June 30, 2019, Medicare cost report was not yet filed as of the date the consolidated financial statements were issued.

Electronic Health Records Incentive Program

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

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

The Healthcare System has recorded revenue of \$0 and \$35,491 for 2019 and 2018, respectively, which is included in electronic health records incentive within unrestricted revenues, gains and other support in the consolidated statements of operations.

County Tax Support

HMHC receives tax support from a portion of property taxes assessed and levied by Barber, Harper, Pratt, Reno and Kingman counties in Kansas. The funds were used to support operations. County tax revenue is recognized in the period in which the funds are received from the various counties and is included in unrestricted revenues, gains and other support as other revenue in the accompanying consolidated statements of operations.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Self-insurance

The Healthcare System self-insures its medical and dental benefits for all eligible employees and dependents and is funded by both employer and employee contributions. The Healthcare System contracts with third-party administrators to provide claims management services. The Healthcare System purchases third-party insurance coverage for certain excess claims and accrues a liability for settling reported and unreported claims as of the balance sheet date.

The Healthcare System also self-insures a portion of its workers' compensation and professional liability claims risk and accrues a liability for the estimated cost of settling all reported and unreported claims as of the balance sheet date. The Healthcare System contracts with third-party administrators to provide claims management services. The Healthcare System has commercial stop-loss coverage through third-party insurance companies which provides additional coverage for workers' compensation and professional liability claims.

As a requirement for being self-funded for workers' compensation in the State of Kansas, the Healthcare System has specifically designated a letter of credit of \$1,896,000,000 and \$2,209,000 in 2019 and 2018, respectively, by naming the Kansas Department of Labor – Division of Workers' Compensation as the beneficiary. There have been no draws against the letter of credit to date.

Professional Liability Claims

The Healthcare System recognizes an accrual for claim liabilities based on estimated ultimate losses and costs associated with settling claims and a receivable to reflect the estimated insurance recoveries, if any. Professional liability claims are described more fully in *Note 9*.

Income Taxes

The Medical Center and its not-for-profit affiliates have been recognized as exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and a similar provision of state law. However, the Healthcare System is subject to federal income tax on any unrelated business taxable income. HHCSI is a taxable corporation which pays taxes at prevailing corporate rates.

The Healthcare System files tax returns in the U.S. federal jurisdiction.

Net Investment Return

Investment return includes dividend and interest income; realized and unrealized gains and losses on investments carried at fair value; less external and direct internal investment expenses.

Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year is included in net assets without donor restrictions. Other investment return is reflected in the consolidated statements of operations and changes in net assets as with or without donor restrictions based upon the existence and nature of any donor or legally imposed restrictions.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Contributions

Contributions are provided to the Healthcare System either with or without restrictions placed on the gift by the donor. Revenues and net assets are separately reported to reflect the nature of those gifts – with or without donor restrictions. The value recorded for each contribution is recognized as follows:

Nature of the Gift	Value Recognized
<i>Conditional gifts, with or without restriction</i>	
Gifts that depend on the Healthcare System overcoming a donor imposed barrier to be entitled to the funds	Not recognized until the gift becomes unconditional, <i>i.e.</i> the donor imposed barrier is met
<i>Unconditional gifts, with or without restriction</i>	
Received at date of gift – cash and other assets	Fair value
Received at date of gift – property, equipment and long-lived assets	Estimated fair value
Expected to be collected within one year	Net realizable value
Collected in future years	Initially reported at fair value determined using the discounted present value of estimated future cash flows technique

In addition to the amount initially recognized, revenue for unconditional gifts to be collected in future years is also recognized each year as the present-value discount is amortized using the level-yield method.

When a donor stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statements of operations as net assets released from restrictions. Absent explicit donor stipulations for the period of time that long-lived assets must be held, expirations of restrictions for gifts of land, buildings, equipment and other long-lived assets are reported when those assets are placed in service.

Gifts and investment income that are originally restricted by the donor and for which the restriction is met in the same time period the gift is received are recorded as revenue with donor restrictions and then released from restriction.

Conditional contributions and investment income having donor stipulations which are satisfied in the gift is received and the investment income is earned are recorded as revenue with donor restrictions and then released from restriction.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Excess (Deficiency) of Revenues Over Expenses

The consolidated statements of operations include excess (deficiency) of revenues over expenses. Changes in net assets without donor restrictions which are excluded from excess (deficiency) of revenues over expenses, consistent with industry practice, include contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets).

Revisions

Certain immaterial revisions have been made to the 2018 consolidated financial statements for the change in classification of the Healthcare System's investments portfolio and the related classification of unrealized gains and losses associated with those investments. These revisions did not have a significant impact on the consolidated financial statement line items impacted.

Note 2: Patient Service Revenue

Patient service revenue is reported at the amount that reflects the consideration to which the Healthcare System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payers (including health insurers and government programs) and others and includes variable consideration for retroactive revenue adjustments due to settlement of audits, reviews and investigations. Generally, the Healthcare System bills the patients and third-party payers several days after the services are performed or the patient is discharged from the facility and patient accounts receivable are due in full when billed. Revenue is recognized as performance obligations are satisfied.

Performance Obligations

Performance obligations are determined based on the nature of the services provided by the Healthcare System. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected charges. The Healthcare System believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in the Healthcare System receiving outpatient mental health services. The Healthcare System measures the performance obligation from the commencement of an outpatient service, to the point when it is no longer required to provide services to that patient, which is generally at the completion of the outpatient services. Revenue for performance obligations satisfied at a point in time is generally recognized when goods are provided to its patients and customers in a retail setting (for example, pharmaceuticals) and the Healthcare System does not believe it is required to provide additional goods related to the patient.

Hutchinson Regional Medical Center, Inc.

Notes to Consolidated Financial Statements

June 30, 2019 and 2018

Because all of its performance obligations relate to contracts with a duration of less than one year, the Healthcare System has elected to apply the optional exemption provided in FASB ASC 606-10-50-14(a) and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

Transaction Price

The Healthcare System determines the transaction price based on standard charges for goods and services provided, reduced by explicit price concessions which consist of contractual adjustments provided to third-party payers, discounts provided to uninsured patients in accordance with the Healthcare System's policy and implicit price concessions provided to uninsured patients. The Healthcare System determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies and historical experience. The Healthcare System determines its estimate of implicit price concessions based on its historical collection experience with this class of patients.

Third-Party Payers

Agreements with third-party payers typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payers follows:

Medicare. Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The Healthcare System is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Healthcare System and audits thereof by the Medicare administrative contractor.

Medicaid. Inpatient acute care services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. All other services rendered to Medicaid beneficiaries are paid at prospective rates determined on either a per diem or a fee-for-service basis.

