

CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Memorial Health System and Subsidiaries
Years Ended September 30, 2019 and 2018
With Report of Independent Auditors

Ernst & Young LLP



Memorial Health System and Subsidiaries
Consolidated Financial Statements and Supplementary Information
Years Ended September 30, 2019 and 2018

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Report of Independent Auditors

The Board of Directors
Memorial Health System

We have audited the accompanying consolidated financial statements of Memorial Health System and Subsidiaries, which comprise the consolidated balance sheets as of September 30, 2019 and 2018, and the related consolidated statements of operations and changes in nets 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 financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor’s Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation and fair presentation of the 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 financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Memorial Health System and Subsidiaries at September 30, 2019 and 2018, and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating balance sheet, consolidating statement of operations and changes in net assets and consolidating statement of cash flows is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the 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 financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Ernst & Young LLP

December 17, 2019

Memorial Health System and Subsidiaries

Consolidated Balance Sheets

(Dollars in Thousands)

	September 30	
	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 91,365	\$ 79,397
Short-term investments	69,728	116,064
Assets whose use is limited	7,565	3,033
Receivables:		
Patient accounts receivable	148,156	142,694
Receivables from third-party payors	11,324	13,620
Receivables held for sale	2,097	1,308
Other receivables	25,674	22,551
Inventories	14,954	14,558
Prepaid expenses	15,496	13,380
Total current assets	386,359	406,605
Long-term investments:		
Unrestricted investments	594,356	579,903
Assets whose use is limited	47,189	43,847
Total long-term investments	641,545	623,750
Property, plant, and equipment, net	583,984	573,422
Other assets:		
Investments in partnerships	6,615	7,577
Beneficial interest in trusts	45,387	46,111
Other	23,810	40,714
Total other assets	75,812	94,402
Total assets	\$ 1,687,700	\$ 1,698,179

Memorial Health System and Subsidiaries

Consolidated Balance Sheets (continued)

(Dollars in Thousands)

	September 30	
	2019	2018
Liabilities and net assets		
Current liabilities:		
Long-term debt	\$ 11,117	\$ 12,945
Accounts payable	71,123	58,650
Accrued payroll	46,657	44,104
Interest payable	5,350	5,093
Payables to third-party payors	46,819	43,816
Other	17,517	16,268
Total current liabilities	198,583	180,876
Noncurrent liabilities:		
Long-term debt obligations, net	328,674	371,059
Deferred compensation and benefits	22,210	17,268
Self-insurance accrued expenses	18,038	18,243
Accrued employee benefits	18,054	17,772
Pension obligations	7,381	6,027
Other	21,627	25,003
Total noncurrent liabilities	415,984	455,372
Total liabilities	614,567	636,248
Net assets:		
Without donor restrictions	1,007,334	996,921
With donor restrictions	65,799	65,010
Total net assets	1,073,133	1,061,931
Total liabilities and net assets	\$ 1,687,700	\$ 1,698,179

See accompanying notes.

Memorial Health System and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets (Dollars in Thousands)

	Years Ended September 30	
	2019	2018
Revenues:		
Net patient service revenues	\$ 949,557	\$ 930,037
Capitation revenues	63,682	60,043
Other revenues	30,300	30,232
Total revenues	1,043,539	1,020,312
Expenses:		
Salaries and wages	404,652	390,362
Employee benefits	105,970	112,255
Physician fees	83,021	67,893
Pharmaceutical supplies	38,881	38,793
Patient service supplies	102,296	98,003
Purchased services and other	138,974	132,027
Hospital provider assessment	28,519	24,640
Purchased medical services	32,598	36,375
Depreciation and amortization	66,830	68,381
Interest expense and other financing costs	14,411	17,149
Total expenses	1,016,152	985,878
Income from operations	27,387	34,434
Nonoperating gains (losses):		
Interest and dividends	9,705	10,481
Realized gain on investments, net	9,597	60,201
Unrealized gain (loss) on investments, net	363	(29,133)
(Loss) gain on derivatives	(1,593)	796
Loss on extinguishment of debt	(731)	-
Net periodic benefit cost	(4,310)	(7,947)
Other revenue (expense), net	(8,662)	(2,585)
Total nonoperating gains, net	4,369	31,813
Excess of revenues over expenses	31,756	66,247

Memorial Health System and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets (continued) (Dollars in Thousands)

	Years Ended September 30	
	2019	2018
Net assets without donor restrictions:		
Excess of revenues over expenses	\$ 31,756	\$ 66,247
Pension and other postretirement liability adjustments	(21,565)	19,920
Other	222	172
Increase in net assets without donor restrictions	10,413	86,339
Net assets with donor restrictions:		
Contributions	3,042	979
Net investment gain	237	1,110
Net assets released from restrictions	(2,427)	(4,772)
Change in fair value of split interest agreements	270	(111)
Other	(333)	(267)
Increase (decrease) in net assets with donor restrictions	789	(3,061)
Change in net assets	11,202	83,278
Net assets, beginning of fiscal year	1,061,931	978,653
Net assets, end of fiscal year	\$ 1,073,133	\$ 1,061,931

See accompanying notes.

Memorial Health System and Subsidiaries

Consolidated Statements of Cash Flows

(Dollars in Thousands)

	Years Ended September 30	
	2019	2018
Operating activities		
Change in net assets	\$ 11,202	\$ 83,278
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Loss on extinguishment of debt	731	–
Loss (gain) on derivatives	1,593	(796)
Interest and dividends	(9,704)	(10,969)
Realized loss on investments, net	(9,795)	(60,841)
Unrealized (gain) loss on investments, net	(485)	28,908
Restricted contributions and other	(3,042)	(979)
Unrealized gain on beneficial interest in trusts	(324)	(158)
Depreciation and amortization	66,830	68,381
Amortization of debt issuance (premiums) costs	(651)	615
(Gain) loss on disposal of assets	(330)	865
Deferred tax asset	(1,300)	–
Pension obligations (assets)	21,565	(19,920)
Changes in assets and liabilities:		
Accounts receivable	(5,462)	13,767
Inventory and other assets	(7,503)	30,641
Estimated third-party payor settlements	5,299	5,448
Accounts payable and other current liabilities	15,500	11,317
Self-insurance and other long-term liabilities	(581)	(7,067)
Net cash provided by operating activities	83,543	142,490
Investing activities		
Acquisition of property and equipment	(79,473)	(59,406)
Proceeds on sale of property	2,739	1,341
Investments classified as trading, net	43,598	(122,677)
Change in investment in partnerships	962	1,698
Net change in other assets	741	1,082
Net cash used in investing activities	(31,433)	(177,962)

Memorial Health System and Subsidiaries

Consolidated Statements of Cash Flows (continued)

(Dollars in Thousands)

	Years Ended September 30	
	2019	2018
Financing activities		
Restricted contributions and other	\$ 3,042	\$ 979
Repayment of long-term debt	(190,819)	(53,809)
Issuance of long-term debt	130,005	–
Premium received, net of debt issuance cost payments	16,582	–
Distributions from beneficial interest in trusts	1,048	848
Net cash used in financing activities	(40,142)	(51,982)
Net increase (decrease) in cash and cash equivalents	11,968	(87,454)
Cash and cash equivalents, beginning of fiscal year	79,397	166,851
Cash and cash equivalents, end of fiscal year	\$ 91,365	\$ 79,397
Supplemental disclosure of cash flow information		
Cash paid for interest	\$ 15,074	\$ 16,417
Noncash investing activity		
Contributions of land	\$ –	\$ 2,211

See accompanying notes.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements *(Dollars in Thousands)*

September 30, 2019

1. Organization

Memorial Health System (Parent) is incorporated as a not-for-profit corporation under the laws of the State of Illinois and is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code (the Code). Memorial Health System and Subsidiaries (collectively, MHS) comprise the following corporations and their subsidiaries:

Memorial Health System

Sole corporate member of:

- Memorial Medical Center (MMC):
 - Memorial Medical Center Foundation (MMCF)
- The Passavant Memorial Area Hospital Association (PAH):
 - Passavant Physician Association (PPA)
 - Jacksonville CRNAs, Inc. (CRNA)
 - Passavant Area Hospital Foundation (PAHF)
- The Abraham Lincoln Memorial Hospital (ALMH)
- Taylorville Memorial Hospital (TMH):
 - Taylorville Memorial Hospital Foundation, Inc. (TMHF)
- Memorial Physician Services (MPS)
- Mental Health Centers of Central Illinois d/b/a Memorial Behavioral Health (MBH):
 - Springfield Residential Services (SRS)
- MHS QALICB, LLC (QALICB)
- Memorial Home Services NFP (MHSvc):
 - Memorial Home Services of Central Illinois, Inc. (MHSCI)
- Memorial Health Ventures (MHV)
- Memorial Health Partners, LLC (MHP)
- Abraham Lincoln Healthcare Foundation (ALHF)
- McDEKK, LLC (McDEKK)

All significant intercompany transactions and balances have been eliminated in the consolidated financial statements.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with a maturity of three months or less when purchased, excluding amounts whose use is limited by Board designation or other arrangements under trust agreements. MHS places its cash and cash equivalents with institutions with high credit quality. However, at certain times, such cash and cash equivalents are in excess of government-provided insurance limits. MHS routinely invests in money market mutual funds. These funds generally invest in highly liquid U.S. government and agency obligations. MHS's cash and cash equivalents are invested in financial instruments that potentially subject MHS to concentrations of credit risk.

Short-Term Investments

Short-term investments primarily include cash and cash equivalents, corporate obligations, government obligations, certificates of deposit, mutual funds, and corporate equity securities that are classified as current assets because such amounts are available to meet MHS's operating cash requirements.

Inventories

Inventories, consisting primarily of medical supplies and drugs, are stated at the lower of cost or net realizable value. Cost is determined using the average cost method.

Long-Term Investments

Long-term investments primarily include unrestricted investments and assets whose use is limited. Assets whose use is limited include amounts set aside under revocable self-insurance trust agreements, assets held by trustees under indenture agreements, assets restricted as to use by donors, cash restricted as to withdrawal or use, and deferred compensation investments. Amounts designated to help meet the current liabilities of MHS have been classified as the current portion of assets whose use is limited in the consolidated balance sheets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Investment securities are recorded at fair value, based on the valuation methodologies used in the fair value measurement and disclosures topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). The cost of securities sold is based on the specific identification method. MHS classifies its investment portfolio as trading, with unrealized gains and losses included in excess of revenues over expenses.

Realized and unrealized gains and losses on investments, interest, and dividends from all other investments are reported as nonoperating gains (losses) unless the income is restricted by donor or law.

MHS has elected the fair value option in accordance with U.S. generally accepted accounting principles (GAAP) when valuing investments in farmland, which are included in unrestricted investments on the consolidated balance sheets.

Available Resources and Liquidity

MHS considers all cash and cash equivalents, short-term investments, and unrestricted investments to be financial assets available and free from restriction to meet cash needs for operating activities of MHS within one year of September 30, 2019.

Property, Plant, and Equipment

Property, plant, and equipment are recorded at cost or, if donated, at fair value at the date of receipt. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets as follows:

Land improvements	5–25 years
Buildings and improvements	10–40 years
Equipment	3–10 years

Leasehold improvements and equipment under capital leases are depreciated or amortized over the corresponding lease term and included in depreciation and amortization expense.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Beneficial Interest in Trusts

MMC and PAH are the beneficiaries of several irrevocable trusts held and administered by third-party trustees. The income from these trusts is distributed annually. The proceeds from the trust are classified as net assets without donor restrictions or net assets with donor restrictions based on the terms of the applicable trust agreement. Beneficial interest in the trusts totaled \$45,387 and \$46,111 as of September 30, 2019 and 2018, respectively, and is equal to the estimated fair value of the underlying trust assets (primarily Illinois farmland). Trust distributions were \$1,048 and \$3,059 in 2019 and 2018, respectively, and are included in other revenue in the nonoperating gains (losses) section of the consolidated statements of operations and changes in net assets.

Other Assets

Other assets primarily consist of cash surrender value of life insurance policies, noncompete agreement clauses in physician acquisition contracts, net pension asset, notes receivables and reinsurance recoveries. Under the terms of the physician employment agreements, vesting to the physicians in the cash surrender values occurs over various terms.

Deferred Compensation Investments

MHS has nonqualified deferred compensation plans available to select employees. Contributions to the plans are invested in mutual funds and are payable to the employees upon vesting, retirement, or resignation. Deferred compensation investments, which are recorded at fair value, and deferred compensation liabilities have been recorded in the accompanying consolidated balance sheets.

Accrued Employee Benefits

Accrued employee benefits consist of the accrual for the paid sick time program and the accrual for post-employment benefits, which consists of three liabilities: the continuation of medical benefits to employees on long-term disability, postretirement health care benefits for certain employee groups that meet special qualifications, and sick time paid at retirement. MHS accrues these benefits based on actuarial estimates.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Net Assets

MHS's net assets are classified as with donor restrictions and without donor restrictions based on the existence or absence of donor-imposed restrictions. Net assets with donor restrictions consist of net assets whose use by MHS has been limited by donors to a specific time period or for a particular purpose or which must be maintained by MHS in perpetuity with the related investment income expendable to support the donor-designated purpose. The general nature of the donor restrictions is to support MHS's mission and health education programs and to assist in capital purchasing.

As of September 30, 2019 and 2018, MHS's endowments consist of 56 and 55, respectively, individual donor-restricted funds established for a variety of purposes. Net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The endowment net asset composition by type of fund consisted of the following as of September 30, 2019:

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total
Donor-restricted endowment funds	\$ —	\$ 8,743	\$ 8,743
Board-designated endowments funds	1,999	—	1,999
Total endowment funds	<u>\$ 1,999</u>	<u>\$ 8,743</u>	<u>\$ 10,742</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

The endowment net asset composition by type of fund consisted of the following as of September 30, 2018:

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total
Donor-restricted endowment funds	\$ —	\$ 8,613	\$ 8,613
Board-designated endowments funds	1,326	—	1,326
Total endowment funds	\$ 1,326	\$ 8,613	\$ 9,939

Of all of MHS's foundations, only MMCF has a policy of appropriating for distribution each year 5% of its endowment funds' average fair value of investments over the prior 36 months as of September 30 of the preceding fiscal year in which the distribution is planned. In establishing this policy, MMCF considers the long-term expected return on its endowments. Accordingly, over the long term, MMCF expects the current spending policy to allow its endowment to grow at the average long-term rate of inflation. This is consistent with MMCF's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specific term, as well as to provide additional real growth through new gifts and investment return.

Net Patient Service Revenues and Accounts Receivable Valuation

MHS provides health care services through inpatient and outpatient care facilities located in central Illinois and grants credit to patients, substantially all of whom are local residents. MHS generally does not require collateral or other security in extending credit to patients; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies, including, but not limited to, Medicare, Medicaid, health maintenance organizations, and commercial insurance policies.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

MHS recognizes revenues in the period in which performance obligations are satisfied. Generally, MHS bills patients and third-party payors several days after services are performed or the patient is discharged. Accounts receivable primarily consist of amounts due from third-party payors and patients. MHS's ability to collect outstanding receivables is critical to its operations and cash flows. Amounts MHS receives for treatment of patients covered by governmental programs and third-party payors as well as directly from patients are subject to explicit and implicit price concessions. Accordingly, the revenue and accounts receivable reported in MHS's consolidated financial statements are recorded at the net consideration to which MHS expects to be entitled to in exchange for providing patient care.

