



Consolidated Financial Statements as of and
for the Years Ended June 30, 2019 and 2018,
Consolidating Schedules as of and
for the Year Ended June 30, 2019, and
Independent Auditors' Report

MIDMICHIGAN HEALTH

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITORS' REPORT	1-2
CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED JUNE 30, 2019 AND 2018:	
Balance Sheets	3
Statements of Operations and Changes in Net Assets	4-5
Statements of Cash Flows	6
Notes to Consolidated Financial Statements	7-44
MIDMICHIGAN HEALTH SUPPLEMENTARY CONSOLIDATING INFORMATION AS OF AND FOR THE YEAR ENDED JUNE 30, 2019:	45
Consolidating Schedule – Balance Sheet Information	46
Consolidating Schedule – Statement of Operations and Changes in Net Assets Information	47-48



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INDEPENDENT AUDITORS' REPORT

To the Audit Committee and the Board of Directors of
MidMichigan Health
Midland, Michigan

We have audited the accompanying consolidated financial statements of MidMichigan Health and its subsidiaries, which comprise the consolidated balance sheets as of June 30, 2019 and 2018, and the related consolidated statements of operations and changes in net assets and of cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

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

Report on Supplementary Consolidating Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary consolidating information listed in the table of contents on pages 46-48 is presented for the purpose of additional analysis of the consolidated financial statements rather than to present the financial position and results of operations of the individual subsidiaries and is not a required part of the consolidated financial statements. This supplementary consolidating information is the responsibility of MidMichigan Health's management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Deloitte + Touche LLP

October 14, 2019

MIDMICHIGAN HEALTH
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

	As of June 30,	
	2019	2018
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 15,581	\$ 20,782
Accounts receivable for patient services — net of allowance for doubtful accounts of \$39,585 as of 2018	86,094	89,585
Estimated receivables from third-party payors	10,060	14,857
Inventories	11,788	12,124
Prepaid expenses and other current assets	7,914	10,837
Assets limited or restricted as to use — current portion	19,270	17,447
Total current assets	<u>150,707</u>	<u>165,632</u>
ASSETS LIMITED AS TO USE AND INVESTMENTS:		
Investments — less current portion	139,434	132,180
Limited as to use by Board for capital acquisitions	538,253	488,536
Self-insurance, deferred compensation, and other	47,055	47,398
Limited as to use by donor or time restriction	50,156	47,640
Total assets limited as to use and investments	<u>774,898</u>	<u>715,754</u>
PROPERTY AND EQUIPMENT — Net	<u>442,467</u>	<u>430,209</u>
INVESTMENTS IN JOINT VENTURES	<u>7,388</u>	<u>7,945</u>
OTHER ASSETS	<u>22,078</u>	<u>21,225</u>
TOTAL ASSETS	<u>\$ 1,397,538</u>	<u>\$ 1,340,765</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	\$ 42,230	\$ 40,345
Salaries, wages, and payroll-related liabilities	58,381	46,388
Estimated third-party settlements payable	17,216	17,513
Current portion of long-term debt and capital lease obligations	7,779	6,496
Current portion of self-insurance, deferred compensation, and other liabilities	3,984	3,154
Total current liabilities	<u>129,590</u>	<u>113,896</u>
LONG-TERM LIABILITIES:		
Self-insurance, deferred compensation, and other liabilities — less current portion	94,504	83,022
Accrued pension and postretirement benefits	122,857	129,314
Long-term debt and capital lease obligations — less current portion	209,056	217,738
Total long-term liabilities	<u>426,417</u>	<u>430,074</u>
Total liabilities	<u>556,007</u>	<u>543,970</u>
NET ASSETS:		
Without donor restrictions:		
MidMichigan Health	791,352	749,155
Noncontrolling interests	23	-
Total net assets without donor restrictions	<u>791,375</u>	<u>749,155</u>
With donor restrictions	<u>50,156</u>	<u>47,640</u>
Total net assets	<u>841,531</u>	<u>796,795</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 1,397,538</u>	<u>\$ 1,340,765</u>

MIDMICHIGAN HEALTH

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS

(Dollars in thousands)

	For the Years Ended June 30,	
	2019	2018
REVENUE:		
Net patient service revenue before provision for uncollectible accounts	\$	848,502
Less provision for uncollectible accounts		<u>(41,922)</u>
Net patient service revenue	\$	806,580
Other revenue		<u>24,787</u>
Total revenue		<u>831,367</u>
EXPENSES:		
Salaries and wages	402,028	365,831
Employee benefits	92,959	82,231
Supplies	180,089	155,131
Professional fees and other	91,770	71,348
Purchased services and other	86,029	78,821
Depreciation and amortization	50,622	49,367
Utilities	11,800	10,707
Insurance	9,270	9,214
Interest	<u>8,178</u>	<u>7,871</u>
Total expenses		<u>830,521</u>
OPERATING INCOME BEFORE OTHER ITEMS	<u>26,374</u>	<u>846</u>
OTHER ITEMS:		
Postretirement settlement	1,325	-
Asset impairment charges for receivables	<u>-</u>	<u>(10,735)</u>
Total other items		<u>(10,735)</u>
OPERATING INCOME (LOSS) AFTER OTHER ITEMS	<u>27,699</u>	<u>(9,889)</u>
NONOPERATING INCOME:		
Investment income	37,763	60,058
Inherent contribution from acquisition (purchase accounting adjustment)	<u>(1,236)</u>	<u>14,737</u>
Total nonoperating income		<u>74,795</u>
EXCESS OF REVENUE OVER EXPENSES	64,226	64,906
DEFICIT OF REVENUE OVER EXPENSES ATTRIBUTABLE TO NONCONTROLLING INTERESTS	<u>(26)</u>	<u>-</u>
EXCESS OF REVENUE OVER EXPENSES — NET OF NONCONTROLLING INTERESTS	<u>\$ 64,252</u>	<u>\$ 64,906</u>

(Continued)

MIDMICHIGAN HEALTH**CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS***(Dollars in thousands)*

	For the Years Ended June 30,	
	2019	2018
NET ASSETS WITHOUT DONOR RESTRICTIONS:		
Excess of revenue over expenses	\$ 64,226	\$ 64,906
Net assets released from restrictions — capital acquisitions	352	1,850
Net cumulative unrealized gains on equity investments due to adoption of ASU No. 2016-01	145,748	-
Change in unrealized investment return	(145,748)	(20,429)
Contribution from noncontrolling interests	49	-
Postretirement-related liability adjustments	(22,407)	19,260
	<u>42,220</u>	<u>65,587</u>
Increase in net assets without donor restrictions		
NET ASSETS WITH DONOR RESTRICTIONS:		
Pledges, contributions, grants, and interest income	4,597	10,655
Acquisition of West Branch	-	1,262
Net assets released from restrictions	(1,950)	(4,565)
Investment (losses) gains	(131)	26
	<u>2,516</u>	<u>7,378</u>
Increase in net assets with donor restrictions		
INCREASE IN NET ASSETS	44,736	72,965
NET ASSETS — Beginning of year	796,795	723,830
NET ASSETS — End of year	\$ <u>841,531</u>	\$ <u>796,795</u>

See notes to consolidated financial statements.

(Concluded)

MIDMICHIGAN HEALTH
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

	For the Years Ended June 30,	
	2019	2018
OPERATING ACTIVITIES:		
Increase in net assets	\$ 44,736	\$ 72,965
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	50,622	49,367
Postretirement-related liability adjustments	22,407	(19,260)
Provision for uncollectible accounts	-	41,922
Gain on sale of joint venture	-	(770)
Gains and losses on investments-net	(28,413)	(33,191)
Restricted contributions and restricted investment income received	(4,597)	(11,917)
Loss on disposal of property, plant, and equipment	809	2,522
Inherent contribution from acquisition (purchase accounting adjustment)	1,236	(14,737)
Contributions from noncontrolling interests	(49)	-
Equity earnings in joint ventures	(441)	(167)
Distributions received from investments in joint ventures	1,693	1,895
Changes in operating assets and liabilities:		
Accounts receivable for patient services	3,491	(39,172)
Accounts payable and accrued expenses	15,022	4,724
Estimated third-party settlements payable	4,500	(10,378)
Prepaid expenses, other current assets, and inventories	3,259	(3,196)
Self-insurance, deferred compensation, and other liabilities	(17,941)	(20,680)
Other changes in operating assets and liabilities	(973)	(184)
Net cash provided by operating activities	<u>95,361</u>	<u>19,743</u>
INVESTING ACTIVITIES:		
Additions to property and equipment	(64,561)	(55,953)
Net cash acquired from acquisition	-	425
Purchase of investments	(47,655)	(107,167)
Sale of investments	15,101	132,117
Proceeds from sale of joint venture	-	1,766
Contributions to joint ventures	(695)	(2,168)
Net cash used in investing activities	<u>(97,810)</u>	<u>(30,980)</u>
FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	-	6,291
Contributions from noncontrolling interests	49	-
Restricted contributions and restricted investment income received	4,597	11,917
Payment of long-term debt	(7,398)	(6,677)
Net cash (used in) provided by financing activities	<u>(2,752)</u>	<u>11,531</u>
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(5,201)	294
CASH AND CASH EQUIVALENTS — Beginning of year	<u>20,782</u>	<u>20,488</u>
CASH AND CASH EQUIVALENTS — End of year	<u>\$ 15,581</u>	<u>\$ 20,782</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest	\$ 9,105	\$ 8,547
Noncash additions to property and equipment	\$ 3,893	\$ 5,037
New capital lease obligation for equipment	\$ -	\$ 1,816

See notes to consolidated financial statements.

MIDMICHIGAN HEALTH
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED JUNE 30, 2019 AND 2018
(Dollars in thousands)

1. ORGANIZATION AND MISSION

Organization

MidMichigan Health, a Michigan not-for-profit corporation, and its subsidiaries are collectively referred to as “MidMichigan Health.” MidMichigan Health operates a network of health services, including inpatient and outpatient services, physician services, home health care, and rehabilitation services primarily in Midland, Alpena, Clare, Gladwin, Gratiot, Isabella, and Ogemaw counties.

The following entities are collectively referred to as “Subsidiaries”:

Sole corporate member organizations:

- MidMichigan Medical Center — Midland (Midland)
- MidMichigan Medical Center — Alpena (Alpena)
- MidMichigan Medical Center — Clare (Clare)
- MidMichigan Medical Center — Gladwin (Gladwin)
- MidMichigan Medical Center — Gratiot (Gratiot)
- MidMichigan Medical Center – West Branch (West Branch)
- MidMichigan Physicians Group (MPG)
- MidMichigan Visiting Nurse Association dba MidMichigan Home Care (MHC)
- MidMichigan Collaborative Care Organization (MCCO)
- MidMichigan Health Foundation (Foundation)
- Tolfree Foundation
- Hospice of Helping Hands, Inc.

100% of capital stock owned:

- MidMichigan Health Development Associates (MHDA)

Majority interest – MidMichigan Health Pain Management

In February 2019, West Branch and West Branch PMG, LLC entered in an agreement to form MidMichigan Health Pain Management whereby West Branch holds a majority controlling interest.

Effective April 1, 2018, MidMichigan Health and John Tolfree Hospital (dba West Branch Regional Medical Center) and its subsidiaries (collectively, WBRMC) entered into an agreement whereby MidMichigan Health became the sole corporate member of WBRMC and the hospital changed its name to MidMichigan Medical Center – West Branch (see Note 3).

Mission

MidMichigan Health’s vision, “We celebrate the power of health throughout life – with you,” promotes health throughout each person’s lifetime by providing seamless care, including inpatient, outpatient, physician, home health care, psychiatric, and rehabilitation services. The mission statement for MidMichigan Health provides the purpose for its existence. The mission statement is as follows:

“Our mission is to provide excellent health services to improve the quality of life for people in our communities. Our patients remain the focus of everything we do.”

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements have been presented in conformity with accounting principles generally accepted in the United States of America (GAAP). Included in MidMichigan Health's consolidated financial statements are all of its wholly owned or controlled subsidiaries. All intercompany transactions have been eliminated in consolidation. The preparation of consolidated financial statements in conformity with GAAP requires management to make assumptions and estimates that affect the reported amounts. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents having an original maturity of 90 days or less when purchased are considered to be cash and cash equivalents. Cash equivalents are stated at fair value, which approximates cost.

Revenue Recognition

On July 1, 2018, MidMichigan Health adopted the Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, (ASU 2014-09) using the modified retrospective method of application to all contracts. This ASU outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance, and requires significantly expanded disclosures about revenue recognition. The core principal of the revenue guidance is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The primary change was in the presentation of the provision for uncollectible accounts, which relates to self-pay patients and amounts due from patients with insurance for co-pays and deductibles. Under the ASU, the majority of what was previously classified as provision for uncollectible accounts is now reflected as implicit price concessions and, therefore, a direct deduction to patient service revenue. For the year ended June 30, 2019, MidMichigan Health recorded \$45,018 of implicit price concessions as a direct reduction of patient service revenue that would have been recorded as a provision for uncollectible accounts prior to the adoption of the ASU 2014-09. Other than this change in presentation and disclosure, the adoption of this ASU did not have a significant impact to revenue recognized for the year ended June 30, 2019.