The Kansas Medicaid plan includes provisions for a provider assessment program. Under that program, all hospitals, other than critical access hospitals, pay an assessment. The program then distributes the assessments and additional federal monies to Kansas Medicaid providers. Assessments incurred under the program are included in purchased services, supplies and other in the accompanying consolidated statements of operations. Distributions received from the program are included in patient service revenue in the accompanying consolidated statements of operations.

Hutchinson Regional Medical Center, Inc.

Notes to Consolidated Financial Statements

June 30, 2019 and 2018

Other. Payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations provide for payment using prospectively determined rates and discounts from established charges.

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge the Healthcare System's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon the Healthcare System. In addition, the contracts the Healthcare System has with commercial payers also provide for retroactive audit and review of claims.

Settlements with third-party payers for retroactive adjustments due to cost report or other audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payer, correspondence from the payer and the Healthcare System's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known based on newly available information or as years are settled or are no longer subject to such audits, reviews and investigations. Adjustments arising from a change in the transaction price were not significant in 2019 and 2018.

Patient and Uninsured Payers

Generally, patients who are covered by third-party payers are responsible for related deductibles and coinsurance, which vary in amount. The Healthcare System also provides services to uninsured patients and offers those uninsured patients a discount, either by policy or law, from standard charges. The Healthcare System estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts and implicit price concessions based on historical collection experience. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. For the years ended June 30, 2019 and 2018, additional revenue of \$1,263,408 and \$1,096,933, respectively, was recognized due to changes in its estimates of implicit price concessions, discounts and contractual adjustments for performance obligations satisfied in prior years. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Consistent with the Healthcare System’s mission, care is provided to patients regardless of their ability to pay. Therefore, the Healthcare System has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances, such as copays and deductibles. The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts the Healthcare System expects to collect based on its collection history with those patients. For the years ended June 30, 2019 and 2018, implicit price concessions were \$26,856,330 and \$25,224,131, respectively.

Patients who meet the Healthcare System’s criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue.

Refund Liabilities

From time to time the Healthcare System will receive overpayments of patient balances from third-party payers or patients resulting in amounts owed back to either the patients or third-party payers. These amounts are excluded from revenues and are recorded as liabilities until they are refunded. As of June 30, 2019 and 2018, the Healthcare System has a liability for refunds to third-party payers and patients recorded of \$2,623,246 and \$1,299,033, respectively.

Revenue Composition

The Healthcare System has determined that the nature, amount, timing and uncertainty of revenue and cash flows are affected by the following factors: payers, and timing of when revenue is recognized. Tables providing details of these factors are presented below.

The composition of patient service revenue by primary payer for the years ended June 30, 2019 and 2018 is as follows:

	<u>2019</u>	<u>2018</u>
Medicare	\$ 60,257,686	\$ 67,644,842
Medicaid	10,019,059	11,757,527
Other third-party payers	67,808,312	52,251,549
Self-pay	<u>4,632,847</u>	<u>5,796,164</u>
Total	<u>\$ 142,717,904</u>	<u>\$ 137,450,082</u>

Revenue from patients’ deductibles and coinsurance are included in the categories presented above based on the primary payer.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

The composition of patient service revenue by consolidated entity and primary payer for the years ended June 30, 2019 and 2018 is as follows:

June 30, 2019					
	Hutchinson Regional Medical Center, Inc.	Hutchinson Health Care Services, Inc.	Hospice of Reno County, Inc.	Horizons Mental Health Center, Inc.	Total
Medicare	\$ 53,003,261	\$ 1,633,043	\$ 4,933,445	\$ 687,937	\$ 60,257,686
Medicaid	2,692,323	146,166	88,462	7,092,108	10,019,059
Other	64,309,800	1,875,995	128,062	1,494,455	67,808,312
Self-pay	4,079,016	116,749	131,409	305,673	4,632,847
	\$ 124,084,400	\$ 3,771,953	\$ 5,281,378	\$ 9,580,173	\$ 142,717,904
June 30, 2018					
	Hutchinson Regional Medical Center, Inc.	Hutchinson Health Care Services, Inc.	Hospice of Reno County, Inc.	Horizons Mental Health Center, Inc.	Total
Medicare	\$ 61,921,161	\$ 980,691	\$ 4,077,617	\$ 665,373	\$ 67,644,842
Medicaid	4,990,292	139,826	262,100	6,365,309	11,757,527
Other	49,043,145	1,683,202	376,718	1,148,484	52,251,549
Self-pay	4,170,681	343,689	550,396	731,398	5,796,164
	\$ 120,125,279	\$ 3,147,408	\$ 5,266,831	\$ 8,910,564	\$ 137,450,082

The composition of patient service revenue and other non-healthcare related services based on timing of revenue recognition for the years ended June 30, 2019 and 2018, are as follows:

	2019	2018
Timing of revenue and recognition		
Health care services transferred over time	\$ 142,717,904	\$ 137,450,082
Various other revenues at a point in time	4,090,677	2,415,297
	\$ 146,808,581	\$ 139,865,379

Other non-healthcare related services revenue in the table above are included in other revenues within unrestricted revenues, gains and other support in the accompanying consolidated statements of operations.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Financing Component

The Healthcare System has elected the practical expedient allowed under FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third party payers for the effects of a significant financing component due to the Healthcare System's expectation that the period between the time the service is provided to a patient and the time the patient or a third-party payer pays for that service will be one year or less.

However, the Healthcare System does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Note 3: Concentration of Credit Risk

Approximately \$34,830,000 of the Healthcare System's bank deposits were in excess of FDIC insurance limits as of June 30, 2019. The Healthcare System also invests funds in repurchase agreements and money market accounts with various banks which are generally collateralized by or invested in U.S. government or other highly liquid securities. The total of these other liquid asset investments was approximately \$9,632,000 as of June 30, 2019. While not insured or guaranteed by the U.S. government, management believes the credit risk related to these other liquid asset investments is minimal.

Main Line's direct financing leases are all either directly with Hutchinson Clinic or indirectly with companies majority-owned by Hutchinson Clinic.