MHS has agreements with third-party payors that provide for payments at amounts different from its established charges. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and these amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, or investigations. MHS's patient service revenue increased by \$3,667 and \$2,053 in 2019 and 2018, respectively, as the result of these retroactive adjustments.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Noncompliance with Medicare and Medicaid laws and regulations can make MHS subject to significant regulatory action, including substantial fines and penalties, as well as exclusion from the Medicare and Medicaid programs. MHS's management believes that adequate provisions have been made for adjustments that may result from final determination of amounts earned under these programs consistent with the constraints that are required by ASC 606, *Revenue from Contracts with Customers*.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

The majority of MHS's performance obligations are satisfied over time for the delivery of patient care in both inpatient and outpatient settings. Revenue for performance obligations satisfied over time is recognized based on estimated expected payment at that point in time. MHS believes this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the remaining services needed to satisfy the obligation. Generally, unsatisfied or partially unsatisfied performance obligations at the end of the reporting period are related to patients admitted to MHS's hospitals that have not yet been discharged. MHS measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. As substantially all of MHS's performance obligations are part of a contract that is expected to have a duration of one year or less, MHS has elected to apply the exemption provided by ASC 606-10 to not disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied as of the period-end.

MHS has elected to apply the practical expedient permitted under ASC 606 and does not adjust the estimated amount of consideration from patients and third-party payors for the effects of a significant financing component due to MHS's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less.

MHS uses a portfolio approach to account for categories of patient contracts as a collective group rather than recognizing revenue on an individual contract basis. The portfolios primarily consist of major payor classes for inpatient, outpatient and other patient revenue. Based on historical collection trends and other analysis, MHS believes that revenue recognized by using the portfolio approach approximates the revenue that would have been recognized if an individual contract approach was used.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

MHS's initial estimate of the transaction price is determined by reducing the total standard charges related to the patient services provided by various elements of variable considering, including contractual adjustments, discounts, implicit price concessions and other reductions to MHS's standard charges. MHS determines the transaction price associated with services provided to patients who have third-party payor coverage based on reimbursement terms per contractual agreements, MHS's discount policies and historical experience. Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. For patients with deductibles and coinsurance, or uninsured and underinsured patients who do not apply or do not meet the qualifications for charity care, MHS determines the transaction price associated with services on the basis of charges reduced by implicit price concessions. Implicit price concessions are based upon management's judgmental assessment of historical and expected net collections considering business and general economic conditions in its service area, trends in health care coverage, and other collection indicators. Throughout the year, management assesses the adequacy of the allowance for implicit price concessions, taking into consideration recent write-off experience by payor category, including those not covered by insurance. Subsequent changes to the estimate of the transaction price (determined on a portfolio basis when applicable) are generally recorded as adjustments to patient service revenue in the period of change. For the fiscal years ended September 30, 2019 and 2018, changes in estimates of implicit price concessions, discounts, contractual adjustments or other were not significant.

Capitation Revenues

MHS has entered into risk-based contracts to provide medical services. Under these arrangements, MHS receives capitation payments based on the demographic characteristics of covered members in exchange for providing certain medical services to those members. MHS has engaged in stop-loss insurance contracts to protect against future significant losses for catastrophic cases.

Purchased medical services represent payments made to non-MHS and out-of-network providers for covered medical claims. MHS estimates its liability for covered medical claims, including claims incurred but not reported as of the consolidated balance sheet dates, based upon historical costs incurred and payment-processing experience. The liability for covered medical claims is included in other current liabilities in the accompanying consolidated balance sheets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Charity Care

In support of its mission, MHS provides care to patients who lack financial resources and are deemed to be financially indigent. Traditional charity care includes cost of services provided to persons who MHS determines cannot afford health care because of inadequate resources. The charges for services provided to charity patients are not reported as net patient service revenue. The cost of traditional charity care was \$10,444 and \$9,416 for the fiscal years ended September 30, 2019 and 2018, respectively. MHS calculates the unpaid cost of services by payor using an activity-based costing methodology.

Asset Impairment

MHS considers whether indicators of impairment are present and, if present, performs the necessary tests to determine whether the carrying values of an asset are recoverable. Impairment write-downs are recognized in depreciation expense at the time the impairment is identified. MHS had no asset impairment for the fiscal years ended September 30, 2019 or 2018.

Derivative Financial Instruments

MHS uses interest rate swap instruments as part of a risk management strategy to manage exposure to fluctuations in interest rates and to manage the overall cost of its debt. All derivatives are recognized as either assets or liabilities and are measured at fair value. MHS does not account for any of its interest rate swap instruments as hedges, and accordingly, all realized and unrealized gains and losses resulting from changes in the fair value of derivatives are reflected in nonoperating gains (losses) in the consolidated statements of operations and changes in net assets. The fair values of the interest rate swap instruments are determined based on the present value of expected future cash flows using discount rates appropriate with the risks involved and reflect a credit spread adjustment to the London Interbank Offered Rate (LIBOR) discount curve in order to emulate the credit value adjustment for nonperformance risk.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to MHS are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received or the condition is met. Gifts are reported as net assets with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. A donor restriction expires when a stipulated time restriction ends or the purpose restriction is accomplished. At that time, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions.

Donor-restricted contributions whose restrictions are met within the same year as they are received are reported in other revenue (expense), net in the nonoperating gains (losses) section of the consolidated statements of operations and changes in net assets.

Performance Indicator

MHS's performance indicator excess of revenues over expenses includes all changes in net assets without donor restrictions other than net assets released from restrictions for property acquisitions and pension and other postretirement liability adjustments.

Operating and Nonoperating Gains (Losses)

MHS's primary mission is to improve the health of the people and communities it serves through a broad range of general and specialized health care services, including inpatient acute care, outpatient services, physician services, and other health care services. Activities directly associated with the furtherance of this purpose are considered to be operating activities. Other activities that result in gains or losses peripheral to MHS's primary mission are considered to be nonoperating. Nonoperating activities include interest, dividends, realized and unrealized gains and losses on investments, gains and losses on derivatives, net periodic benefit cost, and other revenues and expenses not related to patient care, such as provision for income taxes and contribution expense.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Functional Classification of Expenses

MHS's accounting policies conform to U.S. GAAP applicable to health care organizations. Substantially all expenses are related to providing health care services to the community. However, there are certain costs not directly attributable to health care services, including certain salaries and benefits, depreciation, and other costs. These costs are allocated to management, general and administrative on a reasonable basis that is consistently applied. Expenses by functional classification consist of the following:

	Year Ended September 30, 2019		
	Health Care Services	Management, General and Administrative	Total
Expenses:			
Salaries and wages	\$ 355,326	\$ 49,326	\$ 404,652
Employee benefits	91,021	14,949	105,970
Physician fees	81,575	1,446	83,021
Pharmaceutical supplies	38,881	–	38,881
Patient services supplies	102,296	–	102,296
Purchased services and other	94,135	44,839	138,974
Hospital provider assessment	28,519	–	28,519
Purchased medical services	32,598	–	32,598
Depreciation	55,452	11,378	66,830
Interest expense and other financing costs	14,411	–	14,411
Total	\$ 894,214	\$ 121,938	\$ 1,016,152

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

	Year Ended September 30, 2018		
	Health Care Services	Management, General and Administrative	Total
Expenses:			
Salaries and wages	\$ 342,505	\$ 47,857	\$ 390,362
Employee benefits	97,751	14,504	112,255
Physician fees	66,490	1,403	67,893
Pharmaceutical supplies	38,793	–	38,793
Patient services supplies	98,003	–	98,003
Purchased services and other	88,525	43,502	132,027
Hospital provider assessment	24,640	–	24,640
Purchased medical services	36,375	–	36,375
Depreciation	57,342	11,039	68,381
Interest expense and other financing costs	17,149	–	17,149
Total	\$ 867,573	\$ 118,305	\$ 985,878

Income Taxes

Each of MHS's subsidiaries, excluding those described in the following paragraph, is a separately incorporated not-for-profit corporation as described under Section 501(c)(3) of the Code and is tax-exempt from federal and state income taxes on related income pursuant to Section 501(a) of the Code. They do, however, operate certain programs that may result in unrelated business income. Upon review as required by ASC 740, *Income Taxes*, no tax provision was recorded for the fiscal years ended September 30, 2019 or 2018.

MHS is no longer subject to income tax examinations for years prior to 2016.

QALICB, McDEKK and MHP are considered disregarded entities for tax purposes and are exempt from income tax. MHSCI is a taxable for-profit corporation, and PPA is a taxable not-for-profit corporation. Both are subject to federal and state income taxes.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Accounting Policies

In April 2016, the FASB issued Accounting Standards Update (ASU) 2016-10 codifying ASC 606, *Revenue from Contracts with Customers*. This ASU supersedes most existing revenue recognition guidance and provides for a single comprehensive principles-based standard for the recognition of revenue across all industries through the application of the following five-step process:

Step 1: Identify the contract(s) with a customer.

Step 2: Identify the performance obligations in the contract.

Step 3: Determine the transaction price.

Step 4: Allocate the transaction price to the performance obligations in the contract.

Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

MHS adopted the standard on October 1, 2018, using the full retrospective method of transition. The adoption of ASU 2016-10 did not result in changes to previously reported revenues, other than presentation.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain amounts in the 2018 consolidated financial statements have been reclassified to conform to 2019 presentation. These reclassifications had no impact on net assets or the excess of revenues over expenses as of and for the fiscal year ended September 30, 2018, as previously reported.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

3. Affiliation With Southern Illinois University School of Medicine

MHS has entered an affiliation agreement with Southern Illinois University School of Medicine (SIU) in an effort to enhance the quality, sophistication and access of health care in central and southern Illinois. The term of the agreement renewed on July 30, 2015, and automatically renews for successive five-year terms, until terminated by either party. The agreement requires an advance notice of either party's intent to terminate the affiliation agreement to be no less than three years prior to the expiration of the current five-year term. The affiliation agreement allows SIU to conduct both graduate and undergraduate medical educational programs at MHS facilities. In addition, the affiliation allows for both parties (including all of SIU's and MHS's subsidiaries) to execute separate agreements to provide the following: academic support, medical director and/or chairman contracts, administrative services, space leases, recruitment contracts, and/or clinical service contracts. MHS also provides other support and funding in the form of grants to SIU through MMCF.

The table below reports the extent to which MHS and SIU have partnered to strengthen their affiliation:

Agreement type	Years Ended September 30	
	2019	2018
Academic support provided	\$ 40,457	\$ 31,862
Grants and contributions provided	2,561	2,736
Medical director/chairman contracts provided	3,716	2,449
Administrative, clinical, recruitment, and other services provided	632	356
Lease revenues	6,200	5,339
Administrative and clinical service revenues	875	854

All agreement types listed above are included in income from operations on the consolidated statements of operations and changes in net assets, except for grants and contributions provided.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

4. Revenues

Net Patient Service Revenues

MHS provides health care services through inpatient, outpatient, and ambulatory care facilities. Certain patients receive services that are covered by governmental and third-party payments, including Medicare and Medicaid (50.8% and 49.2% of net patient service revenues in 2019 and 2018, respectively), at contractual rates generally below MHS's established rates.

The following is the mix of net patient service revenues by major payor source:

	Years Ended September 30	
	2019	2018
Medicare	\$ 344,397	\$ 327,808
Medicaid	137,963	129,876
Managed care	196,861	202,011
BlueCross BlueShield	214,504	211,386
Other commercial payors	50,489	52,345
Patients	5,343	6,611
Total	\$ 949,557	\$ 930,037

MHS is paid for services rendered to Medicare program beneficiaries generally under prospectively determined rates. Those rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. MMC's and PAH's patients receive reimbursement under the prospective payment system (PPS). TMH and ALMH are both designated as critical access hospitals and receive cost-based reimbursement for the majority of their Medicare services.

Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient and home health services rendered to Medicaid program beneficiaries are reimbursed upon a per visit, per diem rate or on a fee-for-service basis. MHS recognizes that revenues and receivables from government agencies are significant to operations, but it does not believe that there are significant credit risks associated with these government agencies.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

4. Revenues (continued)

The following is the mix of net receivables by major payor source:

	September 30	
	2019	2018
Medicare	27.5%	24.0%
Medicaid	10.7	12.4
Managed care	26.5	27.0
BlueCross BlueShield	19.3	19.5
Other commercial payors	12.2	13.2
Patients	3.8	3.9
Total	<u>100.0%</u>	<u>100.0%</u>

Net receivables percentages included in the table above exclude \$2,097 and \$1,308 in State of Illinois receivables classified as held for sale as of September 30, 2019 and 2018, respectively, and described in Note 5.

Hospital Access Improvement Revenue

On July 1, 2018, the Centers for Medicare and Medicaid Services (CMS) authorized the State of Illinois to reform and modernize the present Hospital Assessment Program with federal matching funds. The revised Hospital Assessment Program replaced the previously existing assessment programs that collectively expired on June 30, 2018. The current Hospital Assessment Program is set to expire on June 30, 2020.

The following is a breakdown of the Illinois Hospital Assessment Program:

	Years Ended September 30	
	2019	2018
Hospital access improvement payments included in net patient service revenue	\$ 57,846	\$ 51,651
Hospital provider assessment	28,519	24,640
Net impact of Illinois Hospital Assessment Program	<u>\$ 29,327</u>	<u>\$ 27,011</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

4. Revenues (continued)

Capitation Revenues

MMC and Springfield Clinic, LLP formed a network on July 1, 1999. The purpose of the network is to collaborate with and assist Health Alliance Medical Plans (HAMP) to arrange for, develop, and maintain a network of participating providers and to provide covered services to plan members in the service area. MMC has an agreement with the network to provide medical services to more than 20,000 members of the network as of both September 30, 2019 and 2018. MMC receives a monthly capitation payment based on the number of members, regardless of services provided by MMC or other providers. As of September 30, 2019 and 2018, MHS has recognized a liability for covered medical claims of \$2,250 and \$2,740, respectively.

5. Sale of Receivables Held for Sale

In June 2018, MMC, PAH, ALMH, TMH, MPS, MEC, MHSvc, and MHSCI (Sellers) assigned their respective rights in \$19,667 of receivables held for sale to McDEKK. Subsequently, McDEKK completed the transfer of its newly assigned rights in those receivables to Illinois Financing Partners (IFP). MHS remained servicer of the transferred assets on behalf of IFP. Terms of the transaction resulted in MHS receiving 100% of its sold receivables in the form of cash consideration on the date of sale from IFP.

Also beginning in June 2018, the Sellers entered into a revolving weekly agreement to assign their respective rights in receivables held for sale to McDEKK. Subsequently, McDEKK transfers its newly assigned rights in those receivables to IFP. MHS remains servicer of the transferred assets on behalf of IFP. Terms of the transaction result in MHS receiving 100% of its sold receivables in the form of cash consideration on the date of sale from IFP. In exchange, MHS has assigned all of its rights in the associated timely pay penalties on assigned receivables to IFP.

MHS has no other continuing involvement with the sold receivables except its role as servicer over the transferred assets to IFP. MHS is paid reasonable compensation by IFP in its role as servicer. Management has determined the transfers meet the criteria to qualify for sale accounting under ASC 860, *Transfers and Servicing*, and has accordingly reported the receivables as sold as of September 30, 2019 and 2018.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

5. Sale of Receivables Held for Sale (continued)

MHS has included certain accounts totaling \$2,097 and \$1,308 as of September 30, 2019 and 2018, respectively, which are owed by the State of Illinois for health care services provided to its employees as held for sale and are included in receivables held for sale in the accompanying consolidated balance sheets. Receivable amounts classified as held for sale are valued based on the adjudicated claim value assigned by the insurance provider.