MidMichigan Health elected the practical expedient allowed under Accounting Standards Codification (ASC) 606-10-32-18 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the expectation that the period between the time of the service and the time the service is paid will be one year or less. The impact of any extended payment agreements with patients is not deemed material.

Net Patient Service Revenue and Patient Accounts Receivable

Net patient service revenue is reported at the amount that reflects the consideration to which MidMichigan Health expects to be entitled in exchange for providing patient care. These amounts are primarily due from patients and third-party payors and include variable consideration for retroactive revenue adjustments due to a subsequent audit or review process. Revenue is recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services provided by MidMichigan Health. Generally, performance obligations satisfied over time relate to patients receiving inpatient services. MidMichigan Health measures the performance obligation from the point of hospital admission through discharge. Revenue for performance obligations satisfied at a point in time is recognized when goods or services

are provided, and MidMichigan Health does not believe it is required to provide additional goods or services to the patient. Generally, performance obligations satisfied at a point in time relate to outpatient services.

Because MidMichigan Health's performance obligations relate to contracts with a duration of less than one year, it has elected to apply the optional exemption provided in FASB ASC 606-10-50-14(a) and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. These unsatisfied or partially unsatisfied performance obligations are primarily related to inpatient services and the related contracts are generally completed upon discharge, which generally occurs shortly after the end of the reporting period.

MidMichigan Health determines the transaction price based on contractual terms for all services covered by insurance or in accordance with MidMichigan Health's policies with regards to uninsured patients. MidMichigan Health determines its estimate of implicit price concessions based on its historical collection experience with each class of patients using a portfolio approach as a practical expedient to account for patient contracts as a collective group rather than individually. The consolidated financial statement effects of using this practical expedient are not materially different from an individual contract approach.

Patient Accounts Receivable

Patient accounts receivable are stated at estimated net realizable amounts from patients, third-party payors, and other insurers to which MidMichigan Health expects to be entitled in exchange for providing patient care. Management periodically reviews the adequacy of the implicit price concessions (during 2019) or the allowance for doubtful accounts (during 2018) based on historical experience, trends in health care coverage, and other collection indicators.

For receivables associated with services provided to patients who have third-party coverage, MidMichigan Health analyzes contractually due amounts and implicit price concessions (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely) to record receivables at their estimated net realizable value. For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), MidMichigan Health records significant price concessions in the period of service on the basis of its historical experience.

Patient Financial Assistance

MidMichigan Health administers a patient financial assistance policy designed to provide financial assistance for uninsured patients, as well as for insured patients with limited resources. For uninsured patients who meet the qualifications stipulated in MidMichigan Health's patient financial assistance policy, emergency, and other medically necessary inpatient and outpatient services are provided at no cost. For uninsured patients that do not qualify for full financial assistance, MidMichigan Health offers an explicit price concession off standard rates for services provided that result in net charges that do not exceed traditional Medicare payment rates. MidMichigan Health offers a 40% discount for all uninsured patients that do not qualify for financial assistance. The discount is offered regardless of the patient's ability to pay. Insured patients with limited financial resources may qualify for financial assistance with deductibles, coinsurances, and co-pays. The accounts receivable from patient balances represented 46.5% and 46.7% of total accounts receivable at June 30, 2019 and 2018, respectively.

Reimbursement from Third-Party Payors

Reimbursement from most payors for inpatient and outpatient services varies according to a patient classification system that is based on clinical, diagnostic, and other factors. Revenues under traditional Medicare and Medicaid programs, as well as Blue Cross, are based primarily on prospective payment systems. For Medicare, retrospectively determined non-claims-based revenues, such as indirect medical education, direct graduate

medical education, disproportionate share hospital payments, and bad debt expense reimbursement, are estimated using historical trends and current factors. These revenues are reported on Medicare cost reports, which are subject to audit by Medicare auditors and administrative and judicial review, prior to final settlement. These settlements can take several years to resolve. Because the laws, regulations, instructions, and rule interpretations governing Medicare reimbursement are complex and change frequently, the estimates recorded could change in subsequent periods. Medicaid revenues have the potential to be reduced based on an upper payment limit calculated through the Medicaid cost report, which is subject to review and adjustment by Medicaid auditors. Blue Cross revenues are also subject to a final settlement, where auditors reprice claims based on settlement rates. These represent the major payors included in accounts receivable for patient services at June 30, 2019 and 2018.

Settlements with third-party payors for retroactive adjustments are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor, and MidMichigan Health's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as new information becomes available or as years are final settled.

Generally, patients covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. MidMichigan Health estimates the transaction price for these patients and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense. Bad debt expense for the year ended June 30, 2019, was not material to the consolidated financial statements.

Charity Care

It is an inherent part of MidMichigan Health's mission to provide necessary medical care free of charge, or at a discount, to individuals without insurance or other means of paying for such care. As the amounts determined to qualify for charity care are not pursued for collection, they are not reported as net patient service revenue.

Inventories

Inventories consist primarily of medical supplies and pharmaceuticals and are stated at the lower of cost or net realizable value. The cost of inventories is determined principally by the weighted-average cost method.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, investments, accounts receivable, accounts payable, accrued expenses, estimated third-party settlements, and debt. The fair value of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses, and estimated third-party settlements approximated their financial statement carrying amount as of June 30, 2019 and 2018, because of their short-term maturity. The fair value of the other instruments is disclosed in Notes 7, 10, and 12.

Assets Limited as to Use, Investments, and Investment Income

Assets limited as to use consist primarily of investments limited as to use by donors, unconditional promises to contribute, assets held by trustees under debt or other agreements (including deferred compensation arrangements) and for self-insurance, and board-designated assets set aside for a specified future use. The

current portion of cash and investments limited as to use primarily represents the assets that are required for current liabilities, debt service, and professional liability as of June 30, 2019 and 2018.

Investments, inclusive of assets limited as to use, include marketable debt and equity securities. Investments in debt and equity securities with readily determinable fair values are measured at fair value using quoted market prices or model-driven valuations. Investments also include investments in commingled funds structured as limited liability corporations or partnerships. These investments are measured at net asset value (NAV) (see Note 7).

Investments also include alternatives. Alternative investments consist of limited partnerships that invest primarily in real estate and hedge funds. These investments are generally not marketable and may be divested only at specified times. Investments in real estate funds and hedge funds are measured at fair value based on MidMichigan Health's interest in the NAV of the respective fund. The estimated valuations of hedge fund and real estate investments are subject to uncertainty and could differ had a ready market existed for these investments. Such differences could be material.

Investment income includes interest, dividends, realized gains and losses, and unrealized gains and losses, and is a part of nonoperating income, in calculating excess of revenue over expenses. Investment income from unrestricted investments and board-designated funds are included in nonoperating income. Nonoperating income consists principally of investment income.

Investment Risks

Investment securities are subject to various risks, such as interest rate risk, market risk, and credit risk. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in values in the near term could materially affect the amounts reported in the accompanying consolidated financial statements (see Note 7).

Unconditional Promises to Contribute

Unconditional promises to contribute (pledges receivable) are recorded at the net present value of their estimated future cash flows. Estimated future cash flows due after one year are discounted using interest rates commensurate with the time value of money concept. The discount rate utilized approximates the risk-free investment rate of MidMichigan Health. MidMichigan Health maintains an estimated allowance for uncollectible pledges based upon management's assessment of historical and expected net collections considering business and economic conditions and other collection indicators. Net unconditional promises to contribute are reported in assets limited as to use by donor or time restriction in the accompanying consolidated balance sheets and amounted to \$4,676 and \$9,121 as of June 30, 2019 and 2018, respectively.

Property and Equipment

Property and equipment, including capitalized internal-use software, are recorded at cost or at fair value at the date of acquisition or receipt, if donated. Expenditures that substantially increase the useful life of existing property and equipment are capitalized. Routine maintenance and repairs are expensed as incurred. Depreciation expense is recognized over the estimated useful lives of the assets using either the straight-line or accelerated method and includes capital lease and internal-use software amortization. The useful lives of these assets range from 3 to 40 years.

Costs of computer software developed or obtained for internal use, including external direct costs of materials and services, payroll, and payroll-related costs of employees directly associated with internal-use software development projects, and interest costs incurred during the development period are expensed or capitalized depending on whether the costs are incurred in the preliminary project stage, development stage, or operational stage. Capitalized internal-use software is included in equipment with useful lives ranging from 3 to 12 years.

Capitalized Interest

Interest expense from bond proceeds, net of interest income, incurred during the construction of major projects is capitalized during the construction period. Such capitalized interest is amortized over the depreciable life of the related assets on a straight-line basis. Interest costs are not capitalized on assets established with donor-restricted assets. There was no interest expense capitalized during the years ended June 30, 2019 and 2018.

Impairment

MidMichigan Health periodically, or when a triggering event occurs, evaluates the carrying value of its long-lived assets for impairment. This evaluation is based principally on the projected, undiscounted cash flows generated by the related assets. During the years ended June 30, 2019 and 2018, no such impairment was considered necessary.

Ownership Interests in Other Health-Related Entities

MidMichigan Health has affiliations with and interests in other organizations that are not consolidated. These organizations primarily provide outpatient health care and managed care contracting services. An ownership interest in another health-related entity in which MidMichigan Health has the ability to exercise significant influence over the operating and financial decisions of the investee, but does not have operational control, is accounted for on the equity basis (see Note 14), and the income (loss) is reflected in other revenue. An ownership interest in a health-related entity of less than 20%, in which MidMichigan Health does not have the ability to exercise significant influence over the operating and financial decisions of the investee, is carried at fair value, which is not material to the consolidated financial statements.

Other Assets

Other assets include prepaid postretirement assets, long-term notes receivable, and definite-lived intangible assets. The net balances of definite-lived intangible assets include noncompete agreements, payor contracts, and other definite-lived intangible assets with finite lives amortized using the straight-line method over their estimated useful life, which is estimated to be 10 years.

Net Assets without Donor Restrictions

Net assets without donor restrictions are available for use in general operations and are not subject to donor restrictions. The governing board has designated, from net assets without donor restrictions, net assets for future use as described in Note 6.

Net Assets with Donor Restrictions

Net assets with donor restrictions are those subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. These assets are generally restricted for funding a specific program, capital projects, and other purposes. Other donor restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. These assets are generally restricted to provide ongoing income for a specific program.

During fiscal 2019 and 2018, net assets were released from donor restrictions for purchasing property and equipment of \$352 and \$1,850, respectively, and incurring expenses of \$1,950 and \$2,715, respectively, both of which satisfied the restricted purposes of the donors. Net assets released from restriction used in operations are included in other revenue in the accompanying consolidated statements of operations and changes in net assets.

Noncontrolling Interests

The consolidated financial statements include all assets, liabilities, revenue, and expenses of less than 100% owned or controlled entities that MidMichigan Health controls in accordance with applicable accounting guidance. Accordingly, MidMichigan Health has reflected a noncontrolling interest for the portion of net assets not owned or controlled by MidMichigan Health on the consolidated balance sheets.

Contributions

Contributions, including unconditional promises to contribute cash and other assets are recognized at fair value at the time received. For financial reporting purposes, MidMichigan Health distinguishes between contributions that are without donor restrictions and those that have donor restrictions placed on their use by the donors. Conditional gifts are reported at fair value when the conditions have been substantially met. Contributions are reported as net assets with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When the restrictions have been met, these restricted contributions are recorded as net assets without donor restrictions and reported in the consolidated statements of operations and changes in net assets as other revenue (if time restricted or restricted for operating purposes) or reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions used for purchase of property and equipment (if restricted for capital acquisition). Contributions for which donors have not stipulated restrictions are reported as other revenue in the consolidated statements of operations and changes in net assets.

Other Revenue

Other revenue includes assets released from restrictions, cafeteria sales, reimbursement of outside services, county emergency medical services subsidies, income from contract pharmacy arrangements, performance incentives, and other miscellaneous sources.

Self-Insured Employee Benefits

Most of the employees of MidMichigan Health are covered by the self-funded employee health insurance program. The provisions of this program permit employees and their dependents to elect to receive medical care at either subsidiaries of MidMichigan Health or other health care providers. MidMichigan Health pays the claims as incurred. Net patient service revenue includes \$22,714 and \$18,629 for fiscal 2019 and 2018, respectively, for medical services provided by MidMichigan Health to its employees and dependents in such years. Employee health claims under the self-insurance plan that are provided by MidMichigan Health are recognized as employee benefits expense and net patient service revenue in the consolidated statements of operations and changes in net assets. Included in accrued expenses is \$9,002 and \$6,695 for estimated unprocessed claims and claims incurred, but not reported, as of June 30, 2019 and 2018, respectively.

Estimated Professional Liability Costs

The provision for insurance includes estimated medical malpractice claims. These estimates include the ultimate costs for both reported claims and claims incurred, but not reported.