The Healthcare System grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payer agreements. The mix of net receivables from patients and third-party payers at June 30, 2019 and 2018, is:

	<u>2019</u>	<u>2018</u>
Medicare	28%	41%
Medicaid	1%	2%
Commercial	19%	11%
Blue Cross	13%	9%
Private pay	<u>39%</u>	<u>37%</u>
	<u>100%</u>	<u>100%</u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 4: Investments and Investment Return

Assets Limited As To Use

Assets limited as to use at June 30 include:

	2019	2018
Internally Designated for Capital Improvements		
Money market accounts	\$ 1,852,632	\$ 701,939
Equity investments		
Common stock	-	270,418
Mutual funds	15,296,610	13,706,562
International mutual funds	1,365,601	2,281,757
Fixed income investments		
Mortgage	440,097	276,940
Treasury and agencies	338,624	580,490
Certificates of deposit	502,089	-
Asset-backed	141,754	374,971
Municipal bonds	147,539	83,934
Preferred stock	60,159	49,713
International bonds	-	346,443
Tax-exempt general obligations	30,314	29,986
Taxable high yield	115,310	153,237
Bond mutual funds	2,887,440	3,780,272
Corporate bonds	1,679,645	1,331,606
Alternative investments (mutual funds)		
Hedge mutual funds	452,958	499,517
Infrastructure mutual funds	-	255,700
Traded real estate mutual funds	-	87,102
Alternative mutual funds	931,504	191,885
	\$ 26,242,276	\$ 25,002,472

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

	2019	2018
Internally Designated for Self-Funded Employee Health, Workers' Compensation and Professional Liability Insurance		
Money market accounts	\$ 872,231	\$ 1,768,037
Equity investments		
Mutual funds	-	37,844
Fixed income investments		
Treasury and agencies	4,379,205	4,190,639
Certificates of deposit	1,428,014	503,352
	\$ 6,679,450	\$ 6,499,872

Interests in Net Assets of Foundations

Hutchinson Regional Medical Foundation

The Foundation was organized as a separate not-for-profit corporation in 1979, dedicated to the support of the Medical Center and its not-for-profit affiliates. The Medical Center's two predecessor operating entities transferred their interest as beneficiaries in certain estates to the Foundation in 1979. The Foundation's operations are managed by a Board of Directors (separate from the Board of Directors of the Medical Center) comprised of former board members of the Medical Center and its not-for-profit affiliates.

The following is a summary of the assets, liabilities, net assets, revenues, expenses, and changes in net assets of the Foundation as of June 30, 2019 and 2018:

	2019	2018
Cash and investments	\$ 35,605,704	\$ 35,881,461
Other assets	12,548	13,872
	\$ 35,618,252	\$ 35,895,333
Accounts payable	\$ 5,863	\$ 771
Due to related party	-	61,292
Assets held under agency agreement	7,595,282	7,160,060
Net assets	28,017,107	28,673,210
	\$ 35,618,252	\$ 35,895,333

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

	2019	2018
Revenues, Gains and Other Support	\$ 1,737,880	\$ 2,262,712
Expenses and Losses	2,393,983	4,202,260
Change in Net Assets	\$ (656,103)	\$ (1,939,548)

Hutchinson Community Foundation

HoRC transferred assets to HCF to establish the Hospice of Reno County Fund (Fund) and designated HoRC as the beneficiary of the Fund. HCF invests the assets and allocates investment earnings and administration fees to the Fund. HoRC controls any distributions from the Fund as directed by the Board of Directors. The net assets of the Fund at June 30, 2019 and 2018, were \$1,543,347 and \$1,441,491, respectively, and are included in interests in net assets of foundations in the accompanying consolidated balance sheets. The change in the net assets of the Fund for the years ended June 30, 2019 and 2018, was an increase of \$101,856 and a decrease of \$3,662, respectively, and is included in other income (loss) as other in the consolidated statements of operations.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Long-term Investments

Long-term investments at June 30 include:

	<u>2019</u>	<u>2018</u>
Money market accounts	\$ 6,906,670	\$ 5,524,827
Equity investments		
Common stock	5,612,526	3,934,455
Mutual funds	27,747,724	24,845,091
International mutual funds	3,339,525	6,262,471
Fixed income investments		
Mortgage	1,104,647	534,139
Treasury and agencies	2,780,264	11,783,449
Asset-backed	207,887	488,884
Municipal bonds	465,921	122,935
Preferred stock	146,729	121,179
International bonds	10,043	684,775
Tax-exempt general obligations	40,419	39,981
Taxable high yield funds	281,186	348,012
Bond mutual funds	4,655,077	6,910,962
Corporate bonds	5,558,085	6,196,600
Government bonds	-	149,705
Alternative investments (mutual funds)		
Hedge mutual funds	1,107,529	1,218,134
Infrastructure mutual funds	-	623,301
Traded real estate mutual funds	83,874	212,401
Alternative mutual funds	1,340,802	806,882
Investment in HASC	20,000	20,000
Investment in DDC	621,142	621,142
Investment in VHA	192,317	192,317
	<u>\$ 62,222,367</u>	<u>\$ 71,641,642</u>

The Medical Center has a 20% interest in Hutchinson Ambulatory Surgical Center LLC (HASC), a 13.30% interest in DaVita Dialysis Center, formerly Bladon Dialysis, LLC d/b/a Dialysis Center of Hutchinson (DDC), and preferred stock of Voluntary Hospitals of America, Inc. (VHA). The Medical Center accounts for its investment in HASC and DDC under the cost method. The VHA preferred stock will be redeemed by VHA in August 2019 and is carried at its estimated net present value as of June 30, 2019 and 2018, respectively.

The surgical facility's building and equipment are leased from Main Line (see *Note 6*). The net investment in the two leases is \$610,000 and \$802,832 at June 30, 2019 and 2018, respectively. Leasing income for these two leases was \$48,645 and \$67,357 for the years ended June 30, 2019 and 2018, respectively.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Investment Return, Net

Total investment return, net is comprised of the following:

	<u>2019</u>	<u>2018</u>
Interest and dividend income	\$ 2,725,243	\$ 2,202,886
Realized and unrealized gains on trading securities	<u>2,550,705</u>	<u>3,554,916</u>
	<u>\$ 5,275,948</u>	<u>\$ 5,757,802</u>

None of the Healthcare System's individual investment holdings represent 5% or more of the total investments (assets limited as to use and long-term investments) noted above at June 30, 2019.

The following table presents the Healthcare System's individual investment holdings that represent 5% or more of the total investments (assets limited as to use and long-term investments) noted above at June 30, 2018.

Individual Investment Holdings	<u>Fair Value</u>
iShares Core S&P 500 ETF	<u>\$ 5,584,419</u>

Note 5: Property and Equipment

Property and equipment at June 30 are summarized as follows:

	<u>2019</u>	<u>2018</u>
Land	\$ 1,839,225	\$ 1,839,225
Land improvements	5,972,813	4,825,431
Buildings	98,559,920	74,769,796
Equipment	168,341,318	138,133,927
Leasehold improvements	<u>2,137,473</u>	<u>1,579,703</u>
	276,850,749	221,148,082
Less accumulated depreciation	<u>183,222,570</u>	<u>172,192,747</u>
	93,628,179	48,955,335
Construction in progress	<u>3,286,793</u>	<u>45,755,992</u>
Property and equipment, net	<u>\$ 96,914,972</u>	<u>\$ 94,711,327</u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 6: Net Investment in Direct Financing Leases

The master facilities lease entered into during 1998 with Hutchinson Clinic expires June 30, 2028. The lessee may extend the lease for five years beyond any expiration date. The lessee may also purchase the building at fair value at any time. In November 2005, a supplement to the master facilities lease was executed. The supplement lease covers a medical office building completed in March 2006 and expires on March 1, 2036.