6. Investments

MHS's investments are exposed to various kinds and levels of risk. Fixed-income securities expose MHS to interest rate risk, credit risk, and liquidity risk. As interest rates change, the value of many fixed-income securities is affected. Credit risk is the risk that the obligor of the security will not fulfill its obligations. Liquidity risk is affected by the willingness of market participants to buy and sell given securities. Equity securities expose MHS to market risk, performance risk, and liquidity risk. Market risk is the risk associated with major movements of the equity markets, both foreign and domestic. Performance risk is the risk associated with a company's operating performance. Liquidity risk, as previously defined, tends to be higher for foreign equities and equities related to small capitalization companies.

The composition of short-term and long-term investments, all at fair market value, is set forth in the following table:

	September 30	
	2019	2018
Cash and cash equivalents	\$ 19,312	\$ 34,159
Certificates of deposit	6,637	24,381
U.S. Treasury obligations	30,733	69,311
Government obligations	35,978	5,689
Corporate obligations	179,545	96,571
Foreign obligations	26,146	9,886
Domestic equities	71,944	78,215
International equities	11,105	5,989
Investment in farmland	27,071	27,811
Mutual funds	154,676	191,622
Equity – commingled funds	153,382	198,013
Accrued interest receivable and other	2,309	1,200
Short-term and long-term investments	\$ 718,838	\$ 742,847

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820, *Fair Value Measurement*, establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). Certain of MHS's financial assets and financial liabilities are measured at fair value on a recurring basis, including investments, beneficial interest in trusts, and interest rate swap agreements. The three levels of the fair value hierarchy and a description of the valuation methodologies used for instruments measured at fair value are as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the reporting date. Level 1 primarily consists of financial instruments such as money market securities and listed equities.

Level 2 – Pricing inputs other than quoted prices included in Level 1, which are either directly observable or can be derived or supported from observable data as of the reporting date. Level 2 inputs may include quoted prices for similar assets and liabilities in non-active markets or pricing models whose inputs are observable for substantially the full term of the asset or liability.

Level 3 – Pricing inputs include those that are significant to the fair value of the financial asset or financial liability and are not observable from objective sources. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

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

Financial instruments categorized as Level 3 consist of investments in farmland and beneficial interest in trusts. Investments in farmland have been valued based on market value appraisals of the corresponding real estate. Beneficial interest in trusts are recorded at fair value based on MHS's interest in the value of the underlying trust assets. Real estate appraisals on land held within the trust are used as unobservable inputs to estimate MHS's allocable portion of trust assets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The fair value of financial assets and financial liabilities measured at fair value on a recurring basis was determined using the following inputs at September 30, 2019:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 19,312	\$ –	\$ –	\$ 19,312
Certificates of deposit	–	6,637	–	6,637
U.S. Treasury obligations	30,733	–	–	30,733
Government obligations	–	35,978	–	35,978
Corporate obligations	–	179,545	–	179,545
Foreign obligations	–	26,146	–	26,146
Domestic equities	71,944	–	–	71,944
International equities	11,105	–	–	11,105
Investments in farmland	–	–	27,071	27,071
Mutual funds equities	154,676	–	–	154,676
Subtotal	<u>287,770</u>	<u>248,306</u>	<u>27,071</u>	<u>563,147</u>
Assets not at fair value:				
Assets measured at net asset value: ¹				
Equity – commingled funds	–	–	–	153,382
Accrued interest and dividends receivable	–	–	–	2,309
Short-term and long-term investments	287,770	248,306	27,071	718,838
Beneficial interest in trusts	–	–	45,387	45,387
Total assets	<u>\$ 287,770</u>	<u>\$ 248,306</u>	<u>\$ 72,458</u>	<u>\$ 764,225</u>
Liabilities				
Interest rate swaps	\$ –	\$ 3,465	\$ –	\$ 3,465

¹ In accordance with ASC 820, certain investments that are measured at fair value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to amounts presented on the consolidated balance sheets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The following table presents the category, fair value, redemption frequency, and redemption notice period for assets, the fair values which are estimated using net asset value per share as of September 30, 2019:

<u>Assets</u>	<u>Fair Value</u>	<u>Unfunded Commitment</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Equity – commingled funds ^a	\$ 153,382	\$ –	Weekly	3 days

^a. Includes investments in domestic large cap equity securities. The fair values of the investments in this class have been estimated using the net asset value per share of the investments.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The fair value of financial assets and financial liabilities measured at fair value on a recurring basis was determined using the following inputs at September 30, 2018:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 34,159	\$ –	\$ –	\$ 34,159
Certificates of deposit	–	24,381	–	24,381
U.S. Treasury obligations	69,311	–	–	69,311
Government obligations	–	5,689	–	5,689
Corporate obligations	–	96,571	–	96,571
Foreign obligations	–	9,886	–	9,886
Domestic equities	78,215	–	–	78,215
International equities	5,989	–	–	5,989
Investments in farmland	–	–	27,811	27,811
Mutual funds equities	191,622	–	–	191,622
Subtotal	379,296	136,527	27,811	543,634
Assets not at fair value:				
Assets measured at net asset value: ¹				
Equity – commingled funds	–	–	–	198,013
Accrued interest and dividends receivable	–	–	–	1,200
Short-term and long-term investments	379,296	136,527	27,811	742,847
Beneficial interest in trusts	–	–	46,111	46,111
Total assets	<u>\$ 379,296</u>	<u>\$ 136,527</u>	<u>\$ 73,922</u>	<u>\$ 788,958</u>
Liabilities				
Interest rate swaps	\$ –	\$ 2,667	\$ –	\$ 2,667

¹ In accordance with ASC 820, certain investments that are measured at fair value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to amounts presented on the consolidated balance sheets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The following table presents the category, fair value, redemption frequency, and redemption notice period for assets, the fair values which are estimated using net asset value per share as of September 30, 2018:

<u>Assets</u>	<u>Fair Value</u>	<u>Unfunded Commitment</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Equity – commingled funds ^a	\$ 146,996	\$ –	Weekly	3 days
Equity – commingled funds ^b	51,017	–	Monthly	10–30 days

^a. Includes investments in domestic large cap equity securities. The fair values of the investments in this class have been estimated using the net asset value per share of the investments.

^b. Includes investments in emerging market equity securities. The fair values of the investments in this class have been estimated using the net asset value per share of the investments.

The table below sets forth a summary of changes in the fair value of MHS’s Level 3 assets for the period from October 1, 2017 to September 30, 2019.

	<u>Beneficial Interest in Trusts</u>	<u>Investments in Farmland</u>	<u>Total</u>
Total as of October 1, 2017	\$ 49,012	\$ 25,370	\$ 74,382
Trust distribution	(3,059)	2,211	(848)
Contributions of farmland	–	408	408
Realized and unrealized gains (losses)	158	(178)	(20)
Total as of September 30, 2018	46,111	27,811	73,922
Trust distribution	(1,048)	–	(1,048)
Contributions of farmland	–	–	–
Realized and unrealized gains (losses)	324	(740)	(416)
Total as of September 30, 2019	<u>\$ 45,387</u>	<u>\$ 27,071</u>	<u>\$ 72,458</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements (continued)

	Years Ended September 30	
	2019	2018
Unrealized losses related to Level 3 financial instruments held	\$ (416)	\$ (20)

8. Property, Plant, and Equipment

The following is a summary of property, plant, and equipment:

	September 30	
	2019	2018
Land	\$ 34,270	\$ 35,301
Land improvements	58,931	57,804
Buildings	716,825	696,581
Equipment	380,668	366,845
Construction-in-progress	78,043	52,364
Subtotal	1,268,737	1,208,895
Less accumulated depreciation	684,753	635,473
Property, plant, and equipment, net	\$ 583,984	\$ 573,422

Capitalized interest was \$284 and \$311 for the fiscal years ended September 30, 2019 and 2018, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

9. Long-Term Debt Obligations

Long-term debt obligations are as follows:

	September 30	
	2019	2018
Obligated Group:		
Tax-exempt Variable Rate Demand Revenue Bonds (Series 2003) at an average annual variable interest rate of 1.20% for the fiscal year ended September 30, 2018, and retired in 2019.	\$ —	\$ 15,080
Taxable Variable Rate Demand Revenue Bonds (Series 2004) at an average annual variable interest rate of 1.66% for the fiscal year ended September 30, 2018, and retired in 2019.	—	10,025
Tax-exempt Revenue Bonds (Series 2009) secured by pledged revenues of the MHS Obligated Group at an annual fixed interest rate of 5.00% as of September 30, 2018, and retired in 2019.	—	85,208
Taxable Direct Note Obligation 2012C at a stated annual fixed interest rate of 4.32% as of September 30, 2019 and 2018.	47,156	49,557
Tax-exempt Revenue Bonds (Series 2014A) secured by pledged revenues of the MHS Obligated Group at an annual fixed interest rate of 5.00% as of September 30, 2019 and 2018.	56,625	57,805
Tax-Exempt Variable Rate Revenue Bonds (Series 2014B), privately placed, puttable starting in 2024, at an annual variable interest rate of 2.40% and 1.96% for the fiscal years ended September 30, 2019 and 2018, respectively.	56,275	57,565
Taxable Direct Note Obligation 2016 secured by pledged revenues of the MHS Obligated Group at an average variable rate of 3.19% and 2.13% for the fiscal years ended September 30, 2019 and 2018, respectively.	15,000	30,000
Tax-exempt Revenue Bonds (Series 2019) secured by pledged revenues of the MHS Obligated Group at an annual fixed interest rate of 5.00% as of September 30, 2019.	130,005	—
Obligated Group debt subtotal	305,061	305,240

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

9. Long-Term Debt Obligations (continued)

	September 30 2019	September 30 2018
Other entities:		
Indenture issued to ALMH as part of the tax-exempt revenue bonds (Series 2009) secured by pledged revenues of the MHS Obligated Group at an annual fixed rate of 5.00% as of September 30, 2018, and retired in 2019.	\$ —	\$ 41,530
Indenture issued to TMH as part of the tax-exempt revenue bonds (Series 2009) secured by pledged revenues of the MHS Obligated Group at an annual fixed rate of 5.00% as of September 30, 2018, and retired in 2019.	—	17,797
Tax-Exempt Variable Rate Revenue Refunding Bonds (Series 2015), privately placed issued by PAH and guaranteed by the Obligated Group, puttable starting in 2025, at an annual variable interest rate of 2.83% and 2.10% for the fiscal years ended September 30, 2019 and 2018, respectively.	18,916	20,224
Total long-term obligations	323,977	384,791
Less current installments of long-term obligations	11,117	12,945
Less unamortized debt issuance costs, discounts, and (premiums)	(15,814)	787
Long-term debt obligations, net	\$ 328,674	\$ 371,059

All of MHS's debt is under an amended and restated Master Trust Indenture (MTI) dated December 1, 2009. Currently, the Parent and MMC are the corporations that are Obligated Group members under the MTI. The MTI requires the Obligated Group to maintain debt covenants, including meeting a minimum debt service coverage ratio, minimum days cash on hand, and a minimum rating requirement, all as defined in the MTI. Management believes MHS is in compliance with these covenants and conditions as of September 30, 2019.

During 2019, the Series 2019 bonds were issued in the amount of \$130,005 at a premium of \$18,432. The Series 2019 bond proceeds were used to current refund the Series 2009 bonds and reimburse members of the Obligated Group for costs incurred in the construction, renovation, remodeling and equipping of certain MHS facilities.

MHS maintained letters of credit with JP Morgan Chase Bank supporting the Series 2003 and Series 2004 bonds. As of September 30, 2019, the letters of credit have been cancelled with the retiring of both the Series 2003 and Series 2004 bonds in 2019.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

9. Long-Term Debt Obligations (continued)

Aggregate maturities of long-term obligations at September 30, 2019, are as follows:

Fiscal year ending September 30	
2020	\$ 11,117
2021	11,590
2022	11,999
2023	12,647
2024	13,170
Thereafter	263,454
Total	<u>\$ 323,977</u>

Interest expense is \$14,965 and \$16,085 for the fiscal years ended September 30, 2019 and 2018, respectively.

The valuation for the estimated fair value of long-term debt is completed by a third-party service and takes into account a number of factors, including, but not limited to, any one or more of the following: (i) general interest rate and market conditions; (ii) macroeconomic and/or deal-specific credit fundamentals; (iii) valuations of other financial instruments that may be comparable in terms of rating, structure, maturity, and/or covenant protection; (iv) investor opinions above the respective deal parties; (v) size of the transaction; (vi) cash flow projections, which in turn are based on assumptions about certain parameters that include, but are not limited to, default, recovery, prepayment, and reinvestment rates; (vii) administrator reports, asset manager estimates, broker quotations, and/or trustee reports; and (viii) comparable trades, where observable. Based on the inputs in determining the estimated fair value of debt, this liability is considered to be Level 2 measurement. The estimated fair value of long-term debt at September 30, 2019 and 2018, based on quoted market prices for the same or similar issues was \$355,978 and \$390,791, respectively, which includes consideration of third-party credit enhancements, of which there is no impact.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

10. Derivatives

MHS has interest rate-related derivative instruments to manage its exposure on its variable-rate debt instruments and does not enter into derivative instruments for any purpose other than risk management purposes. The objective of these interest swaps is to mitigate interest rate fluctuations and synthetically fix the interest rate of the related bond series. Interest rate swap contracts between MHS and a third party (counterparty) provide for the periodic exchange of payments between the parties based on changes in a defined index and a fixed rate and expose MHS to market risk and credit risk. Credit risk is the risk that contractual obligations of the counterparties will not be fulfilled.

Concentrations of credit risk relate to groups of counterparties that have similar economic or industry characteristics, which could cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Counterparty credit risk is managed by requiring high credit standards for MHS's counterparties. The counterparties to these contracts are financial institutions that carry investment-grade credit ratings. MHS does not anticipate nonperformance by its counterparties. Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates. The market risk associated with interest rate changes is managed by established and monitoring parameters, which limit the types and degree of market risk that may be undertaken. Management also mitigates risk through periodic reviews of MHS's derivative positions in the context of its blended cost of capital.

The following is a summary of the outstanding positions under these interest rate swap agreements, which are long-term liabilities:

<u>Expiration Date</u>	<u>MHS Pays</u>	<u>MHS Receives</u>	<u>Notional Amount</u>	<u>Fair Value</u>		<u>Gain (Loss) on Derivatives</u>	
				<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
October 1, 2022	3.69%	70% of LIBOR	\$ 12,580	\$ 582	\$ 572	\$ (265)	\$ 240
October 1, 2024	4.99%	100% of LIBOR	8,360	668	560	(327)	253
December 1, 2031	2.95%	67% of LIBOR	12,840	1,056	796	(437)	45
December 1, 2031	3.45%	67% of LIBOR	7,630	1,159	739	(564)	258
			<u>\$ 41,410</u>	<u>\$ 3,465</u>	<u>\$ 2,667</u>	<u>\$ (1,593)</u>	<u>\$ 796</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

11. New Markets Tax Credit Program

QALICB is party to a 35-year loan agreement for \$16,770 with a direct lender through the U.S. Department of the Treasury Community Development Financial Institution (CDFI) Fund New Markets Tax Credit (NMTC) Program for reimbursement of certain capital expenditures which qualify as a Qualified Low Income Community Investment (QLICI). The loan (QLICI notes payable) bears annual interest at a fixed rate of 0.98% and has a bilateral put/call option that becomes effective in December 2022. The QLICI notes payable are reported as other noncurrent liabilities on the consolidated balance sheets. To facilitate the NMTC transaction, MMC concurrently loaned \$11,628 to a newly created special purpose entity (SPE). This note receivable owed from the SPE is reported in other assets in the non-current section of the consolidated balance sheets.