Tax Status

MidMichigan Health and all subsidiaries, except MHDA, MCCO, and MidMichigan Health Pain Management, have been recognized as exempt from federal income taxes under provisions of the Internal Revenue Code (IRC) Section 501(a) as organizations described in IRC Section 501(c)(3). All of these exempt organizations are classified as public charities. MHDA is exempt from federal income taxes under provisions of IRC Section 501(a) as an organization described in Section 501(c)(2). MCCO is a single-member limited liability company, and the majority of its activity is considered exempt from tax since it is conducted by MidMichigan Health. MidMichigan

Health Pain Management is a two-member for-profit limited liability company, in which MidMichigan Health holds a 51% majority interest. MidMichigan Health's share of this income is considered exempt from tax. MidMichigan Health does not have any material uncertain tax positions as of June 30, 2019 and 2018.

Consolidated Statements of Operations and Changes in Net Assets

For purposes of display, transactions deemed by management to be ongoing, major, or necessary for our mission, delivering health care to our communities, are reported as operating revenue and expenses. Peripheral or incidental transactions are reported as nonoperating income.

Other Items

Other items include unusual and nonrecurring revenues and expenses. During 2019, MidMichigan Health recognized a nonrecurring postretirement settlement of \$1,325 related to the termination of the MidMichigan Health – ARMC Medicare Part B reimbursement program. During 2018, MidMichigan Health recognized a nonrecurring asset impairment charge for receivables of \$10,735 related to recording patient receivables at their net realizable value.

Performance Indicator

The consolidated statements of operations and changes in net assets include the excess of revenue over expenses as the performance indicator. Excess of revenue over expenses includes all changes in net assets without donor restrictions, except for permanent transfers of assets to and from subsidiaries for other than goods and services, contributions of (and assets released from donor restrictions related to) long-lived assets, and other items that are required by GAAP to be reported separately (such as postretirement-related changes other than net periodic postretirement costs, and the cumulative effect of changes in accounting principles). Certain income and expenses that are included in the performance indicator are separately presented as other items.

Nonoperating Income

Nonoperating income includes items not directly associated with patient care or other activities not relating to the core operations of MidMichigan Health. Nonoperating income consists primarily of investment income (including interest, dividends, and realized and unrealized gains and losses).

Accounting Pronouncements Adopted

In May 2014, the FASB issued ASU No. 2014-09. This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance, and requires significantly expanded disclosures about revenue recognition. The core principle of the revenue guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Effective July 1, 2018, MidMichigan Health adopted this guidance using a modified retrospective method of application, which resulted in changes to the presentation and disclosure of revenue as previously discussed in Note 2.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-For-Profit Entities*. This guidance simplifies and improves how not-for-profit entities classify net assets, as well as the information presented in financial statements and notes about liquidity, financial performance, and cash flows. This guidance was effective for MidMichigan Health for the reporting period ended June 30, 2019. The adoption of this guidance expanded certain footnote disclosures and changed the presentation to two classes of net assets versus the previously required three classes. Although the adoption

affected the presentation of net assets, it had no impact to the total amount of net assets or revenues over expenses shown in the consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This guidance requires equity investments to be measured at fair value with changes in fair value recognized in net income and amends certain disclosure requirements associated with the fair value of financial instruments. MidMichigan Health early adopted the guidance as of July 1, 2018 and reclassified \$145,748 of cumulative unrealized investment gains on certain equity investments from change in unrealized investment return in net assets without donor restrictions to net cumulative unrealized gain on equity investments due to adoption of ASU No. 2016-01 in the consolidated statements of operations and changes in net assets.

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made*. This guidance clarifies and improves the accounting for contributions received and contribution made and current guidance about whether a transfer of assets is a contribution or an exchange transaction. This guidance was effective for MidMichigan Health beginning July 1, 2018. The adoption of this guidance did not have a material impact on MidMichigan Health's consolidated financial statements.

Accounting Pronouncements Pending Adoption

In November 2018, the FASB issued ASU No. 2018-18, *Collaborative Arrangements (Topic 808): Clarifying the Interaction between Topic 808 and Topic 606*. This guidance clarifies whether certain transactions between collaborative arrangement participants should be accounted for with revenue under Topic 606. This guidance is effective for MidMichigan Health beginning July 1, 2021. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles – Goodwill and Other – Internal-use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. This guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software and hosting arrangements that include an internal-use software license. This guidance is effective for MidMichigan Health beginning July 1, 2021. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-14, *Compensation-Retirement Benefits-Defined Benefit Plans-General (Subtopic 715-20): Disclosure Framework-Changes to the Disclosure Requirements for Defined Benefit Plans*. This guidance, as part of the FASB's disclosure framework project to improve the effectiveness of the notes to the financial statements, removes, clarifies, and adds certain disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance is effective for MidMichigan Health beginning July 1, 2022. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement*. This guidance modifies and improves the effectiveness of fair value measurement disclosures as part of the FASB's disclosure framework project. This guidance is effective for MidMichigan Health beginning July 1, 2020. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In March 2017, the FASB issued ASU No. 2017-07, *Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This guidance requires the service cost component of net periodic benefit cost related to defined benefit pension and postretirement benefit plans to be reported in the same financial statement line as other compensation costs arising from

services rendered during the period. The other components of net periodic benefit cost are required to be presented separately from service costs and outside of operating income in the consolidated statements of operations and changes in net assets. Only the service cost component of net periodic benefit cost will be eligible for capitalization in assets. This guidance is effective for MidMichigan Health beginning July 1, 2019. The adoption of this guidance will result in the reclassification of \$6,280 of other components of net periodic pension cost from a benefits expense credit to nonoperating income in the consolidated statements of operations and changes in net assets.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. This guidance adds and clarifies guidance in the presentation of changes in restricted cash on the statement of cash flows and requires restricted cash to be included with cash and cash equivalents in the consolidated statements of cash flows. This guidance does not provide a definition of restricted cash. This guidance is effective for MidMichigan Health beginning July 1, 2019. The adoption of this guidance is not expected to have a material impact on MidMichigan Health's consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This guidance adds or clarifies guidance on the classification of certain cash receipts and payments in the consolidated statements of cash flows. This guidance is effective for MidMichigan Health beginning July 1, 2019. The adoption of this guidance is not expected to have a material impact on MidMichigan Health's consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. This guidance increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The primary change is the recognition on the balance sheet of lease assets for the right to use of the underlying asset and lease liability for the obligation to make payments by lessees for leases currently classified as operating leases. MidMichigan Health is adopting the optional cumulative-effect adjustment method of transition to apply the lease standard at the adoption date of July 1, 2019. Upon adoption, MidMichigan Health will record operating lease right-of-use assets and operating lease liabilities of \$8,400, representing the present value of future lease payments under operating leases.

3. BUSINESS ACQUISITION

MidMichigan Health entered into the following significant acquisition activity during the year ended June 30, 2018:

John Tolfree Hospital (dba West Branch Regional Medical Center) and subsidiaries

As part of the agreement between MidMichigan Health and WBRMC, MidMichigan Health committed to invest \$28,000 over the next 10 years for capital improvements in West Branch, funding of West Branch's retirement plan obligations, and the assumption of all liabilities, including all current and long-term debt.

West Branch assets include an 88-bed hospital located in West Branch, Michigan that provides comprehensive inpatient and outpatient services. West Branch subsidiaries include Tolfree Foundation and Hospice of Helping Hands, Inc. The primary purpose of the acquisition is to further the missions of MidMichigan Health and West Branch, provide new opportunities and efficiencies, and further the health system's response to health reform, ensuring that the health care needs of the communities served will continue to be met.

The acquisition resulted in the recognition of an inherent contribution of \$14,737 for the year ended June 30, 2018, in the consolidated statement of operations and changes in net assets. For the year ended June 30, 2019, a reduction of \$1,236 was made to the total asset value and the inherent contribution that was initially recorded at the time of acquisition, as allowed under ASC 805 *Business Combinations* during the measurement period.

Summarized consolidated balance sheet information for West Branch as of April 1, 2018, is shown below:

	2018
Cash and cash equivalents	\$ 1,687
Accounts receivable — net	5,088
Other current assets	3,473
Assets limited or restricted as to use	12,225
Property and equipment — net	32,819
Investments in joint ventures	<u>237</u>
Total assets acquired	<u>\$ 55,529</u>
Accounts payable and accrued expenses	\$ 2,176
Salaries, wages, and payroll-related liabilities	1,636
Estimated third-party settlements payable	1,780
Other current liabilities	1,026
Accrued pension and postretirement benefits	16,338
Long-term debt — less current portion	11,558
Other liabilities	<u>5,016</u>
Total liabilities assumed	<u>\$ 39,530</u>
Unrestricted net assets	\$ 14,737
Temporarily restricted net assets	121
Permanently restricted net assets	<u>1,141</u>
Total net assets	<u>\$ 15,999</u>

Operating results of West Branch, for the period from April 1, 2018, through June 30, 2018, included total revenues of \$11,614, operating losses of \$1,161, and expenses over revenue of \$(928).

4. NET PATIENT SERVICE REVENUE

A substantial portion of net patient service revenue is paid by Medicare, Medicaid, and Blue Cross based on contractual rates or under cost-reimbursement agreements in 2019 and 2018. Provisions for estimated retroactive adjustments under these agreements for current and prior years have been reflected in the accounts based upon the most current information available. Revenue disclosures under ASC 606 include enhanced disclosures on the disaggregation of revenue. The composition of net patient service revenue recognized by major payor source and service line for the year ended June 30, 2019, is as follows:

	<u>2019</u>	
Medicare	\$ 439,534	47.3 %
Blue Cross	191,177	20.6
Medicaid	127,253	13.7
Commercial, self-pay, and other	<u>170,201</u>	<u>18.4</u>
Total net patient service revenue by payor	<u>\$ 928,165</u>	<u>100.0 %</u>

	<u>2019</u>	
Hospital operations	\$ 786,896	84.8 %
Physician operations	116,840	12.6
Home health	<u>24,429</u>	<u>2.6</u>
Total net patient service revenue by service line	<u>\$ 928,165</u>	<u>100.0 %</u>

Under ASC 605, MidMichigan Health's revenue disclosure shows the sources of net patient service revenue before provision for uncollectible accounts for the year ended June 30, 2018, as follows:

	<u>2018</u>	
Medicare	\$ 391,243	46.1 %
Blue Cross	168,303	19.8
Medicaid	102,238	12.1
Commercial, self-pay, and other	<u>186,718</u>	<u>22.0</u>
Net patient service revenue	<u>\$ 848,502</u>	<u>100.0 %</u>

A summary of the payment arrangements by major payor source is as follows:

Medicare — Inpatient and outpatient services rendered to Medicare program beneficiaries are paid primarily at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Certain items are reimbursed at a tentative rate, with final settlement determined after submission of annual cost reports and audits thereof by the Medicare Administrative Contractors.

Medicaid — Reimbursement for services rendered to Medicaid program beneficiaries includes prospectively determined rates per discharge, per diem payments, and discounts from established charges, statewide distribution pools, fee schedules, and cost-reimbursement methodologies, with certain limitations. Cost-reimbursable items are reimbursed at a tentative rate, with final settlement determined after submission of annual cost reports and audits thereof by the Medicare Administrative Contractor and state Medicaid administrators.

In December 2003, the Centers for Medicare and Medicaid Services (CMS) approved the Michigan Hospital Assessment Program (the "Program") to improve Medicaid reimbursement for Michigan hospitals. The Program increased net patient service revenue in the form of additional Medicaid payments and increased fees through tax assessments from the State of Michigan. The net benefit to MidMichigan Health from the Program was \$27,305 and \$19,628 during the years ended June 30, 2019 and 2018, respectively. For the years ended June 30, 2019 and 2018, the Medicaid payment of \$48,360 and \$37,042, respectively, was included in net patient service revenue, representing 5.2% and 4.4%, respectively, of the net patient service revenue, and the tax assessment of \$21,055 and \$17,414, respectively, was included in professional fees and other in the consolidated statements of operations and changes in net assets. The Program is subject to federal acceptance of the assessments for federal matching funding and may be limited or eliminated in the future.

Blue Cross Blue Shield of Michigan — Reimbursement for services to subscriber patients include prospectively set, clinically adjusted per discharge rates, per diem rates, fee schedule rates, and discounts from established charges.

Commercial, Self-Pay, and Other — Reimbursement for services to certain patients is received from commercial insurance carriers, health maintenance organizations, preferred provider organizations, and directly from patients. The basis for reimbursement includes prospectively determined rates per discharge, per diem payments, and discounts from established charges. Michigan law limits amounts collectable from uninsured patients.

Changes in estimates relating to prior periods increased net patient service revenue by \$5,031 and \$1,767 in fiscal 2019 and 2018, respectively. Laws and regulations governing government and other payment programs are complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimated third-party settlements could change by a material amount.

As of June 30, 2019, letters of final settlements have not been received from Medicare for fiscal 2016 through fiscal 2019, Blue Cross for fiscal 2019, and Medicaid for fiscal 2016 through fiscal 2019. The estimated receivables from or payables to third-party payors related to settlements are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as needed until final settlements are determined. In addition, MidMichigan Health filed formal appeals relating to the settlement of certain prior-year Medicare cost reports.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medicaid programs, can be subject to review and interpretation, as well as regulatory actions unknown and unasserted at this time. Federal government activity continues with respect to investigations and allegations concerning possible violations of regulations by health care providers, which could result in the imposition of significant fines and penalties, as well as significant repayment of previously billed and collected revenues from patient services. Management believes that MidMichigan Health is in compliance with current laws and regulations.