The building lease with the ambulatory surgery center expires March 31, 2021. The lessee may extend the lease for five years beyond any expiration date. The lessee may also purchase the building at fair value at any time.

The master equipment lease entered into during 1998 with Hutchinson Clinic expired June 30, 2003. The lessee had exercised options to extend the lease for an additional five-year term which expired on December 31, 2018. There were no further extensions.

The master equipment lease with the ambulatory surgery center expired December 31, 2013. The lessee had exercised its option to extend the lease for another five years which expired December 31, 2018. There were no further extensions.

Monthly payments are adjusted to reflect amounts expended by Main Line for building improvements and equipment acquisitions after inception of the leases. Main Line's net investment in direct financing leases that was used for new building construction, building improvements and equipment acquisitions added to the property subject to these leases, increased by \$274,930 and \$42,170, respectively, during 2019 and 2018.

The following lists the components of the net investment in direct financing leases:

	<u>2019</u>	<u>2018</u>
Total minimum lease payments to be received	\$ 23,231,565	\$ 25,303,377
Unguaranteed equipment residual values	-	26,364
Unearned leasing income	(6,887,088)	(7,995,147)
	<u>16,344,477</u>	<u>17,334,594</u>
Less current maturities	<u>1,265,713</u>	<u>1,191,934</u>
Net investment, excluding current maturities	<u>\$ 15,078,764</u>	<u>\$ 16,142,660</u>

Minimum lease payments to be received during future fiscal years are as follows:

2020	\$ 2,386,537
2021	2,384,066
2022	2,338,725
2023	2,149,103
2024	2,149,103
Thereafter	<u>11,824,031</u>
	<u>\$ 23,231,565</u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 7: Net Investment in Leased Rental Property

Main Line owns an office building located in Hutchinson, Kansas, which is leased to various businesses under operating leases expiring on various dates through 2037. Main Line's net investment in leased rental property is included in *Note 5*.

Main Line's rental income for the years ended June 30, 2019 and 2018, was \$741,071 and \$496,409, respectively, and is included in unrestricted revenues, gains and other support as other in the accompanying consolidated statements of operations. Minimum lease payments to be received during future fiscal years are as follows:

2020	\$ 691,517
2021	634,691
2022	554,724
2023	535,285
2024	493,267
Thereafter	<u>4,887,772</u>
	<u><u>\$ 7,797,256</u></u>

Office space is leased to HMHC and HoRC, both related entities to Main Line through common ownership. Minimum lease payments to be received from HMHC and HoRC during future fiscal years through October 2037 total \$6,445,977.

Note 8: Long-term Debt and Capital Lease Obligations

Long-term debt and capital lease obligations are summarized as follows:

	<u>2019</u>	<u>2018</u>
Series 2016 Revenue Bonds (A)	\$ 35,015,000	\$ 35,800,000
Capital lease obligations (B)	<u>89,104</u>	<u>148,474</u>
	35,104,104	35,948,474
Add: Unamortized debt premium	829,186	866,108
Less: Unamortized debt issuance costs	(379,064)	(395,924)
Less: Current maturities	<u>(873,559)</u>	<u>(842,831)</u>
	<u><u>\$ 34,680,667</u></u>	<u><u>\$ 35,575,827</u></u>

(A) In December 2016, the Medical Center issued Series 2016 Hospital Facilities Revenue Bonds in the amount of \$36,520,000. Principal is payable annually and interest is payable semiannually through 2042. The bonds bear interest at 4% until December 2022, and 5% thereafter until maturity.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

The loan agreement contains various restrictive covenants, including, but not limited to, a minimum required level of days cash on hand of 60 days, a minimum required debt service coverage ratio of 1.20 and restrictions on incurrence of additional debt.

- (B) At a rate of imputed interest at 1.25% due through 2021; collateralized by property and equipment. Property and equipment include the following property under capital leases:

	<u>2019</u>	<u>2018</u>
Equipment	\$ 287,042	\$ 287,042
Less accumulated depreciation	<u>65,240</u>	<u>45,953</u>
	<u>\$ 221,802</u>	<u>\$ 241,089</u>

Scheduled principal repayments on long-term debt and payments on capital lease obligations for the next five years and thereafter are as follows:

	Long-term Debt (Excluding Capital Lease Obligations)	Capital Lease Obligations
2020	\$ 815,000	\$ 59,388
2021	880,000	30,689
2022	940,000	-
2023	980,000	-
2024	1,030,000	-
Thereafter	<u>30,370,000</u>	<u>-</u>
	<u>\$ 35,015,000</u>	90,077
Less amount representing interest		<u>973</u>
Present value of future minimum lease payments		89,104
Less current maturities		<u>58,559</u>
Noncurrent portion		<u>\$ 30,545</u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 9: Professional Liability Claims

The Healthcare System is self-insured for the first \$200,000 per occurrence and \$600,000 in aggregate of medical malpractice risks. The Healthcare System is further covered by the Kansas Health Care Stabilization Fund for claims in excess of the self-insured professional liability plan limits up to \$800,000 pursuant to any one judgment or settlement against it for any one party, subject to an aggregate limitation for all judgments or settlements arising from all claims made in the policy or plan year in the amount of \$2,400,000. The Healthcare System purchases commercial insurance coverage which provides for umbrella liability in excess of the underlying limits set forth above in the amount of \$20,000,000 per occurrence with an aggregate amount in any policy year of \$20,000,000. All coverage is on a claims made basis. Losses from asserted and unasserted claims identified under the Healthcare System's incident reporting system are accrued based on estimates that incorporate the Healthcare System's past experience, as well as other considerations, including the nature of each claim or incident and relevant trend factors. It is reasonably possible that the Healthcare System's estimate of losses will change by a material amount in the near term.

The Healthcare System has established an agency account at a local bank to fund expected future malpractice losses and claims expenses. The agency account is funded based on the findings of an actuary. The balance of the agency accounts, which is included in assets limited as to use, was \$1,349,925 and \$1,670,054 at June 30, 2019 and 2018, respectively. The Healthcare System has included in accrued liabilities an accrual of \$239,000 and \$443,000 at June 30, 2019 and 2018, respectively, for the estimated present value of expected future malpractice losses and claims expenses.