Upon maintaining compliance under the NMTC program, management expects the bilateral put/call option to be exercised in 2022, which will trigger the transaction structure to unwind and result in immediate cancelation of the QLICI notes payable and note receivable balances. As a result, management anticipates recognizing a gain of \$5,142 on the consolidated statement of operations and changes in net assets in 2022. Total interest expense on the QLICI notes payable totaled \$169 and \$166 for the fiscal years ended September 30, 2019 and 2018, respectively. Total interest income on the notes receivable totaled \$116 for both the fiscal years ended September 30, 2019 and 2018.

12. Liability Programs

MHS is involved in litigation arising in the ordinary course of business. Claims alleging professional or general liability have been asserted against MHS and are currently in various stages of litigation. MHS is self-insured for claims of up to \$1,000 individually and \$6,000 in the aggregate and has commercial claims-made excess insurance coverage up to \$25,000 per claim and \$25,000 in the aggregate.

Accruals related to the estimated self-insurance liability and the corresponding charge to expense are actuarially determined for asserted and unasserted claims using historical claims experience and other relevant industry and hospital-specific factors and trends, discounted at an annual interest rate of 1.84% and 2.73% as of September 30, 2019 and 2018, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

12. Liability Programs (continued)

The general and professional liability was \$13,915 and \$14,017 at September 30, 2019 and 2018, respectively, including tail coverage on the claims-made policy. Insurance receivables related to excess coverage are \$2,835 and \$2,861 at September 30, 2019 and 2018, respectively. Amounts charged to purchased services and other expense in the consolidated statements of operations and changes in net assets are as follows:

	Years Ended September 30	
	2019	2018
Self-insurance	\$ 3,560	\$ 1,122
Insured	2,019	2,206
Total	<u>\$ 5,579</u>	<u>\$ 3,328</u>

MHS maintains a revocable general and professional liability trust fund containing investments of \$10,208 and \$9,592 at September 30, 2019 and 2018, respectively.

MHS also provides for workers' compensation through a self-insurance trust or through insured programs. The funding level for this trust and estimation of the related liability are actuarially determined. Amounts charged to expense for this coverage for the fiscal years ended September 30, 2019 and 2018, were \$703 and \$287, respectively, and are included in employee benefits in the consolidated statements of operations and changes in net assets. The workers' compensation liability was \$4,171 and \$4,278 at September 30, 2019 and 2018, respectively, discounted at 1.82% and 2.63% as of September 30, 2019 and 2018, respectively. The insurance receivable related to excess coverage is \$486 and \$375 at September 30, 2019 and 2018, respectively. MHS maintains a revocable workers' compensation liability trust fund containing investments of \$4,367 and \$4,250 at September 30, 2019 and 2018, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans

Defined Benefit Plans

The MHS defined benefit pension plan (MHS Pension) covers substantially all of the employees of MHS, MMC, MPS and MHSvc who began employment prior to January 1, 2012. Contributions are made to the plans to meet the target funding level established by management and have exceeded the net pension cost each year. On December 31, 2011, the MHS Pension was frozen for participation and benefit accumulation. The benefits are based on years of service and the employee's compensation during the highest five consecutive years of the last ten years of employment prior to being frozen. Unvested participants on December 31, 2011, are still eligible to vest assuming service period requirements are met.

MHS also has a supplemental retirement defined benefit plan (MHS Restoration) covering MHS and MMC executives, which was frozen to new participants on December 31, 2009. Eligible participants in the MHS Restoration as of January 1, 2010, will continue to accrue benefits. The MPS Pension Restoration Plan covered physicians and was frozen for both new participation and benefits accruals as of December 31, 2011. Both restoration plans were designed to cover participants whose annual compensation exceeds the Internal Revenue Service cap limits for pension plan contributions and are unfunded.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

The following table sets forth the benefit obligation and assets of MHS's defined benefit plans' funded status as recognized in MHS's consolidated balance sheets:

	September 30	
	2019	2018
Change in benefit obligation:		
Benefit obligation – beginning of year	\$ 442,223	\$ 466,903
Service cost	184	432
Interest cost	19,456	18,910
Actuarial loss (gain)	72,839	(20,886)
Benefits paid	(18,850)	(23,136)
Benefit obligation – end of year	515,852	442,223
Change in plan assets:		
Fair value of plan assets – beginning of year	453,371	458,360
Actual gain on plan assets	68,928	11,242
Employer contribution	649	6,905
Benefits paid	(18,850)	(23,136)
Fair value of plan assets – end of year	504,098	453,371
(Underfunded) over-funded status, net	\$ (11,754)	\$ 11,148

Funded status consists of \$11,754 of unfunded benefit obligation as of September 30, 2019. The funded status as of September 30, 2018, includes an unfunded liability of \$7,502 for the MHS Restoration plan and a net pension asset of \$18,650 recorded in other assets on the consolidated balance sheet.

Amounts recognized in net assets without donor restrictions consist of the following:

	September 30	
	2019	2018
Unrecognized actuarial loss	\$ 145,444	\$ 123,825

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

Changes in plan assets and benefit obligations recognized in net assets without donor restrictions include the following:

	Years Ended September 30	
	2019	2018
Current actuarial loss (gain)	\$ 29,641	\$ (2,905)
Amortization of loss	(11,387)	(13,706)
Settlement charge (benefit)	1,581	(3,614)
	\$ 19,835	\$ (20,225)

The actuarial loss included in net assets without donor restrictions expected to be recognized in net periodic pension cost during the year ending September 30, 2020, is \$13,154.

Components of net periodic benefit cost are as follows:

	Years Ended September 30	
	2019	2018
Service cost	\$ 184	\$ 432
Interest cost	19,456	18,910
Expected return on plan assets	(25,730)	(29,222)
Amortization of net loss and prior service cost	11,387	13,706
Settlement charge (benefit)	(1,581)	3,614
Net periodic benefit cost	\$ 3,716	\$ 7,440

No plan assets are expected to be returned to MHS during the fiscal year ending September 30, 2020.

The accumulated benefit obligations were \$513,681 and \$440,954 at September 30, 2019 and 2018, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

Assumptions

Weighted average assumptions used to determine benefit obligations are as follows:

	September 30	
	2019	2018
Discount rate	3.35%	4.50%
Expected long-term return on plan assets	5.80	5.80

The effects of the changes in actuarial assumptions from 2018 to 2019, which include a revision to the assumed mortality table, increased the projected benefit obligation and the accumulated benefit obligation by \$71,022 and \$70,545, respectively, at September 30, 2019. The effects of the changes in actuarial assumptions from 2017 to 2018, which include a revision to the assumed mortality table, decreased the projected benefit obligation and the accumulated benefit obligation by \$23,649 and \$23,582, respectively, at September 30, 2018.

Weighted average assumptions used to determine net periodic benefit costs are as follows:

	Years Ended September 30	
	2019	2018
Discount rate	4.50%	4.16%
Expected long-term return on plan assets	5.80	6.50

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

The weighted average asset allocation by asset category is as follows:

	Target Asset Allocation 2019	September 30 2019	Target Asset Allocation 2018	September 30 2018
Equity securities	20.0%	16.4%	20.0%	19.4%
Debt securities	80.0	83.1	80.0	79.7
Cash and cash equivalents	–	0.5	–	0.9
Total	100.0%	100%	100.0%	100.0%

The fair value of plan assets measured at fair value was determined using the following inputs at September 30, 2019:

	Level 1	Level 2	Level 3	Total
Assets				
Money market funds	\$ 2,426	\$ –	\$ –	\$ 2,426
U.S. Treasury obligations	35,604	–	–	35,604
Government obligations	–	57,527	–	57,527
Corporate obligations	–	322,234	–	322,234
Mutual funds	54,878	–	–	54,878
Subtotal	92,908	379,761	–	472,669
Assets not at fair value:				
Assets measured at net asset value ¹	–	–	–	27,640
Accrued interest and dividends receivable	–	–	–	3,789
Total assets	\$ 92,908	\$ 379,761	\$ –	\$ 504,098

¹ In accordance with ASC 820, certain investments that are measured at fair value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to amounts presented on the consolidated balance sheets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

The following table presents the category, fair value, redemption frequency, and redemption notice period for assets, the fair values which are estimated using net asset value per share as of September 30, 2019:

<u>Assets</u>	<u>Fair Value</u>	<u>Unfunded Commitment</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Equity – commingled funds ^a	\$ 27,640	\$ –	Weekly	3 days

^a. Includes investments in domestic small cap equity securities. The fair values of the investments in this class have been estimated using the net asset value per share of the investments.

The fair value of plan assets measured at fair value was determined using the following inputs at September 30, 2018:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets				
Money market funds	\$ 3,951	\$ –	\$ –	\$ 3,951
U.S. Treasury obligations	73,055	–	–	73,055
Government obligations	–	28,500	–	28,500
Corporate obligations	–	257,086	–	257,086
Domestic equities	53,272	–	–	53,272
Mutual funds	34,639	–	–	34,639
Subtotal	164,917	285,586	–	450,503
Assets not at fair value:				
Accrued interest and dividends receivable	–	–	–	2,868
Total assets	<u>\$ 164,917</u>	<u>\$ 285,586</u>	<u>\$ –</u>	<u>\$ 453,371</u>

At September 30, 2019 and 2018, fair value methodologies for Level 1 and Level 2 assets are consistent with the inputs described in Note 7. There are no Level 3 assets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

Investment managers are employed to invest pension fund assets in a structured portfolio governed by management policy consisting of fixed income and equity securities. The fixed income portion of the total portfolio has been constructed to hedge the corresponding plans liabilities under a strategy referred to as liability driven investing. This strategy reduces risk of deterioration in the plan's overall funded status. Investment performance is monitored and compared against stated management policy investment objectives. The plan's structured portfolio also takes into consideration the cash flow requirements of the plan to provide for the monthly payout of benefits required. Projected rates of return for each asset category were selected after analyzing historical experience and future expectations of the returns and volatility for assets of the category.

During the fiscal year ending September 30, 2020, MHS does not anticipate making any material contributions to the plan.

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

Fiscal year ending September 30	
2020	\$ 22,283
2021	23,087
2022	24,643
2023	23,752
2024	24,641
2025–29	133,687

Defined Contribution Plans

The Defined Contribution Plan is intended to qualify as a profit-sharing plan under Code Section 401(a) and includes a cash or deferred arrangement that is approved to qualify under Code Section 401(k). The plan allows employee contributions and an employer matching contribution of up to 3% of eligible pay and provides a discretionary service-based employer contribution of between 3% and 7%. All eligible employees of MHS, MMC, MPS, MHSvc, MBH, PAH, ALMH and TMH are included in the Defined Contribution Plan.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Retirement Plans (continued)

MHS contributes the employer match throughout the year, as the employee contributes to the plan through payroll deduction. The services-based contributions for the Defined Contribution Plan calendar plan year are discretionary and subject to approval by the MHS Board of Directors. As of December 17, 2019, no approval of contribution has been made for plan calendar year 2019. PAH sponsored two defined contribution plans with an employer match provision, the PAH Tax Deferred Annuity Plan and the PAH Employees' Pension Plan. Both plans were frozen on December 31, 2018. The PAH Employees' Pension Plan was merged into the Defined Contribution Plan on July 29, 2019. The PAH Tax Deferred Annuity Plan was merged with other frozen legacy plans into an MHS 403(b) Plan.

MHS also has a Defined Contribution Restoration Plan. This plan is intended to qualify as an eligible deferred compensation plan under Code Section 457(b). Through December 31, 2017, this plan excluded anyone eligible to receive a benefit under the MHS Restoration plan. The plan was amended and restated January 1, 2018, providing that no employer contributions will be made after December 31, 2017, an employee deferral option was added for all eligible employees and renamed the Memorial Health System 457(b) Deferral Plan.

Defined contribution retirement expense for the plans previously mentioned is as follows:

	Years Ended September 30	
	2019	2018
MHS Defined Contribution Plan	\$ 23,705	\$ 20,741
MHS Defined Contribution Restoration Plan	–	513
PAH Tax Deferred Annuity and Employees' Pension Plans	401	2,018
Total retirement expense	\$ 24,106	\$ 23,272

14. Post-Employment and Other Benefits

MHS and PAH provide unfunded post-employment benefit plans to certain employees. The costs for these plans were \$949 and \$869 for the fiscal years ended September 30, 2019 and 2018, respectively. As of September 30, 2019 and 2018, the accumulated post-employment benefit obligation was \$13,698 and \$11,989, respectively. Annual discount rates ranged from 3.35% to 4.50%. The plans assume a medical plan trend rate of 6.75% in 2019 grading down to the ultimate rate of 4.03% in 2075.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

14. Post-Employment and Other Benefits (continued)

A one-percentage-point increase in the assumed medical plan trend rates would have increased the accumulated post-employment benefit obligation by \$2,206 and \$1,762 at September 30, 2019 and 2018, respectively. A one-percentage-point decrease in the assumed medical plan trend rates would have decreased the accumulated post-employment benefit obligation by \$1,752 and \$1,414 at September 30, 2019 and 2018, respectively.

Included in net assets without donor restrictions are the following amounts that have not yet been recognized in net periodic post-employment benefit cost:

	September 30	
	<u>2019</u>	<u>2018</u>
Unrecognized actuarial losses	\$ 4,736	\$ 3,005

Other post-employment and other benefit plans liabilities include continuation of medical benefits to employees on long-term disability, sick time paid to employees upon retirement, and the paid sick time program to current active employees, which were \$5,610 and \$6,232 at September 30, 2019 and 2018, respectively.

15. Operating Leases

Revenues

Rental revenues were \$16,599 and \$15,152 for the fiscal years ended September 30, 2019 and 2018, respectively, from non-MHS entities. As of September 30, 2019 and 2018, the cost of the buildings held for lease was \$165,201 and \$155,737, respectively, and the related accumulated depreciation was \$70,349 and \$54,943, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

15. Operating Leases (continued)

Future minimum rental revenue under noncancelable operating leases as of September 30, 2019, which have initial or remaining terms in excess of one year, is as follows:

Fiscal years ending September 30	
2020	\$ 11,497
2021	9,460
2022	9,109
2023	8,617
2024	6,767
Thereafter	39,005
Total minimum lease revenue	<u>\$ 84,455</u>

Expenses

Rental expense was \$3,762 and \$2,996 for the fiscal years ended September 30, 2019 and 2018, respectively.

Future minimum rental payments under noncancelable operating leases as of September 30, 2019, which have initial or remaining terms in excess of one year, are as follows:

Fiscal years ending September 30	
2020	\$ 1,741
2021	1,544
2022	1,100
2023	620
2024	90
Thereafter	51
Total minimum lease payment	<u>\$ 5,146</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

16. Commitments and Contingencies

Firm commitments for construction-in-progress totaled \$28,498 as of September 30, 2019.

Regulatory Compliance

The U.S. Department of Justice and other federal and state agencies are increasing resources dedicated to regulatory investigations and compliance audits of health care providers. MHS is not exempt from these regulatory efforts and has received inquiries from federal and state agencies with regard to such initiatives. In consultation with legal counsel, management estimates these matters will be resolved without material adverse effect on MHS's consolidated balance sheets or consolidated statements of operations and changes in net assets. MHS has a formal corporate compliance function, which management believes will help monitor MHS's compliance with applicable laws and regulations.