5. CHARITY CARE AND COMMUNITY BENEFIT

As part of its mission, MidMichigan Health provides services to patients without regard to their ability to pay for these services. For some of its patient services, MidMichigan Health receives no payment or payment that is less than the full cost of providing the services. Additionally, MidMichigan Health demonstrates its exempt purpose to benefit the communities it serves by operating emergency rooms and other clinical services open to the public 24 hours a day, seven days a week; providing facilities for the education and training of health care professionals; and conducting research for the study of new drugs that offer the promise of improving health care.

MidMichigan Health has an established charity care policy and maintains records to identify and monitor the level of charity care it provides. MidMichigan Health voluntarily provides free care to all patients who are unable to pay for all or part of their health care expenses as determined by MidMichigan Health's criteria for charity care. MidMichigan Health reports charity care on the basis of cost, as computed using a cost-to-charge ratio methodology. In addition to charity care, MidMichigan Health provides services to Medicare, Medicaid, and other public programs for which the payments received are less than the cost of providing services. The unpaid costs attributed to providing services under these programs are considered a community benefit. MidMichigan Health also provides research and community health services, such as community education and outreach in the form of free or low-cost clinics; health education; donations for the community; multiple health promotion and wellness programs, such as health screening; and various community projects and support groups.

MidMichigan Health's quantifiable costs of charity care and unreimbursed Medicaid, community benefits, and other uncompensated care provided for the years ended June 30, 2019 and 2018, are as follows:

	2019	2018
Charity care and unreimbursed Medicaid — at cost:		
Charity care	\$ 7,456	\$ 9,433
Unreimbursed Medicaid	<u>24,864</u>	<u>35,256</u>
Total charity care and unreimbursed Medicaid — at cost	<u>32,320</u>	<u>44,689</u>
Community benefits — at cost:		
Medical education	10,255	9,987
Community services, including community building activities of \$275 and \$599 for the years ended June 30, 2019 and 2018, respectively	<u>1,662</u>	<u>2,120</u>
Total community benefits — at cost	<u>11,917</u>	<u>12,107</u>
Total charity care and unreimbursed Medicaid and community benefits — at cost	<u>44,237</u>	<u>56,796</u>
Other uncompensated care — at cost:		
Uncompensated services	16,650	20,124
Unreimbursed Medicare	<u>29,984</u>	<u>29,193</u>
Total other uncompensated care — at cost	<u>46,634</u>	<u>49,317</u>
Total community benefit — at cost	<u>\$ 90,871</u>	<u>\$ 106,113</u>

6. ASSETS LIMITED AS TO USE AND INVESTMENTS

Assets limited as to use and investments consist primarily of marketable equity and debt securities, which are held in investment pools to satisfy the investment objectives for which the assets are held or to satisfy donor restrictions. MidMichigan Health also holds certain investments in alternative securities consisting of hedge funds and real estate investments (see Note 2). Assets limited as to use by donor or time restriction also include unconditional promises to contribute.

A summary of the composition of assets limited as to use and investments as of June 30, 2019 and 2018, is as follows:

	2019	2018
Assets without donor restrictions:		
Investments	\$ 139,434	\$ 132,180
Funds designated for malpractice and general liability	22,659	23,480
Funds designated for deferred compensation	27,898	25,918
Funds designated for debt service	15,768	15,447
Funds board designated for capital and other	<u>538,253</u>	<u>488,536</u>
Total assets without donor restrictions	<u>744,012</u>	<u>685,561</u>
Assets with donor restrictions:		
Perpetual in nature	17,523	16,903
Purpose restricted	27,730	21,248
Pledges receivable and other	<u>4,903</u>	<u>9,489</u>
Total assets with donor restrictions	<u>50,156</u>	<u>47,640</u>
Total assets limited as to use and investments	794,168	733,201
Less requirements for current liabilities	<u>(19,270)</u>	<u>(17,447)</u>
Noncurrent assets limited as to use and investments	<u>\$ 774,898</u>	<u>\$ 715,754</u>

Substantially all pledges are deemed collectible and consist of the following amounts as of June 30, 2019:

Years Ending June 30

2020	\$ 3,453
2021	1,359
2022	252
2023	251
2024 and thereafter	<u>2</u>
Total expected collections	5,317
Unamortized discount	<u>(414)</u>
Total pledges receivable and other	<u>\$ 4,903</u>

The composition and presentation of investment income and the realized and unrealized gains and losses on all investments for the years ended June 30, 2019 and 2018, are as follows:

	2019	2018
Interest and dividends — net	\$ 9,350	\$ 6,397
Realized gains — net	194	48,143
Unrealized investment return	<u>28,219</u>	<u>(14,911)</u>
Total investment return	<u>\$ 37,763</u>	<u>\$ 39,629</u>
Reported as:		
Nonoperating income	\$ 37,763	\$ 60,058
Changes in unrealized investment return	<u>-</u>	<u>(20,429)</u>
Total investment return	<u>\$ 37,763</u>	<u>\$ 39,629</u>

7. FAIR VALUE MEASUREMENTS

As of June 30, 2019 and 2018, MidMichigan Health’s consolidated financial statements reflect certain assets and liabilities recorded at fair value. Assets and liabilities measured at fair value on a recurring basis in MidMichigan Health’s consolidated financial statements include cash, cash equivalents, investment funds, commingled funds, and pension and postretirement assets. Liabilities measured at fair value on a recurring basis for disclosure only include debt.

Valuation Principles

Under accounting guidance on fair value measurements, fair value is defined as an exit price, representing 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. The valuation techniques used to measure fair value are based upon observable and unobservable inputs. Observable inputs generally reflect market data from independent sources and are supported by market activity, while unobservable inputs are generally unsupported by market activity. The three-level valuation hierarchy, which prioritizes the inputs used in measuring fair value of an asset or liability at the measurement date, includes:

Level 1 Inputs — Quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 Inputs — Quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets and liabilities in nonactive markets, and model-driven valuations whose inputs are observable for the asset or liability, either directly or indirectly.

Level 3 Inputs — Unobservable inputs for which there is little or no market data available and are based on the reporting entity’s own judgment or estimation of the assumptions that market participants would use in pricing the asset or liability.

Valuation Methodologies

The instruments listed in the preceding fair value tables use the following valuation techniques and inputs as of the valuation date:

Cash and Cash Equivalents — The carrying amounts reported in the consolidated balance sheets approximate their fair value. Certain cash and cash equivalents are included in investments and assets limited or restricted as to use in the consolidated balance sheets.

Equity Securities — Equity securities are valued at the closing price reported on the applicable exchange on which the security is traded and are classified as Level 1 within the fair value hierarchy.

Mutual Funds — Mutual funds are valued using the NAV based on the value of the underlying assets owned by the fund, minus liabilities, divided by the number of shares outstanding, and multiplied by the number of shares owned and are classified as Level 1 within the fair value hierarchy.

Collective Funds — Collective funds are developed for investment by institutional investors only and, therefore, do not require registration with the Securities and Exchange Commission. Collective funds and other nonpublicly traded securities are recorded at fair value based on NAV, which is calculated using the most recent fund financial statements. The funds in this class include fixed-income and equity investments.

Real Estate — MidMichigan Health invests in various commingled real estate funds that are included in investments and assets limited or restricted as to use in the consolidated balance sheets. Real estate funds are recorded based on NAV, which is calculated using the most recent financial statement.

Hedge Fund of Funds — This class includes diversified investments in hedge fund of funds with diverse strategies, including equity long/short, credit long/short, event-driven, relative value, global opportunities, and other multistrategy funds. Hedge fund of funds investments are valued based on MidMichigan Health's ownership interest in the NAV of the respective fund as estimated by the general partner, which approximates fair value. The values for underlying investments are estimated either internally or by an external fund manager based on many factors, including operating performance, balance sheet indicators, growth, and other market and business fundamentals.

Other — Other includes pledges receivable and restricted real estate, which are recorded at fair value based on estimated values and third-party appraisals.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while MidMichigan Health believes that its methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Fair Value Measurements at the Consolidated Balance Sheet Date

The following tables present MidMichigan Health's financial assets measured at fair value on a recurring basis by fair value hierarchy, as of June 30, 2019 and 2018:

Fair Value Measurements as of June 30, 2019	Level 1	Level 2	Level 3	Total Fair Value
Assets:				
Cash equivalents	\$ 22,554	\$ 905	\$ -	\$ 23,459
Mutual funds:				
Fixed-income funds	165,571	-	-	165,571
US equity funds	30,114	-	-	30,114
Non-US equity funds	51,871	-	-	51,871
Equity securities:				
Common stock	1,745	-	-	1,745
Other	<u>4,677</u>	<u>1,016</u>	<u>3,320</u>	<u>9,013</u>
Total — assets at fair value	<u>\$ 276,532</u>	<u>\$ 1,921</u>	<u>\$ 3,320</u>	281,773
Investments measured at net asset value:				
Equity securities:				
Collective funds — US fixed income				76,866
Collective funds — US equity				128,828
Collective funds — Non-US equity				207,927
Alternatives:				
Real estate				79,740
Hedge fund of funds				<u>34,388</u>
Total — assets				<u>\$ 809,522</u>
Fair Value Measurements as of June 30, 2018	Level 1	Level 2	Level 3	Total Fair Value
Assets:				
Cash equivalents	\$ 34,170	\$ 890	\$ -	\$ 35,060
Mutual funds:				
Fixed-income funds	159,399	-	-	159,399
US equity funds	27,637	-	-	27,637
Non-US equity funds	46,339	-	-	46,339
Equity securities:				
Common stock	2,663	-	-	2,663
Other	<u>9,122</u>	<u>2,632</u>	<u>3,320</u>	<u>15,074</u>
Total — assets at fair value	<u>\$ 279,330</u>	<u>\$ 3,522</u>	<u>\$ 3,320</u>	286,172
Investments measured at net asset value:				
Equity securities:				
Collective funds — US fixed income				57,062
Collective funds — US equity				111,879
Collective funds — Non-US equity				190,462
Alternatives:				
Real estate				75,123
Hedge fund of funds				<u>32,918</u>
Total — assets				<u>\$ 753,616</u>

There were no security transfers between Levels 1, 2, and 3 during the years ended June 30, 2019 and 2018.

The following table reconciles the information about the fair value of MidMichigan Health's financial instruments measured at fair value on a recurring basis presented in the table above to the amounts presented in the consolidated balance sheets for the years ended June 30, 2019 and 2018:

	2019	2018
Assets:		
Cash and cash equivalents	\$ 15,581	\$ 20,782
Assets limited or restricted as to use — current portion	19,270	17,447
Assets limited as to use and investments:		
Investments	139,434	132,180
Limited as to use by Board for capital acquisitions	538,253	488,536
Self-insurance, deferred compensation, and other	47,055	47,398
Limited as to use by donor or time restriction	50,156	47,640
Less items not recorded at fair value:		
Loan receivable	(227)	(367)
Total assets	<u>\$ 809,522</u>	<u>\$ 753,616</u>

Level 3 Assets

Assets classified by MidMichigan Health within Level 3 of the fair value hierarchy include donated real estate (land and building) valued at \$3,320 based upon appraisals and tax records at the time of donation. There was no change in the fair value during the year ended June 30, 2019.

Investments in Entities That Report Fair Value using NAV

Included within the fair value table above are investments in certain entities that report fair value using a calculated NAV or its equivalent. The following table summarizes the attributes relating to the nature and risk of such investments as of June 30, 2019:

Entities That Report Fair Value Using NAV	Fair Value 2019 (In Thousands)	Fair Value 2018 (In Thousands)	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Equity funds	\$ 336,755	\$ 302,341	None	Daily/Monthly	4–30 days
Fixed-income funds	76,866	57,062	None	Daily	5 days
Real estate investment funds	79,740	75,123	None	Quarterly	60 days
Hedge fund of funds	34,388	32,918	None	Semiannual	95 days

8. ENDOWMENTS

MidMichigan Health's endowments consist of various funds established for specific purposes. Its endowments include only donor-restricted endowment funds. Net assets associated with endowment funds are classified and reported based on the existence of donor-imposed restrictions. MidMichigan Health considers various factors in making a determination to appropriate or accumulate donor-restricted endowment funds.

The assets are managed in investment pools. The pools use a targeted asset allocation of 45% equity securities, 10% global balanced funds, 30% fixed-income, 10% real estate, and 5% hedge funds. In general, MidMichigan Health uses a long-term rate of return, which is evaluated periodically, to allocate investment earnings to its endowment funds, thus eliminating investment risk on its endowments. The endowment corpus is maintained in perpetuity. MidMichigan Health's spending policy is used as a guideline, in the absence of explicit donor restrictions, to allocate a portion of annual earnings to be maintained in perpetuity along with the corpus. Only amounts exceeding the amounts required to be maintained in perpetuity are expended.