Note 10: Net Assets With Donor Restrictions

Net Assets With Donor Restrictions

Net assets with donor restrictions are available for the following purposes or periods.

	2019	2018
Subject to expenditure for specified purpose		
As directed by the Foundation	\$ 28,017,107	\$ 28,673,210
For Hospice of Reno County services	93,805	95,183
	\$ 28,110,912	\$ 28,768,393
	2019	2018
Not subject to appropriation or expenditure		
Investments to be held in perpetuity, the income is unrestricted	\$ 50,606	\$ 50,606

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Net Assets Released from Restrictions

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of the passage of time or other events specified by donors.

	2019	2018
Purpose restrictions accomplished		
Hospice of Reno County services	\$ 5,617	\$ 1,903
Purchase of equipment	2,012,000	4,000,000
	\$ 2,017,617	\$ 4,001,903

Note 11: Net Assets Without Donor Restrictions

The Healthcare System's governing board has designated, from net assets without donor restrictions, net assets for the following purposes as of June 30:

	2019	2018
Capital improvements	\$ 26,242,276	\$ 25,002,472
Self-funded employee health, workers' compensation and professional liability insurance	8,709,165	8,402,018
	\$ 34,951,441	\$ 33,404,490

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 12: Liquidity and Availability

The Healthcare System's financial assets available within one year of the balance sheet date for general expenditure are:

	<u>2019</u>	<u>2018</u>
Financial assets at year end		
Cash and cash equivalents	\$ 26,242,276	\$ 25,002,472
Assets limited as to use	62,482,180	61,617,045
Funds held on deposit with the Hutchinson Regional Medical Foundation	7,352,127	6,930,640
Patient accounts receivable	33,045,913	31,723,444
Other receivables	1,528,154	1,853,579
Net investment in direct financing leases	16,344,477	17,334,594
Interests in net assets of foundations	29,560,454	30,114,701
Long-term investments	62,222,367	71,641,642
Deposits	<u>24,456</u>	<u>24,465</u>
Total financial assets	<u>238,802,404</u>	<u>246,242,582</u>
Less amounts not available to be used within one year		
Board designated with liquidity horizons greater than one year	32,921,726	31,502,344
Net investment in direct financing leases	15,078,764	16,142,660
Interests in net assets of foundations	29,560,454	30,114,701
Long-term investments	62,222,367	71,641,642
Deposits	<u>24,456</u>	<u>24,465</u>
Financial assets not available to be used within one year	<u>139,807,767</u>	<u>149,425,812</u>
Financial assets available to meet general expenditures within one year	<u>\$ 98,994,637</u>	<u>\$ 96,816,770</u>

The Healthcare System has certain board-designated limited use assets for future capital improvements and self-funded employee health, workers' compensation and professional liability insurance. These assets limited to use, which are more fully described in *Notes 1* and *4*, are not available for general expenditure within the next year. However, the board-designated amounts could be made available, if necessary.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 13: Functional Expenses

The Healthcare System provides health care and mental health services primarily to residents within its geographic area. Certain costs attributable to more than one function have been allocated among the health care services, mental health services, and general and administrative functional expense classifications based on the department in which the expense was incurred. The following schedule presents the natural classification of expenses by function as follows:

	2019				
	Health Care Services	Mental Health Services	General and Administrative	Eliminations	Total
Salaries and wages	\$ 43,148,627	\$ 6,983,799	\$ 11,637,629	\$ -	\$ 61,770,055
Employee benefits	12,582,589	1,492,665	4,541,721	-	18,616,975
Purchased services, supplies and other	51,159,327	1,003,299	18,127,993	(634,550)	69,656,069
Depreciation and amortization	8,328,658	91,252	2,839,800	-	11,259,710
Income tax expense	43,177	-	48,023	-	91,200
Interest	1,300,080	-	345,771	-	1,645,851
	<u>\$ 116,562,458</u>	<u>\$ 9,571,015</u>	<u>\$ 37,540,937</u>	<u>\$ (634,550)</u>	<u>\$ 163,039,860</u>
	2018				
	Health Care Services	Mental Health Services	General and Administrative	Eliminations	Total
Salaries and wages	\$ 36,619,656	\$ 6,866,201	\$ 14,645,242	\$ -	\$ 58,131,099
Employee benefits	9,277,557	1,456,602	4,940,718	-	15,674,877
Purchased services, supplies and other	46,123,329	865,171	20,772,175	(289,148)	67,471,527
Depreciation and amortization	5,589,985	71,238	2,763,890	-	8,425,113
Income tax expense	46,000	-	-	-	46,000
Interest	99,561	-	41,158	-	140,719
	<u>\$ 97,756,088</u>	<u>\$ 9,259,212</u>	<u>\$ 43,163,183</u>	<u>\$ (289,148)</u>	<u>\$ 149,889,335</u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 14: Pension Plan

The Healthcare System has a defined contribution pension plan covering substantially all full-time employees who have completed one year of service. Annual contributions to the plan are based on a percentage of eligible employee compensation. Pension expense was \$3,101,111 and \$2,760,068 for 2019 and 2018, respectively.

Note 15: Disclosures About Fair Value of Assets

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

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

Recurring Measurements

The following table presents the fair value measurements of assets recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2019 and 2018:

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

	June 30, 2019			
	Fair Value Measurements Using			
	Fair Value	Quoted Prices		
		in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Money market accounts	\$ 1,852,632	\$ 1,852,632	\$ -	\$ -
Equity investments				
Mutual funds	15,296,610	15,296,610	-	-
International mutual funds	1,365,601	1,365,601	-	-
Fixed income investments				
Mortgage	440,097	440,097	-	-
Treasury and agencies	338,624	-	338,624	-
Certificates of deposit	502,089	-	502,089	-
Asset-backed	141,754	-	141,754	-
Municipal bonds	147,539	-	147,539	-
Preferred stock	60,159	60,159	-	-
Tax-exempt obligations	30,314	30,314	-	-
Taxable high yield	115,310	115,310	-	-
Bond mutual funds	2,887,440	2,887,440	-	-
Corporate bonds	1,679,645	1,679,645	-	-
Alternative investments (mutual funds)				
Hedge mutual funds	452,958	452,958	-	-
Infrastructure mutual funds	-	-	-	-
Traded real estate mutual funds	-	-	-	-
Alternative mutual funds	931,504	931,504	-	-
Total assets limited as to use for capital improvements	26,242,276	25,112,270	1,130,006	-
Money market accounts	872,231	872,231	-	-
Fixed income investments				
Treasury and agencies	4,379,205	-	4,379,205	-
Certificates of deposit	1,428,014	-	1,428,014	-
Total assets limited as to use for self-funded employee health, workers' compensation and professional liability insurance	6,679,450	872,231	5,807,219	-
Interest in net assets of the Foundation	28,017,107	-	28,017,107	-
Interest in net assets of the HCF	1,543,347	-	1,543,347	-