Litigation

MHS is involved in litigation arising in the normal course of business. After consultation with legal counsel, it is management's opinion that these matters will be resolved without a material adverse effect on MHS's consolidated balance sheets or consolidated statements of operations and changes in net assets.

17. Subsequent Events

MHS evaluated events and transactions occurring subsequent to September 30, 2019, through December 17, 2019, the date the consolidated financial statements were issued.

On October 1, 2019, the Parent entered into an affiliation agreement (the Affiliation Agreement) with Decatur Memorial Hospital (DMH) and its wholly owned subsidiaries to become the sole corporate member of DMH. DMH's wholly owned subsidiaries include Heartland Risk Management Company, a captive insurance subsidiary, and Decatur Memorial Hospital Foundation. The transaction will be accounted for as an acquisition, and acquired assets and liabilities will be recorded at fair value on the date of the affiliation. The Parent and DMH share a mission of providing the highest quality health care services to the communities each serves in central Illinois. The Affiliation Agreement will result in all parties being in the best position to

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

17. Subsequent Events (continued)

continue and strengthen the high-quality health care services each delivers, and to meet the clinical, financial and technological demands of delivering health care in central Illinois, by exploring initiatives that enhance the missions and clinical, operational, management and financial strengths of each party.

The following unaudited pro forma financial results are for the fiscal year ended September 30, 2019. These results reflect the addition of DMH's unaudited results for the fiscal years ended September 30, 2019, to MHS's results for the fiscal year ended September 30, 2019. These results do not include the addition to excess of revenues over expenses that would have occurred on October 1, 2018, for the contribution of DMH's net assets.

	<u>2019</u>
Total operating revenues	\$ 1,362,402
Income from operations	8,508
Excess of revenues over expenses	18,370

The pro forma information provided is a compilation of results only and should not be construed to accurately reflect what the actual results would have been had the affiliation been consummated on October 1, 2018, and is not intended to project MHS's results of operations for any future periods. Due to the timing of the acquisition occurring after the balance sheet date, the acquisition date fair values of the tangible and intangible assets acquired and liabilities assumed has not yet been finalized.

Supplementary Information

**MEMORIAL HEALTH SYSTEM
CONSOLIDATING BALANCE SHEET
SEPTEMBER 30, 2019**
(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP					SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	TOTAL	
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF			PAHF
Assets																		
Current assets:																		
Cash and cash equivalents	\$ 27,156	2,934	21,173	6,998	6,348	66	1,652	5,247	1,192	100	15,139	611	1,439	236	134	940	-	91,365
Short-term investments	16,085	2,771	7,063	34,939	-	-	1,927	3,093	-	-	-	-	3,433	211	206	-	-	69,728
Assets whose use is limited	7,267	-	-	-	-	-	94	118	-	-	-	86	-	-	-	-	-	7,565
Receivables:																		
Patient accounts receivable	118,840	23,563	10,875	6,953	7,386	101	731	4,183	-	-	-	-	-	-	-	-	-	172,632
Allowance for implicit price concessions	(15,744)	(2,408)	(2,425)	(1,810)	(1,779)	-	(149)	(161)	-	-	-	-	-	-	-	-	-	(24,476)
Net patient accounts receivable	103,096	21,155	8,450	5,143	5,607	101	582	4,022	-	-	-	-	-	-	-	-	-	148,156
Receivables from third-party payors	10,905	37	-	382	-	-	-	-	-	-	-	-	-	-	-	-	-	11,324
Due from affiliates	313	71	181	320	279	68	116	30	-	54	226	-	-	-	1	-	(1,659)	-
Receivables held for sale	1,666	86	38	122	152	-	-	33	-	-	-	-	-	-	-	-	-	2,097
Other receivables	14,144	143	330	293	2,612	61	552	879	2	4,790	2,022	105	237	471	10	20	(997)	25,674
Inventories	10,812	1,646	632	386	985	-	-	493	-	-	-	-	-	-	-	-	-	14,954
Prepaid expenses	4,837	958	227	496	313	-	161	63	-	395	8,250	-	123	-	3	-	(330)	15,496
Total current assets	196,281	29,801	38,094	49,079	16,296	296	5,084	13,978	1,194	5,339	25,637	802	5,232	918	354	960	(2,986)	386,359
Long-term investments:																		
Unrestricted investments	399,739	80,424	46,251	1,223	-	-	10,810	209	-	-	3,645	-	17,427	26,307	4,705	3,616	-	594,356
Assets whose use is limited:																		
Self-insurance trusts	11,569	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	11,569
Donor-restricted assets and other	1,103	3,393	-	-	-	-	114	83	-	-	-	222	12,380	269	338	418	-	18,320
Deferred compensation assets	2,099	603	15	57	8,594	-	-	-	-	-	5,932	-	-	-	-	-	-	17,300
Total assets whose use is limited	14,771	3,996	15	57	8,594	-	114	83	-	-	5,932	222	12,380	269	338	418	-	47,189
Total long-term investments	414,510	84,420	46,266	1,280	8,594	-	10,924	292	-	-	9,577	222	29,807	26,576	5,043	4,034	-	641,545
Property, plant, and equipment, net	262,551	38,673	30,276	45,189	5,962	28	3,586	1,802	-	-	178,056	17,459	-	402	-	-	-	583,984
Other assets:																		
Investments in partnerships	-	-	-	-	-	-	21	-	8,346	-	779	-	-	-	-	-	(2,531)	6,615
Interest in net assets of foundation	29,279	4,918	27,806	5,392	-	-	-	-	-	-	-	-	-	-	-	-	(67,395)	-
Beneficial interest in trusts	27,819	17,568	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	45,387
Other	15,181	2,776	293	44	-	-	-	114	-	-	4,359	-	1,043	-	-	-	-	23,810
Total other assets	72,279	25,262	28,099	5,436	-	-	21	114	8,346	-	5,138	-	1,043	-	-	-	(69,926)	75,812
TOTAL ASSETS	\$ 945,621	178,156	142,735	100,984	30,852	324	19,615	16,186	9,540	5,339	218,408	18,483	36,082	27,896	5,397	4,994	(72,912)	1,687,700
Liabilities and net assets																		
Current liabilities:																		
Long-term debt	\$ 6,463	1,327	-	455	-	-	-	-	-	-	2,872	-	-	-	-	-	-	11,117
Accounts payable	45,492	2,062	1,618	5,435	5,308	46	48	2,068	2,078	7,537	-	45	14	5	-	-	(633)	71,123
Accrued payroll	25,650	4,605	2,526	2,961	2,840	96	1,203	823	75	5,876	-	-	-	-	2	-	-	46,657
Interest payable	4,172	40	-	524	-	-	-	-	-	614	-	-	-	-	-	-	-	5,350
Due to affiliates	634	200	29	3	224	-	348	96	-	60	142	95	76	-	-	-	(1,907)	-
Payables to third-party payors	34,404	6,136	3,747	2,532	-	-	-	-	-	-	-	-	-	-	-	-	-	46,819
Other	6,292	2,771	68	31	2,964	27	105	53	-	375	4,083	-	1,194	-	-	-	(446)	17,517
Total current liabilities	123,107	17,141	7,988	11,941	11,336	169	1,704	3,040	-	2,528	21,042	142	1,334	90	5	2	(2,986)	198,583
Noncurrent liabilities:																		
Long-term debt obligations, net	235,011	17,550	-	17,537	-	-	-	-	-	-	58,576	-	-	-	-	-	-	328,674
Deferred compensation and benefits	3,686	603	15	57	8,836	-	-	-	-	-	9,013	-	-	-	-	-	-	22,210
Self-insurance accrued expenses	12,737	3,610	442	206	522	110	-	162	-	249	-	-	-	-	-	-	-	18,038
Accrued employee benefits	5,002	1,196	-	-	7,198	-	103	160	-	4,395	-	-	-	-	-	-	-	18,054
Pension obligations	2,458	-	-	-	799	-	-	-	-	4,124	-	-	-	-	-	-	-	7,381
Other	1,390	2,307	-	446	-	-	-	-	-	807	16,571	106	-	-	-	-	-	21,627
Total noncurrent liabilities	260,284	25,266	457	18,246	17,355	110	103	322	-	77,164	16,571	106	-	-	-	-	-	415,984
Total liabilities	383,391	42,407	8,445	30,187	28,691	279	1,807	3,362	-	2,528	98,206	16,713	1,440	90	5	2	(2,986)	614,567
Net assets:																		
Without donor restrictions	523,271	113,971	134,021	70,459	2,161	45	16,853	12,623	9,540	2,811	120,202	1,770	21,380	27,537	5,054	3,945	(58,309)	1,007,334
With donor restrictions	38,959	21,778	269	338	-	-	955	201	-	-	-	-	13,262	269	338	1,047	(11,617)	65,799
Total net assets	562,230	135,749	134,290	70,797	2,161	45	17,808	12,824	9,540	2,811	120,202	1,770	34,642	27,806	5,392	4,992	(69,926)	1,073,133
TOTAL LIABILITIES AND NET ASSETS	\$ 945,621	178,156	142,735	100,984	30,852	324	19,615	16,186	9,540	5,339	218,408	18,483	36,082	27,896	5,397	4,994	(72,912)	1,687,700

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED SEPTEMBER 30, 2019

(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP					SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	TOTAL		
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF			PAHF	
Gross patient service charges:																			
Inpatient charges	\$ 1,263,052	107,595	21,612	17,816	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,410,075
Outpatient charges	1,209,695	307,946	119,803	99,107	134,418	2,102	15,959	28,419	-	-	-	-	-	-	-	-	-	-	1,917,050
Total gross patient service charges	2,472,747	415,541	141,415	116,923	134,418	2,102	15,959	28,419	-	-	-	-	-	-	-	-	-	-	3,327,125
Deductions from charges:																			
Financial assistance (charity)	9,455	2,845	401	494	26	-	160	32	-	-	-	-	-	-	-	-	-	-	13,413
Explicit price concessions (contractual allowances)	1,794,260	298,500	82,231	65,920	84,549	1,575	2,853	10,764	-	-	-	-	-	-	-	-	-	-	2,340,652
Implicit price concessions (provision for uncollectible accounts)	8,900	6,982	2,666	2,585	1,928	-	48	394	-	-	-	-	-	-	-	-	-	-	23,503
Total deductions from charges	1,812,615	308,327	85,298	68,999	86,503	1,575	3,061	11,190	-	-	-	-	-	-	-	-	-	-	2,377,568
Net patient service revenues	660,132	107,214	56,117	47,924	47,915	527	12,898	17,229	-	-	-	-	-	-	-	-	-	-	949,557
% of total gross patient service charges	26.7%	25.8%	39.7%	41.0%	35.6%	25.1%	80.8%	60.6%	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	28.5%
Capitation revenues	63,682	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	63,682
Other revenues:																			
Management fees	-	-	-	-	-	-	-	-	-	-	62,265	-	-	-	-	-	-	-	(62,265)
Other	10,955	1,629	247	207	1,157	96	528	99	(399)	5,010	23,021	1,989	-	-	-	-	-	-	30,300
Total other revenues	10,955	1,629	247	207	1,157	96	528	99	(399)	5,010	85,286	1,989	-	-	-	-	-	-	(76,504)
Total revenues	734,769	108,843	56,364	48,131	49,072	623	13,426	17,328	(399)	5,010	85,286	1,989	-	-	-	-	-	(76,903)	1,043,539
Expenses:																			
Salaries and wages	227,217	46,586	18,139	16,182	45,998	1,168	8,482	8,989	6	2,123	29,630	132	-	-	-	-	-	-	404,652
Employee benefits	53,047	15,724	5,624	5,459	12,687	273	2,620	2,925	2	624	7,277	39	-	-	-	-	-	-	(331)
Physician fees	66,840	8,003	4,564	3,123	31	-	10	59	-	391	-	-	-	-	-	-	-	-	83,021
Utilities	7,528	1,278	496	695	249	14	335	148	-	27	3,621	150	-	-	-	-	-	-	(1,364)
Pharmaceutical supplies	28,392	4,306	1,272	1,112	3,560	-	-	219	-	20	-	-	-	-	-	-	-	-	38,881
Patient service supplies	89,241	7,459	1,864	1,915	1,465	-	-	352	-	-	-	-	-	-	-	-	-	-	102,296
System management fee	50,414	2,442	1,388	1,213	3,371	-	735	806	7	504	-	-	-	-	-	-	-	-	(60,880)
Purchased services and other	75,079	12,550	4,685	4,310	10,318	344	1,101	3,157	7	3,241	24,589	117	-	-	-	-	-	-	(13,701)
Hospital provider assessment	22,292	3,433	1,521	1,273	-	-	-	-	-	-	-	-	-	-	-	-	-	-	28,519
Purchased medical services	33,098	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(500)
Depreciation	33,892	4,324	4,048	3,871	612	45	414	827	-	-	17,376	1,421	-	-	-	-	-	-	66,830
Amortization of debt issuance expenses	(571)	7	-	(98)	-	-	-	-	-	-	(50)	61	-	-	-	-	-	-	(651)
Interest expense and other financing costs	9,680	535	1,120	672	-	-	-	-	-	-	2,843	212	-	-	-	-	-	-	15,062
Total expenses	696,149	106,647	44,721	39,727	78,291	1,844	13,697	17,482	22	6,930	85,286	2,132	-	-	-	-	-	-	(76,776)
Income (loss) from operations	38,620	2,196	11,643	8,404	(29,219)	(1,221)	(271)	(154)	(421)	(1,920)	-	(143)	-	-	-	-	-	-	(127)
% of total operating revenue	5.3%	2.0%	20.7%	17.5%	(59.5%)	(196.0%)	(2.0%)	(0.9%)	(105.5%)	(38.3%)	0.0%	(7.2%)	NA	NA	NA	NA	NA	NA	2.6%
Nonoperating gains (losses):																			
Interest and dividends	4,603	851	1,183	1,010	510	-	163	97	2	-	470	1	356	329	59	71	-	-	9,705
Realized gain on investments, net	7,233	971	375	150	-	-	184	21	-	-	114	-	323	140	77	9	-	-	9,597
Unrealized gain (loss) on investments, net	1,766	(242)	(690)	211	(572)	-	300	13	-	-	(596)	-	(155)	351	14	(37)	-	-	363
Loss on derivatives	(201)	(1,001)	-	-	-	-	-	-	-	-	(391)	-	-	-	-	-	-	-	(1,593)
(Loss) gain on extinguishment of debt	(386)	-	(67)	(108)	-	-	-	-	-	-	(170)	-	-	-	-	-	-	-	(731)
Change in interest in net assets of foundations	1,117	(43)	481	67	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(1,622)
Provision for income taxes	1,009	178	54	-	(5)	-	(266)	54	-	-	58	-	-	-	-	-	-	-	1,028
Net periodic benefit cost	(3,779)	(91)	-	-	(856)	-	-	(193)	-	-	609	-	-	-	-	-	-	-	(4,310)
Other (expense) revenue, net	(6,815)	784	(13)	(17)	(177)	-	-	1	-	-	(2,802)	-	(123)	(339)	(83)	(233)	127	-	(9,690)
Total nonoperating gains (losses), net	4,547	1,407	1,323	1,313	(1,100)	-	647	(327)	2	-	(2,708)	1	401	481	67	(190)	(1,495)	-	4,369
Excess (deficiency) of revenues over expenses	\$ 43,167	3,603	12,966	9,717	(30,319)	(1,221)	376	(481)	(419)	(1,920)	(2,708)	(142)	401	481	67	(190)	(1,622)	-	31,756
Excess margin %	5.8%	3.3%	22.5%	19.7%	(63.2%)	(196.0%)	2.7%	(2.8%)	105.5%	(38.3%)	(3.3%)	(7.1%)	NA	NA	NA	NA	NA	NA	2.1%