Endowment amounts classified as net assets with donor restrictions as of June 30, 2019 and 2018, are described below:

	2019	2018
Net assets with donor restrictions:		
Hospital capital support	\$ 7,704	\$ 7,485
Hospital operations support	2,893	2,995
Scholarship funds and education	5,001	5,000
Community service funds	<u>1,925</u>	<u>1,423</u>
Total endowment funds	<u>\$ 17,523</u>	<u>\$ 16,903</u>

Changes in endowment net assets for the fiscal years ended June 30, 2019 and 2018, include:

	2019	2018
Endowment net assets — July 1	<u>\$ 16,903</u>	<u>\$ 14,653</u>
Investment return:		
Investment income — net of annual spending appropriation	273	258
Change in net realized and unrealized gains and losses	<u>(131)</u>	<u>26</u>
Total investment return	<u>142</u>	<u>284</u>
Contributions	478	825
Acquisition of West Branch	<u>-</u>	<u>1,141</u>
Endowment net assets — June 30	<u>\$ 17,523</u>	<u>\$ 16,903</u>

Funds with Deficiencies

Periodically, the fair value of assets associated with the individual donor-restricted endowment funds may fall below the level that the donor requires MidMichigan Health to retain as a fund of perpetual duration (underwater endowments). Deficiencies of this nature are reported in net assets without donor restrictions. These deficiencies result from unfavorable market fluctuations or continued appropriation for certain programs that continue to be considered necessary by MidMichigan Health. There were no such deficiencies as of June 30, 2019 and 2018.

9. PROPERTY AND EQUIPMENT

Property and equipment as of June 30, 2019 and 2018, consisted of the following:

	2019	2018
Land and improvements	\$ 42,418	\$ 41,720
Building and improvements	508,318	451,949
Equipment	321,395	323,146
Construction in progress	<u>16,837</u>	<u>30,237</u>
Total	888,968	847,052
Less accumulated depreciation	<u>(446,501)</u>	<u>(416,843)</u>
Property and equipment — net	<u>\$ 442,467</u>	<u>\$ 430,209</u>

Internal-use software is included above in equipment. The net book value was \$36,709 and \$41,774 as of June 30, 2019 and 2018, respectively.

Construction in progress as of June 30, 2019, includes \$2,738 for the second phase of the Cardiovascular Regional Referral Center in Midland (including related relocations), \$6,629 for the new West Branch Emergency Department, \$1,154 for the new Alpena Patient Tower, as well as various smaller capital projects. As of June 30, 2019, significant commitments include \$1,416 related to the Cardiovascular Regional Referral Center.

The book value of equipment under capital lease obligations at June 30, 2019 and 2018, totaled \$1,923 and \$1,845, respectively. The related accumulated depreciation totaled \$600 and \$168, respectively, at June 30, 2019 and 2018. These amounts are included in the above summary of property and equipment.

10. LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS

MidMichigan Health currently has debt outstanding under a master indenture dated December 1, 2014 (the "Master Indenture"), which established an obligated group composed of MidMichigan Health and Midland. The Master Indenture, as supplemented thereto, permits MidMichigan Health to issue obligations to finance certain capital acquisitions and improvements. The MidMichigan Health Credit Group, under the Master Indenture, consists of the obligated group members and all of MidMichigan Health's active controlled subsidiaries, with the exception of MCCO and West Branch. Under the Master Indenture, debt is generally issued as unsecured direct obligations of MidMichigan Health and any future members of the MidMichigan Obligated Group. Proceeds from the tax-exempt revenue and refunding bonds are to be used to finance the construction, acquisition, and equipping of capital improvements. All members of the MidMichigan Obligated Group are jointly and severally liable for debt outstanding of \$202,166 carrying value and \$207,108 fair value as of June 30, 2019.

A summary of MidMichigan Health's long-term debt as of June 30, 2019 and 2018, is as follows:

	Interest Rates	Final Maturity Date	June 30,	
			2019	2018
Fixed-rate revenue bonds:				
Michigan Finance Authority				
Revenue Bonds:				
Series 2014	4.00%–5.00%	June 1, 2039	\$ 163,620	\$ 165,455
Gratiot Community Hospital Finance Authority				
Revenue Bonds:				
Series 1998	5.34%	December 1, 2018	-	116
Other loans payable:				
United States Department of Agriculture Loans	3.25%	October 28, 2035	10,990	11,497
Total fixed-rate debt			174,610	177,068
Variable-rate revenue bonds:				
Michigan Finance Authority				
Revenue Bonds:				
Series 2016	1.28%–2.55%	October 1, 2031	25,000	27,000
Hospital Equipment Loan Program Bonds:				
Series D	0.50%–2.00%	September 15, 2020	1,896	3,413
Total variable-rate debt			26,896	30,413
Other debt:				
Capital lease obligations collateralized				
by equipment	2.75%–6.50%	October 18, 2022	1,793	2,314
Total other debt			1,793	2,314
Total debt and capital lease obligations			203,299	209,795
Less current portion of long-term debt and capital lease obligations			(7,779)	(6,496)
Unamortized debt issue costs on bonds			(1,426)	(1,483)
Unamortized premium on bonds			14,962	15,922
Long-term debt and capital lease obligations — net			\$ 209,056	\$ 217,738
Estimated fair value based on quoted market prices and other relevant information (Level 2 classification)			\$ 221,778	\$ 224,035

Fair Value of Debt

The valuation of the estimated fair value of MidMichigan Health's fixed-rate long-term debt is completed by an independent third party using a pricing scale based on spreads to municipal market data of comparable transactions that price in the market, as well as secondary market trades for comparable credits. As MidMichigan Health is responsible for the determination of fair value, it performs periodic analyses on the prices received from independent third parties to determine whether the prices are reasonable estimates of fair value. As a result of these reviews, MidMichigan Health has not historically adjusted the prices obtained from third parties. Since such

amounts are estimated based on limited available market information and do not acknowledge certain restrictions that may exist, the actual fair value market values for these obligations may differ significantly from what is provided herein or upon settlement of the obligation. The carrying value of MidMichigan Health's variable-rate bonds and other obligations approximates the fair value.

Master Indenture and Other Requirements

Under its various indebtedness agreements, the MidMichigan Health Credit Group is subject to certain financial covenants, including maintaining a minimum historical debt-service coverage and maximum annual debt-service coverage ratios; limitations on selling, leasing, or otherwise disposing of MidMichigan Obligated Group property; and certain other nonfinancial covenants. MidMichigan Health has no knowledge of any default in the performance of the terms, covenants, provisions, or conditions of the Master Indenture. Long-term obligations outstanding as of June 30, 2019 and 2018, excluding amounts issued under the Master Indenture, are generally collateralized by certain property and equipment and secured by a letter of credit with a third-party institution. As of June 30, 2019 and 2018, there were no outstanding draws against the letter of credit related to the Series D Hospital Equipment Loan Program Bonds, which are not subject to remarketing. This letter of credit expires in June 2020. As of June 30, 2019 and 2018, the outstanding obligation was \$1,896 and \$3,413, respectively, which approximated the net book value of property and equipment collateralized. Annual principal payments on long-term debt as of June 30, 2019, are due as follows:

Years Ending June 30

2020	\$ 7,779
2021	6,820
2022	6,555
2023	6,391
2024	6,436
Thereafter	<u>169,318</u>
Total	<u>\$ 203,299</u>

Acquisition/Financing Activities

The acquisition of West Branch, during the year ended June 30, 2018, as described in Note 3, resulted in the assumption of debt of \$12,215. The majority of this debt, \$11,621, is fixed-rate, 20-year loans payable with the United States Department of Agriculture. Under the terms of the loans, West Branch is required to maintain certain deposits with a trustee.

11. OTHER LONG-TERM LIABILITIES

The composition of other long-term liabilities as of June 30, 2019 and 2018, is as follows:

	2019	2018
Self-insurance liabilities	\$ 23,725	\$ 19,600
Estimated payables to third-party payors, long-term	23,845	13,984
Deferred compensation plan liabilities	29,592	28,696
Asset retirement obligations	10,609	10,133
Long-term accrued fees	3,997	6,265
Equity option	3,000	3,000
Unearned revenue	3,720	3,849
Other	<u>-</u>	<u>649</u>
Total self-insurance, deferred compensation, and other liabilities	98,488	86,176
Less current portion	<u>(3,984)</u>	<u>(3,154)</u>
Total	<u>\$ 94,504</u>	<u>\$ 83,022</u>

Asset Retirement Obligations

Asset retirement obligations represent legal or contractual obligations associated with the retirement of tangible long-lived assets that are incurred upon the acquisition, construction, development, or normal operation of that long-lived asset. Asset retirement obligations are required to be recognized in the period in which they are incurred if a reasonable estimate of fair value can be made. The asset retirement obligations are accreted to their present value at the end of each reporting period. The associated estimated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over its useful life. MidMichigan Health annually evaluates its leased and owned properties for potential asset retirement obligations. Based on these reviews, MidMichigan Health identified obligations primarily related to the removal of certain materials previously utilized in the construction process.

The following table summarizes changes in the total liability for asset retirement obligations as of June 30, 2019 and 2018:

	2019	2018
Asset retirement obligation — beginning of year	\$ 10,133	\$ 8,859
Accretion	675	457
Liabilities settled	(199)	(17)
Liabilities incurred (West Branch acquisition)	<u>-</u>	<u>834</u>
Asset retirement obligation — end of year	<u>\$ 10,609</u>	<u>\$ 10,133</u>

12. PENSION, POSTRETIREMENT, AND OTHER EMPLOYEE BENEFIT PLANS

MidMichigan Health maintains a defined benefit/cash balance pension plan (the "Pension Plan"), two defined benefit pension plans (the "Alpena Pension Plan" and the "West Branch Pension Plan"), defined contribution plans, and other postretirement benefit plans that together cover substantially all of MidMichigan Health's employees.

Effective April 1, 2018, MidMichigan Health assumed the obligation for the West Branch Pension Plan, a single employer defined benefit plan, which covers the employees of West Branch. The plan was closed to new

participants. On the effective date, \$24,628 of benefit obligations and \$15,806 of assets were assumed by MidMichigan Health. In May 2018, the plan froze benefit accruals.

Effective April 1, 2016, MidMichigan Health established a new defined benefit plan for Alpena employees, which was a spin-off of the Municipal Employees Retirement System plan that was in place for Alpena employees prior to MidMichigan Health acquiring Alpena.

Effective January 1, 2008, the Pension Plan was amended and changed to a cash balance plan. The majority of MidMichigan Health's employees participate in the qualified noncontributory Pension Plan. Benefits for the Pension Plan are based on pay credits and interest credits; at the end of each calendar year, participant accounts are credited with a percentage of the participant's annual salary. The minimum amounts required to meet the provisions of the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974 (ERISA), as amended, are funded on an annual basis, plus any additional amounts that MidMichigan Health may determine to be appropriate. Plan assets and obligations are measured as of June 30 (the "Measurement Date") each year. The Pension Plan can be terminated by the board subject to certain notification requirements. MidMichigan Health, at this time, does not intend to terminate the Pension Plan.

In addition to the pension programs, MidMichigan Health (primarily, Midland) also provides postretirement health care benefits (the "Postretirement Healthcare Plan") to certain retirees. Further benefits under the Postretirement Healthcare Plan have been curtailed. Contributions are intended to provide not only for benefits attributed to service to date, but also for the related interest cost associated with the Postretirement Healthcare Plan. Retirees who have the Postretirement Healthcare Plan are required to make contributions toward the cost of their benefits based on their years of service at retirement. For retirements on or after January 1, 1994, retirees are required to contribute, in addition to a percentage of the premium based on years of service, the difference between actual cost for a particular year and four times the 1994 cost. Midland reserves the right to amend, modify, or terminate these benefits at any time.

A closed group of Alpena retirees were provided quarterly fixed Medicare Part B premium reimbursement under the Medicare Part B Reimbursement Program. As of January 31, 2019, participants received final reimbursement under the plan and the plan was terminated.

Effective April 1, 2018, MidMichigan Health assumed a \$7,516 postretirement obligation for the West Branch Regional Medical Center and Dental Insurance Plan for Retirees. This plan is unfunded. The plan provides a closed group of retirees' medical and dental coverage.

The table below sets forth the accumulated benefit obligation, the change in the projected benefit obligation, and the change in the plan assets of MidMichigan Health’s pension and postretirement benefit plans (collectively, the “Plans”). The table also reflects the funded status of the Plans as of the Measurement Date and amounts recognized in MidMichigan Health’s consolidated balance sheets as of June 30, 2019 and 2018.