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

	June 30, 2019			
	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Money market accounts	\$ 6,906,670	\$ 6,906,670	\$ -	\$ -
Equity investments				
Common stock	5,612,526	5,612,526	-	-
Mutual funds	27,747,724	27,747,724	-	-
International mutual funds	3,339,525	3,339,525	-	-
Fixed income investments				
Mortgage	1,104,647	1,104,647	-	-
Treasury and agencies	2,780,264	-	2,780,264	-
Asset-backed	207,887	-	207,887	-
Municipal bonds	465,921	-	465,921	-
Preferred stock	146,729	146,729	-	-
International bonds	10,043	10,043	-	-
Tax-exempt obligations	40,419	40,419	-	-
Taxable high yield	281,186	281,186	-	-
Bond mutual funds	4,655,077	4,655,077	-	-
Corporate bonds	5,558,085	5,558,085	-	-
Alternative investments (mutual funds)				
Hedge mutual funds	1,107,529	1,107,529	-	-
Traded real estate mutual funds	83,874	83,874	-	-
Alternative mutual funds	1,340,802	1,340,802	-	-
Investment in HASC (A)	20,000	-	-	-
Investment in DDC (A)	621,142	-	-	-
Investment in VHA (A)	192,317	-	-	-
Total long-term investments	62,222,367	57,934,836	3,454,072	-
Funds held on deposit with the Foundation	7,352,127	-	-	7,352,127
	<u>\$ 132,056,674</u>	<u>\$ 83,919,337</u>	<u>\$ 39,951,751</u>	<u>\$ 7,352,127</u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

	June 30, 2018			
	Fair Value Measurements Using			
	Fair Value	Quoted Prices		
		in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Money market accounts	\$ 701,939	\$ 701,939	\$ -	\$ -
Equity investments				
Common stock	270,418	270,418	-	-
Mutual funds	13,706,562	13,706,562	-	-
International mutual funds	2,281,757	2,281,757	-	-
Fixed income investments				
Mortgage	276,940	276,940	-	-
Treasury and agencies	580,490	-	580,490	-
Asset-backed	374,971	-	374,971	-
Municipal bonds	83,934	-	83,934	-
Preferred stock	49,713	49,713	-	-
International bonds	346,443	346,443	-	-
Tax-exempt obligations	29,986	29,986	-	-
Taxable high yield	153,237	153,237	-	-
Bond mutual funds	3,780,272	3,780,272	-	-
Corporate bonds	1,331,606	1,331,606	-	-
Alternative investments (mutual funds)				
Hedge mutual funds	499,517	499,517	-	-
Infrastructure mutual funds	255,700	255,700	-	-
Traded real estate mutual funds	87,102	87,102	-	-
Alternative mutual funds	191,885	191,885	-	-
Total assets limited as to use for capital improvements	25,002,472	23,963,077	1,039,395	-
Money market accounts	1,768,037	1,768,037	-	-
Equity investments				
Mutual funds	37,844	37,844	-	-
Fixed income investments				
Treasury and agencies	4,190,639	4,190,639	-	-
Certificates of deposit	503,352	503,352	-	-
Total assets limited as to use for self-funded employee health, workers' compensation and professional liability insurance	6,499,872	6,499,872	-	-
Interest in net assets of the Foundation	28,673,210	-	28,673,210	-
Interest in net assets of the HCF	1,441,491	-	1,441,491	-

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

	June 30, 2018			
	Fair Value Measurements Using			
	Quoted Prices	in Active	Significant	Significant
	Fair Value	Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Money market accounts	\$ 5,524,827	\$ 5,524,827	\$ -	\$ -
Equity investments				
Common stock	3,934,455	3,934,455	-	-
Mutual funds	24,845,091	24,845,091	-	-
International mutual funds	6,262,471	6,262,471	-	-
Fixed income investments				
Mortgage	534,139	534,139	-	-
Treasury and agencies	11,783,449	-	11,783,449	-
Asset-backed	488,884	-	488,884	-
Municipal bonds	122,935	-	122,935	-
Preferred stock	121,179	121,179	-	-
International bonds	684,775	684,775	-	-
Tax-exempt obligations	39,981	39,981	-	-
Taxable high yield	348,012	348,012	-	-
Bond mutual funds	6,910,962	6,910,962	-	-
Corporate bonds	6,196,600	6,196,600	-	-
Government bonds	149,705	149,705	-	-
Alternative investments (mutual funds)				
Hedge mutual funds	1,218,134	1,218,134	-	-
Infrastructure mutual funds	623,301	623,301	-	-
Traded real estate mutual funds	212,401	212,401	-	-
Alternative mutual funds	806,882	806,882	-	-
Investment in HASC (A)	20,000	-	-	-
Investment in DDC (A)	621,142	-	-	-
Investment in VHA (A)	192,317	-	-	-
Total long-term investments	71,641,642	58,412,915	12,395,268	-
Funds held on deposit with the Foundation	6,930,640	-	-	6,930,640
	<u>\$ 140,189,327</u>	<u>\$ 88,875,864</u>	<u>\$ 43,549,364</u>	<u>\$ 6,930,640</u>

(A) The investments in HASC and DDC are carried at cost and the investment in VHA preferred stock is carried at its estimated net present value (*Note 4*). These investments have not been classified in the fair value hierarchy. The amounts included above are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended June 30, 2019.

Investments and Interests in Net Assets of Foundations

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

Funds Held on Deposit with the Foundation

Funds held on deposit with the Foundation through an investment pool totaled \$7,352,127 and \$6,930,640, respectively. The Healthcare System cannot look through the investment pool to its underlying investments for fair value measurement purposes. Rather, the Healthcare System must consider if relevant observable inputs exist for interests in the investment pool. The funds held on deposit with the Foundation are classified as Level 3 under the fair value hierarchy because no observable inputs exist for interests in the investment pool. However, at June 30, 2019 and 2018, approximately 98% and 97%, respectively, of the underlying investments of the investment pool fall within Level 1 classification under the fair value hierarchy.