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2019

(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP					SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	TOTAL	
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF			PAHF
Net assets without donor restrictions:																		
Excess (deficiency) of revenues over expenses	\$ 43,167	3,603	12,966	9,717	(30,319)	(1,221)	376	(481)	(419)	(1,920)	(2,708)	(142)	401	481	67	(190)	(1,622)	31,756
Pension and other postretirement liability adjustments	(16,546)	(554)	-	-	(932)	-	-	-	-	-	(3,533)	-	-	-	-	-	-	(21,565)
Amortization of ineffective portion of derivatives	55	-	-	-	-	-	-	-	-	-	9	-	-	-	-	-	-	64
Other	-	(22)	-	-	-	-	-	-	-	-	-	-	176	-	-	4	-	158
Transfers to related organizations	(42,850)	(1,004)	(2,766)	(351)	-	(186)	-	-	-	(193)	(38,928)	(1,328)	-	-	-	-	-	87,606
Transfers from related organizations	4,334	155	-	-	31,706	861	-	-	-	3,005	46,738	-	664	-	-	143	(87,606)	-
(Decrease) increase in net assets without donor restrictions	(11,840)	2,178	10,200	9,366	455	(546)	376	(481)	(419)	892	1,578	(1,470)	1,241	481	67	(43)	(1,622)	10,413
Net assets with donor restrictions:																		
Contributions	247	-	-	-	-	-	22	-	-	-	-	-	2,241	31	131	370	-	3,042
Net investment (loss) gain	-	(187)	-	-	-	-	-	-	-	-	-	-	422	-	1	1	-	237
Net assets released from restrictions	(943)	-	-	-	-	-	(20)	-	-	-	-	-	(1,109)	(93)	(75)	(187)	-	(2,427)
Change in fair value of split interest agreements	272	(15)	-	-	-	-	-	-	-	-	-	-	13	-	-	-	-	270
Change in interest in net assets of foundations	(742)	180	(62)	57	-	-	-	-	-	-	-	-	-	-	-	-	567	-
Other	-	(47)	-	-	-	-	-	-	-	-	-	-	(282)	-	-	(4)	-	(333)
(Decrease) increase in net assets with donor restrictions	(1,166)	(69)	(62)	57	-	-	2	-	-	-	-	-	1,285	(62)	57	180	567	789
(Decrease) increase in net assets	(13,006)	2,109	10,138	9,423	455	(546)	376	(479)	(419)	892	1,578	(1,470)	2,526	419	124	137	(1,055)	11,202
Net assets, beginning of period	575,236	133,640	124,152	61,374	1,706	591	17,432	13,303	9,959	1,919	118,624	3,240	32,116	27,387	5,268	4,855	(68,871)	1,061,931
Net assets, end of period	\$ 562,230	135,749	134,290	70,797	2,161	45	17,808	12,824	9,540	2,811	120,202	1,770	34,642	27,806	5,392	4,992	(69,926)	1,073,133

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED SEPTEMBER 30, 2019
(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP						SYSTEM RESOURCES GROUP	FOUNDATIONS				ELIMI-NATIONS	TOTAL	
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF			PAHF
Cash flows from operating activities:																		
Changes in net assets	\$ (13,006)	2,109	10,138	9,423	455	(546)	376	(479)	(419)	892	1,578	(1,470)	2,526	419	124	137	(1,055)	11,202
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:																		
Loss on extinguishment of debt	386	-	67	108	-	-	-	-	-	-	170	-	-	-	-	-	-	731
201	201	1,001	-	-	-	-	-	-	-	-	391	-	-	-	-	-	-	1,593
Interest and dividends	(4,603)	(664)	(1,183)	(1,010)	(510)	-	(163)	(97)	(2)	-	(470)	(1)	(540)	(329)	(60)	(72)	-	(9,704)
Realized (gain) loss on investments, net	(7,233)	(971)	(375)	(150)	-	-	(184)	(21)	-	-	(114)	-	(521)	(140)	(77)	(9)	-	(9,795)
Unrealized (gain) loss on investments, net	(1,766)	242	690	(211)	572	-	(300)	(13)	-	-	596	-	33	(351)	(14)	37	-	(485)
Restricted contributions and other	(247)	-	-	-	-	-	-	(22)	-	-	-	-	(2,241)	(31)	(131)	(370)	-	(3,042)
(Increase) decrease in beneficial interest in trusts	(272)	(52)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(324)
Depreciation (premiums) costs	33,892	4,324	4,048	3,871	612	45	414	827	-	-	17,376	1,421	-	-	-	-	-	66,830
Amortization of debt issuance (premiums) costs	(571)	7	-	(98)	-	-	-	-	-	-	(50)	61	-	-	-	-	-	(651)
(Gain) loss on disposal of assets	(294)	(16)	20	-	-	(39)	-	-	-	-	(1)	-	-	-	-	-	-	(330)
Deferred tax asset	(1,009)	(178)	(54)	-	-	-	-	-	-	-	(59)	-	-	-	-	-	-	(1,300)
Pension obligations	16,546	554	-	-	932	-	-	-	-	-	3,533	-	-	-	-	-	-	21,565
Changes in assets and liabilities:																		
(Increase) decrease in accounts receivable	(1,970)	(2,727)	(1,301)	(232)	595	396	562	(785)	-	-	-	-	-	-	-	-	-	(5,462)
(Increase) decrease in inventory and other assets	(559)	(844)	(310)	(44)	(944)	30	98	162	-	(2,696)	(3,227)	(100)	(54)	(263)	11	(20)	1,257	(7,503)
Increase (decrease) in estimated third-party payor settlements	1,262	735	1,341	1,961	-	-	-	-	-	-	-	-	-	-	-	-	-	5,299
Increase (decrease) in accounts payable and other current liabilities	10,461	528	(168)	138	1,728	56	22	434	(1)	1,190	2,110	-	273	(19)	-	2	(1,254)	15,500
Increase (decrease) in self-insurance and other long-term liabilities	2,930	(1,445)	(61)	122	(345)	(65)	(16)	(87)	-	-	(1,603)	-	(11)	-	-	-	-	(581)
Amount due (from) to affiliates	(745)	158	38	(51)	(20)	(64)	(14)	(25)	-	(53)	604	37	101	33	(2)	-	-	3
Change in interest in net assets of foundations	(375)	(137)	(419)	(124)	-	-	-	-	-	-	-	-	-	-	-	-	-	1,055
Transfers to (from) related organizations	38,516	849	2,766	351	(31,706)	(675)	-	-	-	(2,812)	(7,810)	1,328	(664)	-	-	(143)	-	-
Net cash provided by (used in) operating activities	71,544	3,473	15,237	14,054	(28,631)	(862)	795	(106)	(422)	(3,479)	13,024	1,276	(1,098)	(681)	(149)	(438)	6	83,543
Cash flows from investing activities:																		
Acquisition of property and equipment	(29,996)	(4,325)	(2,849)	(24,074)	(140)	-	(53)	(1,100)	-	-	(16,928)	-	-	(8)	-	-	-	(79,473)
Proceeds on sale of property	2,407	18	-	-	-	155	-	-	-	-	159	-	-	-	-	-	-	2,739
(Deposits) withdrawals in investments, net	(584)	1,000	36,606	5,000	(1,822)	-	-	(3,000)	-	-	11,600	-	(2,443)	501	-	76	-	46,934
Other investment activity, net	(5,198)	(331)	1,411	(42)	1,171	-	(360)	42	2	-	(298)	212	-	(48)	103	-	-	(3,336)
Change in investment in partnerships	-	-	-	-	-	-	10	-	935	-	17	-	-	-	-	-	-	962
Net change in other assets	-	-	-	-	-	-	-	-	-	-	139	-	608	-	-	-	(6)	741
Net cash (used in) provided by investing activities	(33,371)	(3,638)	35,168	(19,116)	(791)	155	(403)	(4,058)	937	-	(5,311)	212	(1,835)	445	103	76	(6)	(31,433)
Cash flows from financing activities:																		
Restricted contributions and other	247	-	-	-	-	-	-	22	-	-	-	-	2,241	31	131	370	-	3,042
Repayment of long-term debt	(106,175)	(1,308)	(41,530)	(17,797)	-	-	-	-	-	-	(24,009)	-	-	-	-	-	-	(190,819)
Issuance of long-term debt	101,119	-	-	16,008	-	-	-	-	-	-	12,878	-	-	-	-	-	-	130,005
Premiums received, net of debt issuance cost payments	12,970	-	-	2,003	-	-	-	-	-	-	1,609	-	-	-	-	-	-	16,582
Distributions from beneficial interest in trusts	750	298	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,048
Transfers (to) from related organizations	(38,516)	(849)	(2,766)	(351)	31,706	675	-	-	-	2,812	7,810	(1,328)	664	-	-	143	-	-
Net cash flows (used in) provided by financing activities	(29,605)	(1,859)	(44,296)	(137)	31,706	675	-	22	-	2,812	(1,712)	(1,328)	2,905	31	131	513	-	(40,142)
Net increase (decrease) in cash and cash equivalents	8,568	(2,024)	6,109	(5,199)	2,284	(32)	392	(4,142)	515	(667)	6,001	160	(28)	(205)	85	151	-	11,968
Cash and cash equivalents, beginning of period	18,588	4,958	15,064	12,197	4,064	98	1,260	9,389	677	767	9,138	451	1,467	441	49	789	-	79,397
Cash and cash equivalents, end of period	\$ 27,156	2,934	21,173	6,998	6,348	66	1,652	5,247	1,192	100	15,139	611	1,439	236	134	940	-	91,365

**MEMORIAL HEALTH SYSTEM
CONSOLIDATING BALANCE SHEET
SEPTEMBER 30, 2018**

(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP						SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	TOTAL
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF	PAHF		
Assets																		
Current assets:																		
Cash and cash equivalents	\$ 18,588	4,958	15,064	12,197	4,064	98	1,260	9,389	677	767	9,138	451	1,467	441	49	789	-	79,397
Short-term investments	46,339	3,726	23,971	38,609	-	-	1,511	-	-	-	-	-	1,528	204	176	-	-	116,064
Assets whose use is limited	2,600	-	-	-	-	-	113	116	-	-	-	204	-	-	-	-	-	3,033
Receivables:																		
Patient accounts receivable	114,194	20,972	9,638	6,427	7,643	727	1,430	3,396	-	-	-	-	-	-	-	-	-	164,427
Allowance for implicit price concessions	(13,068)	(2,544)	(2,489)	(1,516)	(1,441)	(230)	(286)	(159)	-	-	-	-	-	-	-	-	-	(21,733)
Net patient accounts receivable	101,126	18,428	7,149	4,911	6,202	497	1,144	3,237	-	-	-	-	-	-	-	-	-	142,694
Receivables from third-party payors	13,197	-	-	423	-	-	-	-	-	-	-	-	-	-	-	-	-	13,620
Due from affiliates	177	112	194	266	829	4	90	83	1	802	-	6	-	-	-	-	(2,564)	
Receivables held for sale	896	131	39	54	160	-	-	28	-	-	-	-	-	-	-	-	-	1,308
Other receivables	14,635	360	143	42	1,746	91	670	633	1	2,472	1,796	5	227	176	24	-	(470)	22,551
Inventories	10,415	1,715	603	449	947	-	-	429	-	-	-	-	-	-	-	-	-	14,558
Prepaid expenses	5,345	996	253	732	291	-	141	88	1	17	5,437	-	79	-	-	-	-	13,380
Total current assets	213,318	30,426	47,416	57,683	14,239	690	4,929	14,003	679	3,257	17,173	660	3,307	821	249	789	(3,034)	406,605
Long-term investments:																		
Unrestricted investments	355,547	78,907	66,498	1,186	-	-	10,209	201	-	-	15,350	-	17,724	25,885	4,744	3,652	-	579,903
Assets whose use is limited:																		
Self-insurance trusts	11,242	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	11,242
Donor-restricted assets and other	1,049	3,388	-	-	-	-	105	83	-	-	-	315	10,517	331	281	414	-	16,483
Deferred compensation assets	1,575	747	-	-	7,979	-	-	-	-	-	5,821	-	-	-	-	-	-	16,122
Total assets whose use is limited	13,866	4,135	-	-	7,979	-	105	83	-	-	5,821	315	10,517	331	281	414	-	43,847
Total long-term investments	369,413	83,042	66,498	1,186	7,979	-	10,314	284	-	-	21,171	315	28,241	26,216	5,025	4,066	-	623,750
Property, plant, and equipment, net	269,677	38,674	31,495	23,246	6,434	189	3,947	2,005	-	-	178,449	18,880	-	426	-	-	-	573,422
Other assets:																		
Investments in partnerships	-	-	-	-	-	-	31	-	9,281	-	796	-	-	-	-	-	(2,531)	7,577
Interest in net assets of foundation	28,904	4,781	27,387	5,268	-	-	-	-	-	-	-	-	-	-	-	-	(66,340)	-
Beneficial interest in trusts	28,297	17,814	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	46,111
Other	32,751	1,405	127	31	-	-	-	104	-	-	4,651	-	1,651	-	-	-	(6)	40,714
Total other assets	89,952	24,000	27,514	5,299	-	-	31	104	9,281	-	5,447	-	1,651	-	-	-	(68,877)	94,402
TOTAL ASSETS	\$ 942,360	176,142	172,923	87,414	28,652	879	19,221	16,396	9,960	3,257	222,240	19,855	33,199	27,463	5,274	4,855	(71,911)	1,698,179
Liabilities and net assets																		
Current liabilities:																		
Long-term debt	\$ 6,225	1,308	460	197	-	-	-	-	-	-	4,755	-	-	-	-	-	-	12,945
Accounts payable	38,823	3,145	853	3,695	4,190	41	67	1,535	1	1,031	5,220	16	33	-	-	-	-	58,650
Accrued payroll	24,033	5,331	2,322	2,875	2,546	71	947	907	-	32	5,040	-	-	-	-	-	-	44,104
Interest payable	3,011	43	1,120	480	-	-	-	-	-	-	439	-	-	-	-	-	-	5,093
Due to affiliates	1,243	83	4	-	794	-	336	174	-	-	32	105	-	43	1	-	(2,815)	-
Payables to third-party payors	35,434	5,364	2,406	612	-	-	-	-	-	-	-	-	-	-	-	-	-	43,816
Other	6,395	431	85	23	2,648	1	124	68	-	275	5,488	-	950	-	5	-	(225)	16,268
Total current liabilities	115,164	15,705	7,250	7,882	10,178	113	1,474	2,684	1	1,338	20,974	105	966	76	6	-	(3,040)	180,876
Noncurrent liabilities:																		
Long-term debt obligations, net	227,520	18,870	41,003	17,571	-	-	-	-	-	-	66,095	-	-	-	-	-	-	371,059
Deferred compensation and benefits	1,575	747	-	-	8,221	-	-	-	-	-	6,725	-	-	-	-	-	-	17,268
Self-insurance accrued expenses	13,051	3,411	518	141	505	175	-	196	-	-	246	-	-	-	-	-	-	18,243
Accrued employee benefits	5,591	2,133	-	-	5,844	-	119	213	-	-	3,872	-	-	-	-	-	-	17,772
Pension obligations	862	-	-	-	2,198	-	196	-	-	-	2,771	-	-	-	-	-	-	6,027
Other	3,361	1,636	-	446	-	-	-	-	-	-	2,933	16,510	117	-	-	-	-	25,003
Total noncurrent liabilities	251,960	26,797	41,521	18,158	16,768	175	315	409	-	-	82,642	16,510	117	-	-	-	-	455,372
Total liabilities	367,124	42,502	48,771	26,040	26,946	288	1,789	3,093	1	1,338	103,616	16,615	1,083	76	6	-	(3,040)	636,248
Net assets:																		
Without donor restrictions	535,111	111,793	123,821	61,093	1,706	591	16,477	13,104	9,959	1,919	118,624	3,240	20,139	27,056	4,987	3,988	(56,687)	996,921
With donor restrictions	40,125	21,847	331	281	-	-	955	199	-	-	-	-	11,977	331	281	867	(12,184)	65,010
Total net assets	575,236	133,640	124,152	61,374	1,706	591	17,432	13,303	9,959	1,919	118,624	3,240	32,116	27,387	5,268	4,855	(68,871)	1,061,931
TOTAL LIABILITIES AND NET ASSETS	\$ 942,360	176,142	172,923	87,414	28,652	879	19,221	16,396	9,960	3,257	222,240	19,855	33,199	27,463	5,274	4,855	(71,911)	1,698,179