Obligations and Funded Status	Pension Plans		Postretirement Healthcare Plans	
	2019	2018	2019	2018
Actuarial present value of accumulated benefit obligation	\$ 625,499	\$ 583,263	\$ 11,480	\$ 10,887
Change in benefit obligations:				
Benefit obligation — beginning of measurement period	\$ 608,433	\$ 594,853	\$ 10,887	\$ 4,642
Service cost	10,008	9,612	21	5
Interest cost	24,523	22,257	405	214
Acquisition of West Branch	-	24,628	-	7,516
Pension settlements	(1,077)	-	-	-
Plan changes	-	-	(496)	(708)
Actuarial gains (losses)	40,428	(17,132)	1,346	(203)
Plan participants’ contributions	220	164	-	-
Benefits paid	(28,359)	(25,949)	(683)	(579)
Projected benefit obligation — end of measurement period	\$ 654,176	\$ 608,433	\$ 11,480	\$ 10,887
Change in plan assets:				
Fair value of plan assets — beginning of measurement period	\$ 487,151	\$ 443,274	\$ 17,346	\$ 16,288
Actual return on plan assets	45,946	23,119	1,825	1,468
Acquisition of West Branch	-	15,806	-	-
Plan participants’ contributions	220	164	-	-
Employer contributions	36,194	30,737	413	193
Administrative expenses paid	-	-	(30)	(24)
Pension settlements	(1,077)	-	-	-
Benefits paid	(28,359)	(25,949)	(683)	(579)
Fair value of plan assets — end of measurement period	\$ 540,075	\$ 487,151	\$ 18,871	\$ 17,346
Accrued liability (asset)	\$ 114,101	\$ 121,282	\$ (7,391)	\$ (6,459)
Recognized in the consolidated balance sheets as follows:				
Noncurrent asset	\$ -	\$ -	\$ (16,147)	\$ (14,491)
Noncurrent liability	114,101	121,282	8,756	8,032
Accrued liability (asset)	\$ 114,101	\$ 121,282	\$ (7,391)	\$ (6,459)

The actuarial cost method used to compute the Pension Plan liabilities and expenses is the projected unit credit method.

The components of net periodic pension cost for the Plans were as follows:

Components of Net Periodic Pension Cost Years Ended June 30	Pension Plans		Postretirement Healthcare Plans	
	2019	2018	2019	2018
Net periodic pension cost comprised the following:				
Service cost	\$ 10,008	\$ 9,612	\$ 21	\$ 5
Interest cost	24,523	22,257	405	214
Expected return on plan assets	(29,356)	(27,362)	(1,012)	(1,041)
Amortization of prior service cost and other actuarial amounts	202	215	(39)	(14)
Amortization of unrecognized net loss (gain)	2,747	4,526	(103)	(76)
Settlement cost (credit)	55	-	(1,325)	-
Net periodic pension cost (credit)	<u>\$ 8,179</u>	<u>\$ 9,248</u>	<u>\$ (2,053)</u>	<u>\$ (912)</u>

In accordance with FASB guidance regarding accounting for defined benefit pension and other postretirement plans, all previously unrecognized actuarial losses and prior service costs are reflected in the consolidated balance sheets. The postretirement-related charges other than net periodic benefit cost related to the pension and postretirement health care plans are included as a separate (decrease) increase to net assets without donor restrictions and total \$(22,369) and \$18,855 for fiscal 2019 and 2018, respectively. For fiscal 2019, this amount includes actuarial losses, net prior service credit, and recognition due to plan termination arising during fiscal 2019 of \$(25,176) and a reclassification adjustment for losses and prior service cost reflected in periodic expense in fiscal 2019 of \$2,807. For fiscal 2018, this amount includes actuarial gains and net prior service credit arising during fiscal 2018 of \$14,203 and a reclassification adjustment for losses and prior service cost reflected in periodic expense in fiscal 2018 of \$4,652.

In accordance with FASB ASC Topic 715, *Compensation — Retirement Benefits*, all previously unrecognized actuarial losses are reflected in the consolidated balance sheets. The pension plan and postretirement benefit plan items not yet recognized as a component of periodic pension and postretirement medical plan expense, but included within net assets without donor restrictions, as of and for the years ended June 30, 2019 and 2018, are as follows:

	Pension Plans		Postretirement Healthcare Plans	
	2019	2018	2019	2018
Unrecognized prior service (cost) credit	\$ -	\$ (202)	\$ 246	\$ 969
Unrecognized net actuarial (loss) gain	(56,420)	(35,385)	2,903	3,716
Total	<u>\$ (56,420)</u>	<u>\$ (35,587)</u>	<u>\$ 3,149</u>	<u>\$ 4,685</u>

An estimated \$4,093 in net actuarial loss will be included as a component of periodic pension expense in fiscal 2020. An estimated \$14 in prior service credit and \$58 in net actuarial gain will be included as components of periodic postretirement medical plan expense in fiscal 2020.

Assumptions

The actuarial assumptions used to determine benefit obligations at the measurement date and net periodic benefit cost for the Plans are as follows:

Assumptions Used to Determine Benefit Obligations and Net Periodic Benefit Cost	Pension Plans		Postretirement Healthcare Plans	
	2019	2018	2019	2018
	Discount rate — benefit obligation	3.55-3.60%	4.10–4.15%	3.00-4.00%
Discount rate — pension expense	4.10-4.15	3.80–3.95	3.80-4.00	3.15–4.00
Rate of increase in compensation levels:				
2018		3.50-4.00		
2019	4.00	4.00		
2020-2021	4.00-5.00			
2022 and after	4.00			
Expected return on plan assets	6.00-7.00	6.35-6.50	6.00	6.35
Health care cost trend rate (initial)			5.50-6.67	6.00–7.08
Health care cost trend rate (ultimate)			4.50-5.00	4.50–5.00
Health care cost trend year			2027	2020–2022

The discount rate utilized to measure the Plans' obligations is based on the yield on high-quality fixed-income investments as of the measurement dates of June 30, 2019 and 2018. Future expected actuarially determined cash flows for the Plans are matched against the Towers Watson U.S. RATE:Link 10-90 Pension Discount Curve (a theoretical yield curve derived from bonds with yields that are within the 10th to 90th percentiles of the yields in a universe of AA-graded corporate bonds chosen using defined selection criteria) as of June 30, 2019 and 2018, to arrive at a single discount rate by plan. Peer data and historical returns are reviewed to ensure reasonableness and appropriateness.

MidMichigan Health determines the expected long-term rate of return on plan assets by performing a detailed analysis, with the assistance of MidMichigan Health's actuaries and investment consultants, of historical and expected returns based on the strategic asset allocation approved by the investment committee (the "Investment Committee") under the direction of the Board and the underlying return fundamentals of each asset class. For the years ended June 30, 2019 and 2018, the actual rate of return on plan assets was 9.6% and 5.5%, respectively.

Assumed health care cost trend rates generally have a significant effect on the amounts reported for the Postretirement Healthcare Plan. However, since MidMichigan Health's postretirement costs are capped and the Postretirement Healthcare Plan is closed to any new participants, the impact has been significantly mitigated.

Plan Assets

MidMichigan Health's primary investment objective for its Plans is to achieve a total return on plan assets that meets or exceeds the return on the Plans' liability over a full market cycle with consideration of the Plans' current funded status. MidMichigan Health employs a total return investment approach whereby a mix of equities and fixed-income investments are used to maximize the long-term return of plan assets for a prudent level of risk. Risk tolerance is established through careful consideration of plan liabilities, plan funded status, and MidMichigan Health's consolidated financial condition. The investment portfolio includes a diversified blend of equity and fixed-income investments. Furthermore, equity investments are diversified across US and non-US stocks, as well as growth, value, and small and large capitalizations. Investment management of the Plans is delegated to professional investment management firms that must adhere to policy guidelines and objectives. An independent

investment consultant is used to measure and report on investment performance; perform asset and liability modeling studies and recommend changes to objectives, guidelines, managers, or asset class structure; and inform MidMichigan Health of current investment trends and issues.

Based on consideration of the Plans' projected benefit obligation and long-term investment horizon, the Plans' ability to tolerate risk is in the moderate to aggressive range. Asset allocation is consistent with this level of risk, with assets being a mix of equities and fixed-income securities. Equity investments are diversified across US and non-US stocks. Minimum and maximum ranges are established for each asset class to control risk and maximize the effectiveness of the Plans' asset allocation strategy. Asset allocation is reviewed quarterly and rebalanced, if necessary. To protect against risk, derivative instruments may only be utilized when consistent with the manager's stated style and objectives and may not be used for speculative purposes. Specific investment guidelines, restrictions, and investment return objectives exist for each asset class and corresponding investment manager.

MidMichigan Health's actual weighted-average asset allocations as of June 30, 2019 and 2018, by investment category, as well as the ongoing weighted-average target allocation percentages, are as follows:

	Pension Plans	Pension Plans		Postretirement Healthcare Plans	
	Target	Actual		Actual*	
	2019	2019	2018	2019	2018
Cash and cash equivalents	- %	0.2 %	2.2 %	0.1 %	0.1 %
US equity	16.4	17.4	22.1	32.1	34.2
Non-US equity	14.4	13.8	17.4	-	-
Global equity	18.0	17.7	11.7	30.4	28.9
Emerging markets equity	2.0	1.8	2.2	-	-
Fixed income	<u>49.2</u>	<u>49.1</u>	<u>44.4</u>	<u>37.4</u>	<u>36.8</u>
Total	<u>100.0 %</u>	<u>100.0 %</u>	<u>100.0 %</u>	<u>100.0 %</u>	<u>100.0 %</u>

* Given the nature of the Postretirement Healthcare Plan (curtailed), the Investment Committee reviews and sets its allocation annually. The actual allocation approximates the targeted allocation for the Postretirement Healthcare Plan.

The Plans' asset portfolio by asset category as of June 30, 2019 and 2018, is as follows:

Asset Category as of June 30, 2019	Level 1	Level 2	Level 3	Total Fair Value
Pension plans:				
Cash and cash equivalents	\$ -	\$ 1,793	\$ -	\$ 1,793
Mutual funds:				
Fixed-income funds	81,185	-	-	81,185
US equity fund	33,469	-	-	33,469
Non-US equity fund	33,698	-	-	33,698
Emerging markets fund	<u>9,604</u>	<u>-</u>	<u>-</u>	<u>9,604</u>
Subtotal	<u>\$ 157,956</u>	<u>\$ 1,793</u>	<u>\$ -</u>	159,749
Investments measured at net asset value:				
Equity securities:				
Collective funds — fixed income				184,936
Collective funds — US equity				61,059
Collective funds — non-US equity				41,288
Collective funds — global equity				<u>93,043</u>
Total pension plans assets				<u>\$ 540,075</u>
Postretirement plans:				
Cash and cash equivalents	\$ -	\$ 17	\$ -	\$ 17
Mutual funds:				
Fixed-income funds	<u>7,170</u>	<u>-</u>	<u>-</u>	<u>7,170</u>
Subtotal	<u>\$ 7,170</u>	<u>\$ 17</u>	<u>\$ -</u>	7,187
Investments measured at net asset value:				
Equity securities:				
Collective funds — US equity				5,853
Collective funds — global equity				<u>5,831</u>
Total postretirement plans assets				<u>\$ 18,871</u>

Asset Category as of June 30, 2018	Level 1	Level 2	Level 3	Total Fair Value
Pension plans:				
Cash and cash equivalents	\$ -	\$ 11,672	\$ -	\$ 11,672
Mutual funds:				
Fixed-income funds	19,444	-	-	19,444
US equity fund	58,189	-	-	58,189
Non-US equity fund	48,616	-	-	48,616
Emerging markets fund	<u>10,486</u>	<u>-</u>	<u>-</u>	<u>10,486</u>
Subtotal	<u>\$ 136,735</u>	<u>\$ 11,672</u>	<u>\$ -</u>	<u>148,407</u>
Investments measured at net asset value:				
Equity securities:				
Collective funds — fixed income				196,603
Collective funds — US equity				49,388
Collective funds — non-US equity				35,922
Collective funds — global equity				<u>56,831</u>
Total pension plans assets				<u>\$ 487,151</u>
Postretirement plans:				
Cash and cash equivalents	\$ -	\$ 36	\$ -	\$ 36
Mutual funds:				
Fixed-income funds	<u>6,535</u>	<u>-</u>	<u>-</u>	<u>6,535</u>
Subtotal	<u>\$ 6,535</u>	<u>\$ 36</u>	<u>\$ -</u>	<u>6,571</u>
Investments measured at net asset value:				
Equity securities:				
Collective funds — US equity				5,656
Collective funds — global equity				<u>5,119</u>
Total postretirement plans assets				<u>\$ 17,346</u>

As of June 30, 2019 and 2018, there were no security transfers between Levels 1 and 2 and no securities valued using Level 3 unobservable inputs.

Cash Flows

MidMichigan Health's funding policy is to contribute annually, not less than the minimum required by applicable laws and regulations. MidMichigan Health contributed \$36,194 and \$30,737 to its Pension Plans in fiscal 2019 and 2018, respectively. Pension contributions are expected to be \$33,380 in fiscal 2020.

MidMichigan Health expects to pay the following for pension benefits and expected postretirement benefits:

Estimated benefit payments	Pension Plans	Postretirement Healthcare Plans	
		Before Subsidy	Part D Subsidy
2020	\$ 32,633	\$ 672	\$ 38
2021	31,734	690	38
2022	33,038	701	38
2023	33,946	700	38
2024	35,364	695	38
2025 through 2029	195,384	3,100	159

Other Postretirement Benefit Plans

MidMichigan Health maintains a voluntary tax-deferred retirement savings plan, 403(b) plan, covering substantially all of its employees, except West Branch. Under this defined contribution plan, employees may elect to contribute a percentage of their salary, which may be matched with a discretionary employer contribution in accordance with the provisions of the plan. Benefits are based on matching 50% of an employee's contribution up to 4% of covered compensation. For Alpena, only employees hired as of January 1, 2018, are eligible for the employer matching contribution. Matching amounts become 100% vested after three years of service, and employee-elective deferrals are 100% vested from the date of contribution.