Level 3 Reconciliation

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements associated with funds held on deposit with the Foundation recognized in the accompanying consolidated balance sheets using significant unobservable (Level 3) inputs:

Balance, July 1, 2017	\$ 6,393,550
Interest and dividends	156,621
Net realized and unrealized gains	311,824
Investment fees	(19,820)
Purchases	88,465
	<hr/>
Balance, June 30, 2018	6,930,640
Interest and dividends	207,146
Net realized and unrealized gains	228,575
Investment fees	(20,820)
Purchases	6,586
	<hr/>
Balance, June 30, 2019	<u><u>\$ 7,352,127</u></u>

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 16: Significant Estimates and Concentrations

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

Variable Consideration

Estimates of variable consideration in determining the transaction price for patient service revenue as described in *Notes 1* and *2*.

Professional Liability Claims

Estimates related to the accrual for professional liability claims are described in *Notes 1* and *9*.

Litigation

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

Guarantees

HASC has a \$500,000 line of credit with a local bank. The Healthcare System has guaranteed \$100,000 of this line of credit and is contingently liable under the guarantee should HASC fail to make payments on the line of credit as they become due.

Investments

The Healthcare System invests in various investment securities. 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 change could materially affect the amounts reported in the accompanying consolidated balance sheets.

Hutchinson Regional Medical Center, Inc.
Notes to Consolidated Financial Statements
June 30, 2019 and 2018

Note 17: Change in Accounting Principle

Topic 606 Revenue from Contracts with Customers

On July 1, 2018, the Healthcare System adopted the Financial Accounting Standards Board Accounting Standards Update 2014-09, *Revenue from Contracts with Customers (Topic 606)*, (ASU 2014-09) using a modified-retrospective method of adoption to all contracts with patients at July 1, 2018. The core guidance in ASU 2014-09 is to recognize revenue to depict the transfer of promised goods or services to customers or patients in an amount that reflects the consideration to which the Healthcare System expects to be entitled in exchange for those goods or services. The amount to which the Healthcare System expects to be entitled is calculated as the transaction price and recorded as revenue in exchange for providing patient care services to its patients. Adoption of ASU 2014-09 resulted in changes in presentation of the consolidated financial statements and related disclosures in the notes to the consolidated financial statements. Prior to the adoption of ASU 2014-09, the majority of the provision for doubtful accounts related to patients without insurance, as well as patient responsibility balances for co-pays, co-insurance and deductibles for patients with insurance. Under ASU 2014-09, the estimated amounts due from patients for which the Healthcare System does not expect to be entitled or collect from the patients are considered implicit price concessions and excluded from the Healthcare System's estimation of the transaction price or revenue recorded. The adoption had no impact on operating income, overall change in net assets or net cash provided by operating activities.

Note 18: Subsequent Events

Subsequent events have been evaluated through November 15, 2019, which is the date the consolidated financial statements were issued.

Note 19: Future Change in Accounting Principle

Accounting for Leases

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

Supplementary Information

Hutchinson Regional Medical Center, Inc.
Consolidating Schedule – Balance Sheet
June 30, 2019

Assets

	Hutchinson Regional Medical Center, Inc.	Hutchinson Health Care Services, Inc.	Hospice of Reno County, Inc.	Main Line, Inc.	Horizons Mental Health Center, Inc.	Eliminations and Reclassi- fications	Total
Current Assets							
Cash and cash equivalents	\$ 14,792,149	\$ 1,689,392	\$ 132,822	\$ 5,122,686	\$ 3,367,715	\$ -	\$ 25,104,764
Assets limited as to use, current	2,029,715	-	-	-	-	-	2,029,715
Funds held on deposit with the Hutchinson Regional Medical Foundation	-	-	422,589	-	6,929,538	-	7,352,127
Patient accounts receivable, net	30,771,633	201,613	936,971	-	1,135,696	-	33,045,913
Other receivables	1,415,253	6,071	1,618	58,884	46,328	-	1,528,154
Due from affiliate	615,423	1,491	50,805	3,125	63,997	(734,841)	-
Net investment in direct financing leases	-	-	-	1,265,713	-	-	1,265,713
Supplies	4,578,644	388,736	23,377	-	-	-	4,990,757
Prepaid expenses and other	2,957,050	136,463	34,995	23,448	136,101	(22,340)	3,265,717
Total current assets	57,159,867	2,423,766	1,603,177	6,473,856	11,679,375	(757,181)	78,582,860
Assets Limited As To Use							
Internally designated							
For capital improvements	26,242,276	-	-	-	-	-	26,242,276
For self-funded employee health, workers' compensation and professional liability insurance	6,679,450	-	-	-	-	-	6,679,450
Interests in net assets of foundations	28,017,107	-	1,543,347	-	-	-	29,560,454
	60,938,833	-	1,543,347	-	-	-	62,482,180
Less amount required to meet current obligations	2,029,715	-	-	-	-	-	2,029,715
	58,909,118	-	1,543,347	-	-	-	60,452,465
Property and Equipment, Net	86,756,378	450,676	832,062	7,767,999	1,107,857	-	96,914,972
Other Assets							
Net investment in direct financing leases	-	-	-	15,078,764	-	-	15,078,764
Investment in subsidiary	480,000	-	-	-	-	(480,000)	-
Long-term investments	60,674,517	1,547,850	-	-	-	-	62,222,367
Deposits	-	-	-	24,456	-	-	24,456
	61,154,517	1,547,850	-	15,103,220	-	(480,000)	77,325,587
Total assets	\$ 263,979,880	\$ 4,422,292	\$ 3,978,586	\$ 29,345,075	\$ 12,787,232	\$ (1,237,181)	\$ 313,275,884

Hutchinson Regional Medical Center, Inc.
Consolidating Schedule – Balance Sheet (Continued)
June 30, 2019