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED SEPTEMBER 30, 2018

(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP						SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	TOTAL			
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF	PAHF					
Gross patient service charges:																					
Inpatient charges	\$ 1,188,294	124,281	19,445	17,707	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,349,727	
Outpatient charges	1,135,514	285,872	113,233	90,721	126,133	6,895	15,240	30,497	-	-	-	-	-	-	-	-	-	-	(352)	1,803,753	
Total gross patient service charges	2,323,808	410,153	132,678	108,428	126,133	6,895	15,240	30,497	-	-	-	-	-	-	-	-	-	-	(352)	3,153,480	
Deductions from charges:																					
Financial assistance (charity)	8,198	2,751	496	421	21	1	186	21	-	-	-	-	-	-	-	-	-	-	-	12,095	
Explicit price concessions (contractual allowances)	1,669,374	294,230	77,934	61,363	77,247	4,310	1,914	12,003	-	-	-	-	-	-	-	-	-	-	-	384	2,198,759
Implicit price concessions (provision for uncollectible accounts)	6,831	1,228	2,064	1,031	2,062	14	20	(661)	-	-	-	-	-	-	-	-	-	-	-	-	12,589
Total deductions from charges	1,684,403	298,209	80,494	62,815	79,330	4,325	2,120	11,363	-	-	-	-	-	-	-	-	-	-	-	384	2,223,443
Net patient service revenues	639,405	111,944	52,184	45,613	46,803	2,570	13,120	19,134	-	-	-	-	-	-	-	-	-	-	-	(736)	930,037
% of total gross patient service charges	27.5%	27.3%	39.3%	42.1%	37.1%	37.3%	86.1%	62.7%	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	29.5%
Capitation revenues	60,043	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	60,043
Other revenues:																					
Management fees	-	-	17	-	-	-	-	-	-	-	56,639	-	-	-	-	-	-	-	-	(56,656)	-
Other	11,869	1,619	266	153	1,213	50	634	241	(497)	3,373	21,011	1,885	-	-	-	-	-	-	-	(11,585)	30,232
Total other revenues	11,869	1,619	283	153	1,213	50	634	241	(497)	3,373	77,650	1,885	-	-	-	-	-	-	-	(68,241)	30,232
Total revenues	711,317	113,563	52,467	45,766	48,016	2,620	13,754	19,375	(497)	3,373	77,650	1,885	-	-	-	-	-	-	-	(68,977)	1,020,312
Expenses:																					
Salaries and wages	214,982	47,186	16,955	15,612	44,916	2,943	8,420	10,275	15	1,577	27,367	114	-	-	-	-	-	-	-	-	390,362
Employee benefits	59,707	16,202	5,081	5,206	12,488	537	2,643	3,309	6	413	6,997	32	-	-	-	-	-	-	-	(366)	112,255
Physician fees	52,021	8,236	4,174	3,010	-	10	14	69	-	359	-	-	-	-	-	-	-	-	-	-	67,893
Utilities	7,839	1,280	491	644	248	25	339	113	-	18	3,762	148	-	-	-	-	-	-	-	(1,465)	13,442
Pharmaceutical supplies	28,274	4,568	1,300	992	3,360	30	1	268	-	-	-	-	-	-	-	-	-	-	-	-	38,793
Patient service supplies	85,216	7,495	1,978	1,692	1,048	232	-	342	-	-	-	-	-	-	-	-	-	-	-	-	98,003
System management fee	45,476	2,013	1,283	1,202	3,313	84	669	827	39	269	-	-	-	-	-	-	-	-	-	(55,175)	-
Purchased services and other	70,847	12,909	5,135	5,225	10,173	1,130	1,081	2,870	1	1,413	19,547	61	-	-	-	-	-	-	-	(11,807)	118,585
Hospital provider assessment	19,809	2,747	1,143	941	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	24,640
Purchased medical services	36,375	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	36,375
Depreciation	36,323	4,373	4,367	3,450	634	60	417	956	-	-	16,376	1,425	-	-	-	-	-	-	-	-	68,381
Amortization of debt issuance expenses	297	7	134	58	-	-	-	-	-	-	57	62	-	-	-	-	-	-	-	-	615
Interest expense and other financing costs	9,109	470	2,248	954	-	-	-	-	-	-	3,544	209	-	-	-	-	-	-	-	-	16,534
Total expenses	666,275	107,486	44,289	38,986	76,180	5,051	13,584	19,029	61	4,049	77,650	2,051	-	-	-	-	-	-	-	(68,813)	985,878
Income (loss) from operations	45,042	6,077	8,178	6,780	(28,164)	(2,431)	170	346	(558)	(676)	-	(166)	-	-	-	-	-	-	-	(164)	34,434
% of total operating revenue	6.3%	5.4%	15.6%	14.8%	(58.7%)	(92.8%)	1.2%	1.8%	(112.3%)	(20.0%)	NA	(8.8%)	NA	NA	NA	NA	NA	NA	NA	(0.2%)	3.4%
Nonoperating gains (losses):																					
Interest and dividends	5,566	1,018	1,208	421	591	-	172	46	7	-	773	1	207	385	75	11	-	-	-	-	10,481
Realized gain on investments, net	35,260	9,676	4,967	1,200	-	-	1,168	26	-	-	5,179	-	875	1,595	229	26	-	-	-	-	60,201
Unrealized (loss) gain on investments, net	(17,362)	(6,819)	(1,317)	(894)	65	-	(1,018)	(10)	-	-	(2,741)	-	349	571	(6)	49	-	-	-	-	(29,133)
Gain on derivatives	183	303	-	-	-	-	-	-	-	-	310	-	-	-	-	-	-	-	-	-	796
Change in interest in net assets of foundation	1,859	74	2,326	4,987	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(9,246)	-
Provision for income taxes	-	-	-	-	-	-	-	(749)	-	-	-	-	-	-	-	-	-	-	-	-	(749)
Net periodic benefit cost	(2,306)	(347)	-	-	(627)	-	-	(120)	-	-	(4,547)	-	-	-	-	-	-	-	-	-	(7,947)
Other revenue (expense), net	152	(20)	(504)	66	(673)	-	-	8	-	-	(1,211)	-	506	(225)	(3)	(96)	-	-	-	164	(1,836)
Total nonoperating gains (losses), net	23,352	3,885	6,680	5,780	(644)	-	322	(799)	7	-	(2,237)	1	1,937	2,326	295	(10)	-	-	-	(9,082)	31,813
Excess (deficiency) of revenues over expenses	\$ 68,394	9,962	14,858	12,560	(28,808)	(2,431)	492	(453)	(551)	(676)	(2,237)	(165)	1,937	2,326	295	(10)	-	-	-	(9,246)	66,247
Excess margin %	9.3%	8.5%	25.1%	24.4%	(60.8%)	(92.8%)	3.5%	(2.4%)	112.4%	(20.0%)	(3.0%)	(8.7%)	NA	NA	NA	NA	NA	NA	NA	11.8%	6.3%

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2018
(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP						SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	Total
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF	PAHF		
Net assets without donor restrictions:																		
Excess (deficiency) of revenues over expenses	\$ 68,394	9,962	14,858	12,560	(28,808)	(2,431)	492	(453)	(551)	(676)	(2,237)	(165)	1,937	2,326	295	(10)	(9,246)	66,247
Pension and other postretirement liability adjustments	16,991	-	-	-	(386)	-	-	-	-	-	3,315	-	-	-	-	-	-	19,920
Amortization of ineffective portion of derivatives	55	-	-	-	-	-	-	-	-	-	8	-	-	-	-	-	-	63
Other	16,266	48	-	-	-	-	-	-	-	-	-	-	129	-	-	(68)	(16,266)	109
Transfers to related organizations	(24,545)	(2,659)	-	-	-	(81)	-	-	(2,718)	(763)	(21,885)	(1,101)	-	-	-	-	-	53,752
Transfers from related organizations	1,046	-	-	205	20,119	2,507	225	-	-	2,703	26,795	-	-	-	-	152	(53,752)	-
Increase (decrease) in net assets without donor restrictions	78,207	7,351	14,858	12,765	(9,075)	(5)	717	(453)	(3,269)	1,264	5,996	(1,266)	2,066	2,326	295	74	(25,512)	86,339
Net assets with donor restrictions:																		
Contributions	264	-	-	-	-	-	-	35	-	-	-	-	325	47	84	224	-	979
Net investment gain	-	136	-	-	-	-	-	-	-	-	-	-	973	-	1	-	-	1,110
Net assets released from restrictions	(3,153)	-	-	-	-	-	-	(30)	-	-	-	-	(1,238)	-	(122)	(229)	-	(4,772)
Change in fair value of split interest agreements	(134)	5	-	-	-	-	-	-	-	-	-	-	18	-	-	-	-	(111)
Change in interest in net assets of foundations	10,779	154	(38)	281	-	-	-	-	-	-	-	-	-	-	-	-	(11,176)	-
Other	-	(47)	-	-	-	-	-	-	-	-	-	-	(203)	(85)	-	68	-	(267)
Increase (decrease) in net assets with donor restrictions	7,756	165	(38)	281	-	-	-	5	-	-	-	-	(125)	(38)	(37)	146	(11,176)	(3,061)
Increase (decrease) in net assets	85,963	7,516	14,820	13,046	(9,075)	(5)	717	(448)	(3,269)	1,264	5,996	(1,266)	1,941	2,288	258	220	(36,688)	83,278
Net assets, beginning of period	489,273	126,124	109,332	48,328	10,781	596	16,715	13,751	13,228	655	112,628	4,506	30,175	25,099	5,010	4,635	(32,183)	978,653
Net assets, end of period	\$ 575,236	133,640	124,152	61,374	1,706	591	17,432	13,303	9,959	1,919	118,624	3,240	32,116	27,387	5,268	4,855	(68,871)	1,061,931

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED SEPTEMBER 30, 2018

(dollars in thousands)

	HOSPITAL GROUP				AMBULATORY GROUP						SYSTEM RESOURCES GROUP		FOUNDATIONS				ELIMI-NATIONS	TOTAL	
	MMC	PAH	ALMH	TMH	MPS	PPA	MBH	MHSvc	MHV	MHP	MHS	QALICB	MMCF	ALHF	TMHF	PAHF			
Cash flows from operating activities:																			
Changes in net assets	\$ 85,963	7,516	14,820	13,046	(9,075)	(5)	717	(448)	(3,269)	1,264	5,996	(1,266)	1,941	2,288	258	220	(36,688)	83,278	
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:																			
Non cash contributions	(2,211)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(2,211)
(Gain) loss on derivatives	(183)	(303)	-	-	-	-	-	-	-	-	(310)	-	-	-	-	-	-	-	(796)
Interest and dividends	(5,566)	(1,154)	(1,208)	(421)	(591)	-	(172)	(46)	(7)	-	(773)	(1)	(558)	(385)	(76)	(11)	-	(10,969)	
Realized (gain) loss on investments, net	(35,260)	(9,676)	(4,967)	(1,200)	-	-	(1,168)	(26)	-	-	(5,179)	-	(1,515)	(1,595)	(229)	(26)	-	(60,841)	
Unrealized (gain) loss on investments, net	17,362	6,819	1,317	894	(65)	-	1,018	10	-	-	2,741	-	(574)	(571)	6	(49)	-	28,908	
Restricted contributions and other	(264)	-	-	-	-	-	-	(35)	-	-	-	-	(325)	(47)	(84)	(224)	-	(979)	
(Increase) decrease in beneficial interest in trusts	2,345	(292)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2,053	
Depreciation and amortization	36,323	4,373	4,367	3,450	634	60	417	956	-	-	16,376	1,425	-	-	-	-	-	68,381	
Amortization of debt issuance costs (premiums)	297	7	134	58	-	-	-	-	-	-	57	62	-	-	-	-	-	615	
Loss (gain) on disposal of assets	323	6	-	-	6	(5)	(61)	(6)	-	-	602	-	-	-	-	-	-	865	
Deferred tax asset	(16,991)	-	-	-	386	-	-	-	-	-	(3,315)	-	-	-	-	-	-	(19,920)	
Pension obligations																			
Changes in assets and liabilities:																			
Decrease (increase) in accounts receivable	9,125	60	667	2,536	462	18	(53)	902	50	-	-	-	-	-	-	-	-	13,767	
Decrease (increase) in inventory and other assets	22,635	3,855	1,309	337	480	4	993	1,086	265	(1,795)	1,261	65	(8)	207	(17)	-	(36)	30,641	
Increase (decrease) in estimated third-party payor settlements	5,982	380	1,115	(2,029)	-	-	-	-	-	-	-	-	-	-	-	-	-	5,448	
Increase (decrease) in accounts payable and other current liabilities	4,092	(7)	349	2,967	2,308	(71)	(433)	(325)	(45)	1,299	1,605	(136)	(201)	-	(8)	(7)	(70)	11,317	
Increase (decrease) in self-insurance and other long-term liabilities	1,495	(882)	92	(3)	(2,164)	(13)	315	(68)	-	-	(5,864)	-	25	-	-	-	-	(7,067)	
Amount due to (from) affiliates	1,430	(125)	(326)	(291)	(235)	5	(145)	90	(431)	(1)	58	(195)	1	31	5	-	-	129	
Change in interest in net assets of foundations	(28,904)	(228)	(2,288)	(5,268)	-	-	-	-	-	-	-	-	-	-	-	-	-	36,688	
Transfers to (from) related organizations	23,499	2,659	-	(205)	(20,119)	(2,426)	(225)	-	2,718	(1,940)	(4,910)	1,101	-	-	-	(152)	-	-	
Net cash provided by (used in) operating activities	121,492	13,008	15,381	13,871	(27,973)	(2,433)	1,203	2,090	(719)	(1,173)	8,345	1,055	(1,214)	(72)	(145)	(249)	23	142,490	
Cash flows from investing activities:																			
Acquisition of property and equipment	(33,002)	(5,859)	(1,329)	(6,486)	(116)	-	(315)	(837)	-	-	(11,279)	(72)	-	(111)	-	-	-	(59,406)	
Proceeds on sale of property	60	3	-	-	2	33	126	7	-	-	1,110	-	-	-	-	-	-	1,341	
(Deposits) withdrawals in investments, net	(99,443)	(3,700)	(26,478)	(33,999)	-	-	(2,000)	-	-	-	24,825	-	(225)	-	75	-	-	(140,945)	
Other investment activity, net	10,296	529	464	634	3,325	-	(1,945)	288	114	-	3,868	306	-	271	18	100	-	18,268	
Change in investment in partnerships	-	-	-	-	-	-	(19)	-	1,703	-	14	-	-	-	-	-	-	1,698	
Net change in other assets	-	-	-	-	-	-	-	-	-	-	465	-	640	-	-	-	(23)	1,082	
Net cash (used in) provided by investing activities	(122,089)	(9,027)	(27,343)	(39,851)	3,211	33	(4,153)	(542)	1,817	-	19,003	234	415	160	93	100	(23)	(177,962)	
Cash flows from financing activities:																			
Restricted contributions and other	264	-	-	-	-	-	-	35	-	-	-	-	325	47	84	224	-	979	
Repayment of long-term debt	(19,852)	(2,697)	(360)	(155)	-	-	-	-	-	-	(30,745)	-	-	-	-	-	-	(53,809)	
Distributions from beneficial interest in trusts	700	148	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	848	
Transfers (to) from related organizations	(23,499)	(2,659)	-	-	19,579	2,426	225	-	(2,178)	1,940	5,115	(1,101)	-	-	-	152	-	-	
Net cash flows (used in) provided by financing activities	(42,387)	(5,208)	(360)	(155)	19,579	2,426	225	35	(2,178)	1,940	(25,630)	(1,101)	325	47	84	376	-	(51,982)	
Net (decrease) increase in cash and cash equivalents	(42,984)	(1,227)	(12,322)	(26,135)	(5,183)	26	(2,725)	1,583	(1,080)	767	1,718	188	(474)	135	32	227	-	(87,454)	
Cash and cash equivalents, beginning of period	61,572	6,185	27,386	38,332	9,247	72	3,985	7,806	1,757	-	7,420	263	1,941	306	17	562	-	166,851	
Cash and cash equivalents, end of period	\$ 18,588	4,958	15,064	12,197	4,064	98	1,260	9,389	677	767	9,138	451	1,467	441	49	789	-	79,397	