MidMichigan Health maintains a 401(a) plan for Alpena employees. MidMichigan Health makes matching contributions in accordance with the provisions of the plan. Additionally, all employees hired prior to January 1, 2018, may make elective contributions to the Plan up to the limits contained in the IRC. Employer and employee contributions are self-directed by plan participants hired prior to January 1, 2018 and cannot be changed once elected. Employer matching amounts become 100% vested after three years of service, and employee-elective deferrals are 100% vested from the date of contribution.

MidMichigan Health maintains a separate 403(b) plan for West Branch Employees. Under this defined contribution plan, employees may elect to contribute a percentage of their salary, which may be matched with a discretionary employer contribution for nonunion employees in accordance with the provisions of the plan. Benefits are based on matching 50% of an employee's contribution up to 4% of covered compensation. Union employees receive a discretionary employer contribution, regardless of whether the employees make an elective contribution. Employer matching contributions and employer discretionary contributions become 100% vested after three years of service, and employee-elective deferrals are 100% vested from the date of contribution. Effective January 1, 2020, the West Branch 403(b) plan will be merged with the MidMichigan Health 403(b) plan.

Employer contributions to the plans were \$7,229 and \$6,710 for the years ended June 30, 2019 and 2018, respectively.

MidMichigan Health also sponsors a nonqualified deferred compensation plan, 457(b) plan that permits eligible employees to defer a portion of their compensation. The deferred amounts are distributable in cash after retirement or termination of employment. As of June 30, 2019 and 2018, the assets under these plans totaled \$27,898 and \$25,895, respectively, and the liabilities totaled \$29,592 and \$28,696, respectively. Although these assets are held in a trust, these assets belong to MidMichigan Health and are subject to the claims of MidMichigan Health's general creditors.

MidMichigan Health also sponsors certain nonqualified supplemental plan arrangements that provide retirement benefits to certain employees, as designated by the compensation committee of the Board of Directors. MidMichigan Health has accrued liabilities for the supplemental plan based on actuarial valuations. The supplemental pension plan is unfunded. Benefits are paid when incurred from operating funds.

It is MidMichigan Health's policy to meet all regulatory requirements, including ERISA, the Pension Protection Act of 2006, and the IRC.

13. COMMITMENTS AND CONTINGENCIES

Professional and General Liability Programs

MidMichigan Health self-insures primary medical, professional, and general liability claims. MidMichigan Health has limited its liability by membership in Caymich Insurance Company, Ltd. (Caymich), which provides excess insurance above the self-insurance limits.

Effective April 1, 2018, coverage limits per claim are \$3 million and \$8 million annual aggregate. Caymich self-insures the next layer, with shared risk among its seven members, and purchases reinsurance above that layer. The first \$20 million reinsured limit is also shared among its seven members, and the remaining \$30 million reinsured limit is MidMichigan Health's unshared limit. The total Caymich limit is \$59 million (\$9 million in the retained layer and \$50 million in the reinsured layers). The total amount available for the subsequent layer was \$65 million (shared with the Caymich members). The same structure and limits were in effect from April 1, 2017, through March 31, 2018, as described above. MidMichigan Health also self-insures \$0.1 million per claim in property damage, with commercial insurance providing coverage up to \$650 million per occurrence. Segregated funds, included in assets limited as to use have been established to settle claims, subject to self-insurance limits of liability.

MidMichigan Health has recorded a liability of \$21,137 and \$16,752 as of June 30, 2019 and 2018, respectively, for known claims and unreported incidents. The discount rate used in calculating the present value of the liability was 3.5% for fiscal years ended June 30, 2019 and 2018. Loss reserves are determined based on assumptions that are reviewed and adjusted as necessary.

MidMichigan Health is subject to various other regulatory investigations, legal proceedings, and claims that are incidental to its normal business activities. Management believes the ultimate disposition of such litigation will not have a material effect on the consolidated financial position of MidMichigan Health. Management also believes that MidMichigan Health is in substantial compliance with current laws and regulations.

Workers' Compensation Self-Insurance Program

MidMichigan Health is a qualified self-insurer within the State of Michigan. MidMichigan Health maintains a trust fund for the payment of claims, which includes provisions for known claims and unreported incidents discounted to their present value at 2.75% as of June 30, 2019 and 2018. Excess commercial insurance was purchased, on a statutory basis, from an unrelated commercial insurer. As of June 30, 2019 and 2018, the amount recorded for MidMichigan Health's self-insured workers' compensation liability was \$2,588 and \$2,480, respectively. Loss reserves are determined based on assumptions that are reviewed and adjusted as necessary.

Obligations under Operating Leases

MidMichigan Health leases certain buildings and equipment under noncancelable operating lease agreements with third parties. Total rental expense for operating leases was approximately \$1,998 and \$1,833 for the years ended June 30, 2019 and 2018, respectively, and was included in purchased services and other in the accompanying consolidated statements of operations and changes in net assets.

Total future minimum payments under these leases as of June 30, 2019, are as follows:

Years Ending June 30	
2020	\$ 1,630
2021	989
2022	574
2023	255
2024	233
Thereafter	<u>2,057</u>
Total	<u>\$ 5,738</u>

14. INVESTMENTS IN JOINT VENTURES

MidMichigan Health maintains investments in several unconsolidated joint ventures, with ownership interests ranging from 16% to 51%. Investments in unconsolidated joint ventures, accounted for on the equity method, totaled \$7,388 and \$7,945 as of June 30, 2019 and 2018, respectively, and are included in investments in joint ventures in the accompanying consolidated balance sheets. Income recognized from these joint ventures, reported in other revenue, was \$441 and \$936 during the years ended June 30, 2019 and 2018, respectively.

The summarized financial information for unconsolidated joint ventures as of June 30, 2019 and 2018, consisted of the following:

	2019	2018
Total assets	\$ 22,682	\$ 23,592
Total liabilities	7,150	7,077
Net assets	15,532	16,515
Net revenues	20,026	17,668
Deficiency of revenue over expenses	(2,095)	(1,741)

15. NET ASSETS

Net assets with donor restrictions were available for the following purposes for the years ended June 30, 2019 and 2018:

	2019	2018
Subject to expenditure for healthcare operations	\$ 32,633	\$ 30,737
Endowments subject to MidMichigan Health's endowment spending policy and appropriation	<u>17,523</u>	<u>16,903</u>
Net assets with donor restrictions	<u>\$ 50,156</u>	<u>\$ 47,640</u>

Changes in consolidated net assets without donor restrictions attributable to MidMichigan Health and the noncontrolling interests for the years ended June 30, 2019 and 2018, are as follows:

	MidMichigan Health	Noncontrolling Interests	Total
Net assets without donor restrictions—June 30, 2017	\$ 683,568	\$ -	\$ 683,568
Excess of revenue over expenses	64,906	-	64,906
Net assets released from restrictions — capital acquisitions	1,850	-	1,850
Change in unrealized investment return	(20,429)	-	(20,429)
Postretirement-related liability adjustments	19,260	-	19,260
Increase in net assets without donor restrictions	65,587	-	65,587
Net assets without donor restrictions—June 30, 2018	749,155	-	749,155
Excess of revenue over expenses	64,252	(26)	64,226
Net assets released from restrictions — capital acquisitions	352	-	352
Net cumulative unrealized gains on equity investments due to adoption of ASU No. 2016-01	145,748	-	145,748
Change in unrealized investment return	(145,748)	-	(145,748)
Contribution from noncontrolling interests	-	49	49
Postretirement-related liability adjustments	(22,407)	-	(22,407)
Increase in net assets without donor restrictions	42,197	23	42,220
Net assets without donor restrictions—June 30, 2019	\$ 791,352	\$ 23	\$ 791,375

16. FUNCTIONAL EXPENSES

MidMichigan Health provides health care services to residents within its geographic location. Expenses by functional classification for the year ended June 30, 2019, were as follows:

	Patient Care	Support Services	Fundraising	Total
Salaries and benefits	\$ 409,228	\$ 85,222	\$ 537	\$ 494,987
Supplies	172,357	7,692	40	180,089
Professional fees and other	67,403	24,365	2	91,770
Purchased services and other	58,547	27,243	239	86,029
Depreciation and amortization	46,115	4,507	-	50,622
Utilities	2,073	9,727	-	11,800
Insurance	3,697	5,573	-	9,270
Interest	8,178	-	-	8,178
	<u>\$ 767,598</u>	<u>\$ 164,329</u>	<u>\$ 818</u>	<u>\$ 932,745</u>

The functional classifications of expenses for the year ended June 30, 2018, were as follows:

	2018
Patient care	\$ 653,975
Support services	159,132
Medicaid hospital assessment	<u>17,414</u>
Total	<u>\$ 830,521</u>

The consolidated financial statements report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is

consistently applied. Information technology expenses are allocated to patient care and support services based on the percent of total expense for each category. Departmental expenses may include allocations of costs based on direct assignment, expenses, or other methods.

17. INFORMATION ABOUT LIQUIDITY

MidMichigan Health manages its cash and pooled income investment funds (pooled income fund) to ensure liquidity across all operating units and to meet all regulatory requirements. The level of cash maintained in bank accounts is based on management's determination of future working capital needs, debt service requirements, capital needs, and other cash outflows of the organization. As needed, either excess funds generated from MidMichigan Health's operations are transferred to external investment managers within the pooled income fund or liquidity needs for general expenditures are sourced from external investment managers. The pooled income fund offers the potential for higher returns consistent with reasonable risk while also ensuring adequate liquidity to meet MidMichigan Health's general expenditures, liabilities, and other obligations as they come due.

As of June 30, 2019, the majority of MidMichigan Health's unrestricted cash and short-term investments was available in five days or less. Of the remainder, availability to receive proceeds ranges from one month or less to one year.

MidMichigan Health considers board-designated assets limited as to use to be available within one year for general expenditure with the exception of those assets designated for self-insurance and long-term employee benefit plans.

MidMichigan Health's financial assets as of June 30, 2019, reduced by amounts not available for general use within one year of the balance sheet date because of donor restrictions or internal designations are as follows:

	<u>2019</u>
Financial assets:	
Cash and cash equivalents	\$ 15,581
Accounts receivable for patient services	86,094
Estimated receivables from third-party payors	10,060
Assets limited as to use	<u>794,168</u>
Total financial assets	905,903
Financial assets not available to be used in one year:	
Subject to donor-imposed restrictions	(50,156)
Designated for self-insurance	(22,659)
Designated for deferred compensation	<u>(27,898)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 805,190</u>

18. UNIVERSITY OF MICHIGAN HEALTH SYSTEM TRANSACTION

On June 21, 2013, the University of Michigan Regents through its operating division, the University of Michigan Health System (UMHS), and Michigan Health Corporation, together with MidMichigan Health, executed an affiliation agreement (the "Agreement"). The Agreement objectives include improvement of the health of our residents, increased access to high-quality service, achievement of significant efficiencies, enhancement of clinical integration, and the furtherance of both MidMichigan Health's and UMHS' missions.

As a result of this transaction and the initial term expiring on June 30, 2017, the following key provisions remain:

- The Michigan Health Corporation member class, consisting of a 12% membership interest in MidMichigan Health;
- The MidMichigan Health member class, consisting of an 88% membership interest in MidMichigan Health;
- The automatic renewal for successive 20-year terms;
- The right to purchase up to an additional 8% interest, which expired on June 30, 2019;
- The continuation of the reserve powers (such as termination, dissolution, and approval of certain capital expenditures in excess of various thresholds); and
- With respect to the financials provisions, the indexing for inflation of the annual distribution amount.

The Agreement includes certain restrictive covenants, including the rights of first refusal related to the provision of clinical care, exclusivity, and noncompetes upon the termination of the Agreement and allows for MidMichigan Health's use of the MidMichigan/UMHS Brand.

The Agreement may be terminated under certain conditions. The termination payments range from MidMichigan Health making an exit payment to UMHS, from \$52 million to \$126 million.

Recognition of Membership Interest of UMHS by MidMichigan Health

MidMichigan Health has concluded that its affiliation with UMHS meets the criteria for classifying the Agreement as a collaborative arrangement. MidMichigan Health has evaluated the consolidated financial statement impact and classification of this collaborative arrangement for the years ended June 30, 2019 and 2018. The impacts on the consolidated balance sheets as of June 30, 2019 and 2018, are as follows:

A long-term asset and a long-term liability of \$3 million were recorded to reflect the value of the option provided by MidMichigan Health to Michigan Health Corporation to purchase up to an additional 8% interest (total interest of 20%) at an agreed-upon 5% discount to MidMichigan Health's fair market value at the time of Michigan Health Corporation's notice of its intent to purchase the additional interest.