Liabilities and Net Assets

	Hutchinson Regional Medical Center, Inc.	Hutchinson Health Care Services, Inc.	Hospice of Reno County, Inc.	Main Line, Inc.	Horizons Mental Health Center, Inc.	Eliminations and Reclassi- fications	Total
Current Liabilities							
Current maturities of long-term debt	\$ 815,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 815,000
Current maturities of capital lease obligations	58,559	-	-	-	-	-	58,559
Accounts payable	6,780,690	146,043	88,867	177,894	192,696	-	7,386,190
Accrued expenses	8,175,064	201,896	733,066	-	1,238,902	-	10,348,928
Due to affiliate	144,076	12,260	452,001	24,757	124,087	(757,181)	-
Deferred revenue	10,101	-	-	-	-	-	10,101
Estimated amounts due to third-party payers	3,198,406	-	-	-	-	-	3,198,406
	<u>19,181,896</u>	<u>360,199</u>	<u>1,273,934</u>	<u>202,651</u>	<u>1,555,685</u>	<u>(757,181)</u>	<u>21,817,184</u>
Total current liabilities							
	34,650,122	-	-	-	-	-	34,650,122
Long-term Debt, Net							
	30,545	-	-	-	-	-	30,545
Capital Lease Obligations							
	<u>53,862,563</u>	<u>360,199</u>	<u>1,273,934</u>	<u>202,651</u>	<u>1,555,685</u>	<u>(757,181)</u>	<u>56,497,851</u>
Total liabilities							
Net Assets							
Without donor restrictions	182,100,210	4,062,093	2,560,241	29,142,424	11,231,547	(480,000)	228,616,515
With donor restrictions - purpose restrictions	28,017,107	-	93,805	-	-	-	28,110,912
With donor restrictions - perpetual in nature	-	-	50,606	-	-	-	50,606
	<u>210,117,317</u>	<u>4,062,093</u>	<u>2,704,652</u>	<u>29,142,424</u>	<u>11,231,547</u>	<u>(480,000)</u>	<u>256,778,033</u>
Total net assets							
	<u>\$ 263,979,880</u>	<u>\$ 4,422,292</u>	<u>\$ 3,978,586</u>	<u>\$ 29,345,075</u>	<u>\$ 12,787,232</u>	<u>\$ (1,237,181)</u>	<u>\$ 313,275,884</u>
Total liabilities and net assets							

Hutchinson Regional Medical Center, Inc.
Consolidating Schedule – Statement of Operations
Year Ended June 30, 2019

	Hutchinson Regional Medical Center, Inc.	Hutchinson Health Care Services, Inc.	Hospice of Reno County, Inc.	Main Line, Inc.	Horizons Mental Health Center, Inc.	Eliminations and Reclassi- fications	Total
Unrestricted Revenues, Gains and Other Support							
Patient service revenue	\$ 124,084,400	\$ 3,771,953	\$ 5,281,378	\$ -	\$ 9,580,173	\$ -	\$ 142,717,904
Other	3,595,049	-	598,902	1,986,350	3,556,209	(634,550)	9,101,960
Net assets released from restrictions used for operations	-	-	5,617	-	-	-	5,617
Total unrestricted revenues, gains and other support	<u>127,679,449</u>	<u>3,771,953</u>	<u>5,885,897</u>	<u>1,986,350</u>	<u>13,136,382</u>	<u>(634,550)</u>	<u>151,825,481</u>
Expenses and Losses							
Salaries and wages	48,386,438	1,231,363	4,007,652	-	8,144,602	-	61,770,055
Employee benefits	14,931,266	368,350	1,010,354	-	2,307,005	-	18,616,975
Purchased services, supplies and other	64,073,505	1,650,691	1,424,486	836,360	2,305,577	(634,550)	69,656,069
Depreciation	9,937,176	162,548	145,496	891,013	123,477	-	11,259,710
Income tax expense	-	91,200	-	-	-	-	91,200
Interest	1,645,851	-	-	-	-	-	1,645,851
Total expenses and losses	<u>138,974,236</u>	<u>3,504,152</u>	<u>6,587,988</u>	<u>1,727,373</u>	<u>12,880,661</u>	<u>(634,550)</u>	<u>163,039,860</u>
Operating Income (Loss)	<u>(11,294,787)</u>	<u>267,801</u>	<u>(702,091)</u>	<u>258,977</u>	<u>255,721</u>	<u>-</u>	<u>(11,214,379)</u>
Other Income (Expense)							
Investment return, net	4,673,945	88,243	118,216	-	391,305	-	5,271,709
Contributions received	452,227	-	310,573	-	-	-	762,800
Other	76,155	35	(58,804)	-	38,884	-	56,270
Total other income	<u>5,202,327</u>	<u>88,278</u>	<u>369,985</u>	<u>-</u>	<u>430,189</u>	<u>-</u>	<u>6,090,779</u>
Excess (Deficiency) of Revenues Over Expenses	<u>(6,092,460)</u>	<u>356,079</u>	<u>(332,106)</u>	<u>258,977</u>	<u>685,910</u>	<u>-</u>	<u>(5,123,600)</u>
Net assets released from restriction used for purchase of property and equipment	2,012,000	-	-	-	-	-	2,012,000
Transfers between affiliates	(3,280,909)	-	-	3,280,909	-	-	-
Increase (Decrease) in Net Assets Without Donor Restrictions	<u>\$ (7,361,369)</u>	<u>\$ 356,079</u>	<u>\$ (332,106)</u>	<u>\$ 3,539,886</u>	<u>\$ 685,910</u>	<u>\$ -</u>	<u>\$ (3,111,600)</u>

Hutchinson Regional Medical Center, Inc.
Consolidating Schedule – Statement of Changes in Net Assets
Year Ended June 30, 2019

	Hutchinson Regional Medical Center, Inc.	Hutchinson Health Care Services, Inc.	Hospice of Reno County, Inc.	Main Line, Inc.	Horizons Mental Health Center, Inc.	Eliminations and Reclassi- fications	Total
Net Assets Without Donor Restrictions							
Excess (deficiency) of revenues over expenses	\$ (6,092,460)	\$ 356,079	\$ (332,106)	\$ 258,977	\$ 685,910	\$ -	\$ (5,123,600)
Net assets released from restriction used for purchase of property and equipment	2,012,000	-	-	-	-	-	2,012,000
Transfers between affiliates	(3,280,909)	-	-	3,280,909	-	-	-
	<u>(7,361,369)</u>	<u>356,079</u>	<u>(332,106)</u>	<u>3,539,886</u>	<u>685,910</u>	<u>-</u>	<u>(3,111,600)</u>
Increase (decrease) in net assets without donor restrictions							
Net Assets With Donor Restrictions							
Investment return, net	-	-	4,239	-	-	-	4,239
Contributions received	2,012,000	-	-	-	-	-	2,012,000
Change in interests in net assets of foundations	(656,103)	-	-	-	-	-	(656,103)
Net assets released from restriction used for operations	-	-	(5,617)	-	-	-	(5,617)
Net assets released from restriction used for purchase of property and equipment	(2,012,000)	-	-	-	-	-	(2,012,000)
	<u>(656,103)</u>	<u>-</u>	<u>(1,378)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(657,481)</u>
Increase (decrease) in net assets with donor restrictions							
Change in Net Assets	(8,017,472)	356,079	(333,484)	3,539,886	685,910	-	(3,769,081)
Net Assets, Beginning of Year	218,134,789	3,706,014	3,038,136	25,602,538	10,545,637	(480,000)	260,547,114
Net Assets, End of Year	<u>\$ 210,117,317</u>	<u>\$ 4,062,093</u>	<u>\$ 2,704,652</u>	<u>\$ 29,142,424</u>	<u>\$ 11,231,547</u>	<u>\$ (480,000)</u>	<u>\$ 256,778,033</u>