**MEMORIAL HEALTH SYSTEM
CONSOLIDATING BALANCE SHEET
SEPTEMBER 30, 2019**

(dollars in thousands)

Assets	MMC	MHS	Eliminations	OBLIGATED GROUP TOTAL	NON- OBLIGATED GROUP TOTAL	CONSOLIDATED TOTAL
Current assets:						
Cash and cash equivalents	\$ 27,156	15,139	-	42,295	49,070	91,365
Short-term investments	16,085	-	-	16,085	53,643	69,728
Assets whose use is limited	7,267	-	-	7,267	298	7,565
Receivables:						
Patient accounts receivable	118,840	-	-	118,840	53,792	172,632
Allowance for implicit price concessions	(15,744)	-	-	(15,744)	(8,732)	(24,476)
Net patient accounts receivable	103,096	-	-	103,096	45,060	148,156
Receivables from third-party payors	10,905	-	-	10,905	419	11,324
Due from affiliates	313	226	-	539	(539)	-
Receivables held for sale	1,666	-	-	1,666	431	2,097
Other receivables	14,144	2,022	-	16,166	9,508	25,674
Inventories	10,812	-	-	10,812	4,142	14,954
Prepaid expenses	4,837	8,250	-	13,087	2,409	15,496
Total current assets	196,281	25,637	-	221,918	164,441	386,359
Long-term investments:						
Unrestricted investments	399,739	3,645	-	403,384	190,972	594,356
Assets whose use is limited	14,771	5,932	-	20,703	26,486	47,189
Total long-term investments	414,510	9,577	-	424,087	217,458	641,545
Property, plant, and equipment, net	262,551	178,056	-	440,607	143,377	583,984
Other assets:						
Investments in partnerships	-	779	-	779	5,836	6,615
Interest in net assets of foundation	29,279	-	-	29,279	(29,279)	-
Beneficial interest in trusts	27,819	-	-	27,819	17,568	45,387
Other	15,181	4,359	-	19,540	4,270	23,810
Total other assets	72,279	5,138	-	77,417	(1,605)	75,812
TOTAL ASSETS	945,621	218,408	-	1,164,029	523,671	1,687,700
Liabilities and net assets						
Current liabilities:						
Long-term debt	\$ 6,463	2,872	-	9,335	1,782	11,117
Accounts payable	45,492	7,537	-	53,029	18,094	71,123
Accrued payroll	25,650	5,876	-	31,526	15,131	46,657
Interest payable	4,172	614	-	4,786	564	5,350
Due to affiliates	634	60	-	694	(694)	-
Payables to third-party payors	34,404	-	-	34,404	12,415	46,819
Other	6,292	4,083	-	10,375	7,142	17,517
Total current liabilities	123,107	21,042	-	144,149	54,434	198,583
Noncurrent liabilities:						
Long-term debt obligations, net	235,011	58,576	-	293,587	35,087	328,674
Deferred compensation and benefits	3,686	9,013	-	12,699	9,511	22,210
Self-insurance accrued expenses	12,737	249	-	12,986	5,052	18,038
Accrued employee benefits	5,002	4,395	-	9,397	8,657	18,054
Pension obligations	2,458	4,124	-	6,582	799	7,381
Other	1,390	807	-	2,197	19,430	21,627
Total noncurrent liabilities	260,284	77,164	-	337,448	78,536	415,984
Total liabilities	383,391	98,206	-	481,597	132,970	614,567
Net assets:						
Without donor restrictions	523,271	120,202	-	643,473	363,861	1,007,334
With donor restrictions	38,959	-	-	38,959	26,840	65,799
Total net assets	562,230	120,202	-	682,432	390,701	1,073,133
TOTAL LIABILITIES AND NET ASSETS	\$ 945,621	218,408	-	1,164,029	523,671	1,687,700

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSET
FOR THE YEAR ENDED SEPTEMBER 30, 2019

(dollars in thousands)

	MMC	MHS	Eliminations	OBLIGATED GROUP TOTAL	NON- OBLIGATED GROUP TOTAL	CONSOLIDATED TOTAL
Gross patient service charges:						
Inpatient charges	\$ 1,263,052	-	-	1,263,052	147,023	1,410,075
Outpatient charges	1,209,695	-	-	1,209,695	707,355	1,917,050
Total gross patient service charges	2,472,747	-	-	2,472,747	854,378	3,327,125
Deductions from charges:						
Financial assistance (charity)	9,455	-	-	9,455	3,958	13,413
Explicit price concessions (contractual allowances)	1,794,260	-	-	1,794,260	546,392	2,340,652
Implicit price concessions (provision for uncollectible accounts)	8,900	-	-	8,900	14,603	23,503
Total deductions from charges	1,812,615	-	-	1,812,615	564,953	2,377,568
Net patient service revenues	660,132	-	-	660,132	289,425	949,557
<i>% of total gross patient service charges</i>	26.7%	NA	NA	26.7%	33.9%	28.5%
Capitation revenues	63,682	-	-	63,682	-	63,682
Other revenues:						
Management fees	-	62,265	(51,529)	10,736	(10,736)	-
Other	10,955	23,021	(5,380)	28,596	1,704	30,300
Total other revenues	10,955	85,286	(56,909)	39,332	(9,032)	30,300
Total revenues	734,769	85,286	(56,909)	763,146	280,393	1,043,539
Expenses:						
Salaries and wages	227,217	29,630	-	256,847	147,805	404,652
Employee benefits	53,047	7,277	-	60,324	45,646	105,970
Physician fees	66,840	-	-	66,840	16,181	83,021
Pharmaceutical supplies	28,392	-	-	28,392	10,489	38,881
Patient service supplies	89,241	-	-	89,241	13,055	102,296
System management fee	50,414	-	(50,414)	-	-	-
Purchased services and other	82,607	28,210	(6,495)	104,322	34,652	138,974
Hospital provider assessment	22,292	-	-	22,292	6,227	28,519
Purchased medical services	33,098	-	-	33,098	(500)	32,598
Depreciation	33,892	17,376	-	51,268	15,562	66,830
Interest expense and other financing costs	9,109	2,793	-	11,902	2,509	14,411
Total expenses	696,149	85,286	(56,909)	724,526	291,626	1,016,152
Income (loss) from operations	38,620	-	-	38,620	(11,233)	27,387
<i>% of total operating revenue</i>	5.3%	0.0%	-	5.1%	(4.0%)	2.6%
Nonoperating gains (losses):						
Interest and dividends	4,603	470	-	5,073	4,632	9,705
Realized gain (loss) on investments, net	7,233	114	-	7,347	2,250	9,597
Unrealized gain (loss) on investments, net	1,766	(596)	-	1,170	(807)	363
Gain (loss) on derivatives	(201)	(391)	-	(592)	(1,001)	(1,593)
Gain (loss) on extinguishment of debt	(386)	(170)	-	(556)	(175)	(731)
Change in interest in net assets of foundation	1,117	-	-	1,117	(1,117)	-
Provision for income taxes	1,009	58	-	1,067	(39)	1,028
Net periodic benefit cost	(3,779)	609	-	(3,170)	(1,140)	(4,310)
Other revenue (expense), net	(6,815)	(2,802)	-	(9,617)	(73)	(9,690)
Total nonoperating gains (losses), net	4,547	(2,708)	-	1,839	2,530	4,369
Excess (deficiency) of revenues over expenses	43,167	(2,708)	-	40,459	(8,703)	31,756
<i>Excess margin %</i>	5.8%	(3.3%)	-	5.3%	(3.1%)	3.0%

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2019
(dollars in thousands)

	<u>MMC</u>	<u>MHS</u>	<u>Eliminations</u>	<u>OBLIGATED GROUP TOTAL</u>	<u>NON- OBLIGATED GROUP TOTAL</u>	<u>CONSOLIDATED TOTAL</u>
Net assets without donor restrictions:						
Excess of revenues over expenses	\$ 43,167	(2,708)	-	40,459	(8,703)	31,756
Pension and other postretirement liability adjustments	(16,546)	(3,533)	-	(20,079)	(1,486)	(21,565)
Amortization of ineffective portion of swaps	55	9	-	64	-	64
Other	-	-	-	-	158	158
Transfers to related organizations	(42,850)	(38,928)	42,100	(39,678)	39,678	-
Transfers from related organizations	4,334	46,738	(42,100)	8,972	(8,972)	-
(Decrease) increase in net assets without donor restrictions	<u>(11,840)</u>	<u>1,578</u>	<u>-</u>	<u>(10,262)</u>	<u>20,675</u>	<u>10,413</u>
Net assets with donor restrictions:						
Contributions	247	-	-	247	2,795	3,042
Net investment gain (loss)	-	-	-	-	237	237
Net assets released from restrictions	(943)	-	-	(943)	(1,484)	(2,427)
Change in fair value of split interest agreements	272	-	-	272	(2)	270
Change in interest in net assets of foundation	(742)	-	-	(742)	742	-
Other	-	-	-	-	(333)	(333)
(Decrease) increase in net assets with donor restrictions	<u>(1,166)</u>	<u>-</u>	<u>-</u>	<u>(1,166)</u>	<u>1,955</u>	<u>789</u>
(Decrease) increase in net asset	(13,006)	1,578	-	(11,428)	22,630	11,202
Net assets, beginning of period	575,236	118,624	-	693,860	368,071	1,061,931
Net assets, end of period	<u>\$ 562,230</u>	<u>120,202</u>	<u>-</u>	<u>682,432</u>	<u>390,701</u>	<u>1,073,133</u>

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED SEPTEMBER 30, 2019

(dollars in thousands)

	MMC	MHS	Eliminations	OBLIGATED GROUP TOTAL	NON- OBLIGATED GROUP TOTAL	CONSOLIDATED TOTAL
Cash flows from operating activities:						
Changes in net assets	\$ (13,006)	1,578	-	(11,428)	22,630	11,202
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:						
Loss on extinguishment of debt	386	170	-	556	175	731
Loss on derivatives	201	391	-	592	1,001	1,593
Interest and dividends	(4,603)	(470)	-	(5,073)	(4,631)	(9,704)
Realized (gain) loss on investments, net	(7,233)	(114)	-	(7,347)	(2,448)	(9,795)
Unrealized (gain) loss on investments, net	(1,766)	596	-	(1,170)	685	(485)
Restricted contributions and other	(247)	-	-	(247)	(2,795)	(3,042)
Increase in beneficial interest in trusts	(272)	-	-	(272)	(52)	(324)
Depreciation and amortization	33,892	17,376	-	51,268	15,562	66,830
Amortization of debt issuance (premiums) costs	(571)	(50)	-	(621)	(30)	(651)
(Gain) loss on disposal of assets	(294)	(1)	-	(295)	(35)	(330)
Deferred tax asset	(1,009)	(59)	-	(1,068)	(232)	(1,300)
Pension obligations	16,546	3,533	-	20,079	1,486	21,565
Changes in assets and liabilities:						
(Increase) decrease in accounts receivable	(1,970)	-	-	(1,970)	(3,492)	(5,462)
(Increase) decrease in inventory and other assets	(559)	(3,227)	-	(3,786)	(3,717)	(7,503)
Increase (decrease) in estimated third-party payor settlements	1,262	-	-	1,262	4,037	5,299
Increase (decrease) in accounts payable and other current liabilities	10,461	2,110	-	12,571	2,929	15,500
Increase (decrease) in self-insurance and other long-term liabilities	2,930	(1,603)	-	1,327	(1,908)	(581)
Amount due to (from) affiliates	(745)	604	-	(141)	141	-
Change in interest in net assets of foundation	(375)	-	-	(375)	375	-
Transfers to (from) related organizations	38,516	(7,810)	-	30,706	(30,706)	-
Net cash provided by (used in) operating activities	71,544	13,024	-	84,568	(1,025)	83,543
Cash flows from investing activities:						
Acquisition of property and equipment	(29,996)	(16,928)	-	(46,924)	(32,549)	(79,473)
Proceeds on sale of property	2,407	159	-	2,566	173	2,739
(Deposits) withdrawals in investments, net	(584)	11,600	-	11,016	35,918	46,934
Other investment activity, net	(5,198)	(298)	-	(5,496)	2,160	(3,336)
Change in investment in partnerships	-	17	-	17	945	962
Net change in other assets	-	139	-	139	602	741
Net cash (used in) provided by investing activities	(33,371)	(5,311)	-	(38,682)	7,249	(31,433)
Cash flows from financing activities:						
Restricted contributions and other	247	-	-	247	2,795	3,042
Repayment of long-term debt	(106,175)	(24,009)	-	(130,184)	(60,635)	(190,819)
Issuance of long-term debt	101,119	12,878	-	113,997	16,008	130,005
Premium received, net of debt issuance	12,970	1,609	-	14,579	2,003	16,582
Distributions from beneficial interest in trusts	750	-	-	750	298	1,048
Transfers (to) from related organizations	(38,516)	7,810	-	(30,706)	30,706	-
Net cash flows (used in) provided by financing activities	(29,605)	(1,712)	-	(31,317)	(8,825)	(40,142)
Net increase (decrease) in cash and cash equivalents	8,568	6,001	-	14,569	(2,601)	11,968
Cash and cash equivalents, beginning of period	18,588	9,138	-	27,726	51,671	79,397
Cash and cash equivalents, end of period	\$ 27,156	15,139	-	42,295	49,070	91,365

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