For the years ended June 30, 2019 and 2018, the long-term asset continued to be amortized over its remaining seven-year estimated life and the liability remained at \$3 million for both years. Approximately \$0.6 million was recorded in depreciation and amortization in the consolidated statements of operations and changes in net assets to reflect the estimated long-term asset, which at June 30, 2019, was fully amortized. Michigan Health Corporation did not elect to purchase the additional interest and the liability and amortization reversal occurred on July 1, 2019. The annual distribution of \$4.9 million is included in fees in both fiscal 2019 and 2018 in the consolidated statements of operations and changes in net assets.

Related-Party Transactions

As of and for the years ended June 30, 2019 and 2018, the only significant related-party transaction with UMHS is the payment of the annual distribution, \$4.9 million.

In addition to the Agreement, UMHS and Alpena are the sole members of the North East Michigan Cancer Center (NEMCC). NEMCC was formed in 2001 to provide radiation oncology treatment to patients in northeastern Michigan.

19. SUBSEQUENT EVENTS

Management has evaluated subsequent events through October 14, 2019, the date the consolidated financial statements were issued. As a result of this evaluation, MidMichigan Health has no subsequent events to disclose.

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MIDMICHIGAN HEALTH SUPPLEMENTARY CONSOLIDATING INFORMATION

MIDMICHIGAN HEALTH
CONSOLIDATING SCHEDULE - BALANCE SHEET INFORMATION
AS OF JUNE 30, 2019
(Dollars In thousands)

	Midland	Alpena	Gratiot	Clare	Gladwin	West Branch	MPG	Foundation	Tolfree Foundation	MHC	Hospice of Helping Hands, Inc.	MHDA	MCCO	MidMichigan Health Pain Management	MidMichigan Health	Total	Eliminations	Consolidated	
ASSETS																			
CURRENT ASSETS:																			
Cash and cash equivalents	\$ 905	\$ 285	\$ 639	\$ 178	\$ 293	\$ 2,215	\$ 6,832	\$ -	\$ -	\$ 376	\$ -	\$ 2,744	\$ 1,185	\$ 100	\$ (171)	\$ 15,581	\$ -	\$ 15,581	
Accounts receivable for patient services	42,301	13,107	12,667	4,465	2,776	2,644	3,740	-	-	4,388	-	-	-	6	-	86,094	-	86,094	
Estimated receivables from third-party payors	4,070	1,385	1,703	1,297	397	1,208	-	-	-	-	-	-	-	-	-	10,060	-	10,060	
Inventories	6,057	2,321	1,705	716	680	309	-	-	-	-	-	-	-	-	-	11,788	-	11,788	
Prepaid expenses and other current assets	1,808	420	232	321	185	402	378	-	-	107	-	188	128	14	4,143	8,326	(412)	7,914	
Assets limited or restricted as to use — current portion	12,638	-	2,280	369	483	-	-	-	-	-	-	-	-	-	3,500	19,270	-	19,270	
Total current assets	67,779	17,518	19,226	7,346	4,814	6,778	10,950	-	-	4,871	-	2,932	1,313	120	7,472	151,119	(412)	150,707	
ASSETS LIMITED AS TO USE AND INVESTMENTS:																			
Investments — less current portion	100,913	12,597	7,167	7,602	6,240	-	-	-	-	2,282	-	-	-	-	2,633	139,434	-	139,434	
Limited as to use by Board for capital acquisitions	383,551	47,441	25,100	18,386	47,098	11,126	-	-	-	5,551	-	-	-	-	-	538,253	-	538,253	
Self-insurance, deferred compensation, and other	-	53	-	-	-	-	-	-	-	-	-	-	-	-	47,002	47,055	-	47,055	
Limited as to use by donor or time restriction	-	771	-	-	-	-	-	49,385	-	-	-	-	-	-	-	50,156	-	50,156	
Total assets limited as to use and investments	484,464	60,862	32,267	25,988	53,338	11,126	-	49,385	-	7,833	-	-	-	-	49,635	774,898	-	774,898	
PROPERTY AND EQUIPMENT — net	173,145	68,165	43,994	11,154	3,943	36,386	1,096	-	-	1,338	-	57,319	-	-	45,927	442,467	-	442,467	
INVESTMENTS IN SUBSIDIARIES	-	-	-	-	-	24	-	-	-	-	-	-	-	-	-	839,441	839,465	(839,465)	-
INVESTMENTS IN JOINT VENTURES	1,439	2,942	-	-	-	300	-	-	-	-	-	-	-	-	2,707	7,388	-	7,388	
OTHER ASSETS	17,064	545	41	-	-	-	655	-	-	-	-	-	-	-	3,773	22,078	-	22,078	
TOTAL ASSETS	\$ 743,891	\$ 150,032	\$ 95,528	\$ 44,488	\$ 62,095	\$ 54,614	\$ 12,701	\$ 49,385	\$ -	\$ 14,042	\$ -	\$ 60,251	\$ 1,313	\$ 120	\$ 948,955	\$ 2,237,415	\$ (839,877)	\$ 1,397,538	
LIABILITIES AND NET ASSETS																			
CURRENT LIABILITIES:																			
Accounts payable and accrued expenses	\$ 11,357	\$ 2,279	\$ 2,674	\$ 556	\$ 277	\$ 2,283	\$ 1,198	\$ -	\$ -	\$ 729	\$ -	\$ 18	\$ 5	\$ 73	\$ 21,193	\$ 42,642	\$ (412)	\$ 42,230	
Salaries, wages, and payroll-related liabilities	8,931	3,371	2,563	905	565	2,124	10,864	-	-	807	-	-	99	-	28,152	58,381	-	58,381	
Estimated third-party settlements payable	6,652	2,386	3,543	1,212	719	2,592	112	-	-	-	-	-	-	-	-	17,216	-	17,216	
Current portion of long-term debt and capital lease obligations	6,216	-	608	133	137	685	-	-	-	-	-	-	-	-	-	7,779	-	7,779	
Current portion of self-insurance, deferred compensation, and other liabilities	-	274	-	-	-	-	-	-	-	210	-	-	-	-	3,500	3,984	-	3,984	
Total current liabilities	33,156	8,310	9,388	2,806	1,698	7,684	12,174	-	-	1,746	-	18	104	73	52,845	130,002	(412)	129,590	
LONG-TERM LIABILITIES:																			
Self-insurance, deferred compensation, and other liabilities — less current portion	17,565	7,026	4,891	1,725	1,381	4,648	976	-	-	359	-	25	139	-	55,769	94,504	-	94,504	
Accrued pension and postretirement benefits	-	59,228	-	-	-	15,411	-	-	-	-	-	-	-	-	48,218	122,857	-	122,857	
Long-term debt and capital lease obligations — less current portion	153,284	-	33,152	4,433	7,483	10,704	-	-	-	-	-	-	-	-	-	209,056	-	209,056	
Total long-term liabilities	170,849	66,254	38,043	6,158	8,864	30,763	976	-	-	359	-	25	139	-	103,987	426,417	-	426,417	
Total liabilities	204,005	74,564	47,431	8,964	10,562	38,447	13,150	-	-	2,105	-	43	243	73	156,832	556,419	(412)	556,007	
NET ASSETS:																			
Without donor restrictions:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
MidMichigan Health	539,886	74,697	48,097	35,524	51,533	16,144	(449)	-	-	11,937	-	60,208	1,070	47	792,123	1,630,817	(839,465)	791,352	
Noncontrolling interests	-	-	-	-	-	23	-	-	-	-	-	-	-	-	-	23	-	23	
Total net assets without donor restrictions	539,886	74,697	48,097	35,524	51,533	16,167	(449)	-	-	11,937	-	60,208	1,070	47	792,123	1,630,840	(839,465)	791,375	
With donor restrictions	-	771	-	-	-	-	-	49,385	-	-	-	-	-	-	-	50,156	-	50,156	
Total net assets	539,886	75,468	48,097	35,524	51,533	16,167	(449)	49,385	-	11,937	-	60,208	1,070	47	792,123	1,680,996	(839,465)	841,531	
TOTAL LIABILITIES AND NET ASSETS	\$ 743,891	\$ 150,032	\$ 95,528	\$ 44,488	\$ 62,095	\$ 54,614	\$ 12,701	\$ 49,385	\$ -	\$ 14,042	\$ -	\$ 60,251	\$ 1,313	\$ 120	\$ 948,955	\$ 2,237,415	\$ (839,877)	\$ 1,397,538	

MIDMICHIGAN HEALTH
CONSOLIDATING SCHEDULE - STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS INFORMATION
FOR THE YEAR ENDED JUNE 30, 2019
(Dollars in thousands)

	Midland	Alpena	Gratiot	Clare	Gladwin	West Branch	MPG	Foundation	Tolfree Foundation	MHC	Hospice of Helping Hands, Inc.	MHDA	MCCO	MidMichigan Health Pain Management	MidMichigan Health	Total	Eliminations	Consolidated
REVENUE:																		
Net patient service revenue	\$ 455,138	\$ 140,529	\$ 127,393	\$ 56,312	\$ 30,947	\$ 49,179	\$ 44,218	\$ -	\$ -	\$ 23,613	\$ 816	\$ -	\$ -	\$ 20	\$ -	\$ 928,165	\$ -	\$ 928,165
Other revenue	21,731	4,194	4,340	691	181	1,082	80,252	1,593	4	192	-	6,439	1,893	-	61,257	183,849	(152,895)	30,954
Total revenue	476,869	144,723	131,733	57,003	31,128	50,261	124,470	1,593	4	23,805	816	6,439	1,893	20	61,257	1,112,014	(152,895)	959,119
EXPENSES:																		
Salaries and wages	123,506	46,420	36,996	14,527	8,808	16,316	110,675	-	43	10,913	401	66	638	35	32,684	402,028	-	402,028
Employee benefits	29,579	15,011	9,331	3,882	2,166	5,548	16,501	-	9	2,751	89	21	158	12	7,901	92,959	-	92,959
Supplies	89,276	32,723	19,875	7,257	3,987	14,361	5,621	-	5	6,404	84	17	2	20	457	180,089	-	180,089
Professional fees and other	35,900	13,059	14,208	4,412	3,177	9,200	1,246	-	117	258	56	85	144	2	9,906	91,770	-	91,770
Purchased services and other	65,098	13,355	28,336	11,624	6,450	3,948	16,606	1,593	75	3,434	509	1,226	858	4	20,681	173,797	(87,768)	86,029
Depreciation and amortization	19,289	5,271	5,616	1,391	830	2,994	635	-	-	175	1	4,706	-	-	9,714	50,622	-	50,622
Utilities	4,701	1,434	1,925	642	386	1,036	1,288	-	-	228	13	70	-	-	77	11,800	-	11,800
Insurance	3,527	1,861	1,184	369	242	246	1,610	-	-	152	16	63	-	-	-	9,270	-	9,270
Interest	5,978	-	1,340	180	301	379	-	-	-	-	-	-	-	-	-	8,178	-	8,178
Physician practice investment	43,335	115	9,020	8,076	4,581	-	-	-	-	-	-	-	-	-	-	65,127	(65,127)	-
Total expenses	420,189	129,249	127,831	52,360	30,928	54,028	154,182	1,593	249	24,315	1,169	6,254	1,800	73	81,420	1,085,640	(152,895)	932,745
OPERATING INCOME (LOSS) — BEFORE OTHER ITEMS	56,680	15,474	3,902	4,643	200	(3,767)	(29,712)	-	(245)	(510)	(353)	185	93	(53)	(20,163)	26,374	-	26,374
OTHER ITEMS:																		
Postretirement settlement	-	1,325	-	-	-	-	-	-	-	-	-	-	-	-	-	1,325	-	1,325
Total other items	-	1,325	-	-	-	-	-	-	-	-	-	-	-	-	-	1,325	-	1,325
OPERATING INCOME (LOSS)	56,680	16,799	3,902	4,643	200	(3,767)	(29,712)	-	(245)	(510)	(353)	185	93	(53)	(20,163)	27,699	-	27,699
NONOPERATING INCOME:																		
Investment income	25,566	2,937	1,887	1,392	2,736	982	23	-	(127)	355	62	-	-	-	1,950	37,763	-	37,763
Purchase accounting adjustment	-	-	-	-	-	(1,236)	-	-	-	-	-	-	-	-	-	(1,236)	-	(1,236)
Total nonoperating income	25,566	2,937	1,887	1,392	2,736	(254)	23	-	(127)	355	62	-	-	-	1,950	36,527	-	36,527
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	82,246	19,736	5,789	6,035	2,936	(4,021)	(29,689)	-	(372)	(155)	(291)	185	93	(53)	(18,213)	64,226	-	64,226
DEFICIT OF REVENUE OVER EXPENSES ATTRIBUTABLE TO NONCONTROLLING INTERESTS	-	-	-	-	-	(26)	-	-	-	-	-	-	-	-	-	(26)	-	(26)
EXCESS OF REVENUE OVER EXPENSES - NET OF NONCONTROLLING INTERESTS	\$ 82,246	\$ 19,736	\$ 5,789	\$ 6,035	\$ 2,936	\$ (3,995)	\$ (29,689)	\$ -	\$ (372)	\$ (155)	\$ (291)	\$ 185	\$ 93	\$ (53)	\$ (18,213)	\$ 64,252	\$ -	\$ 64,252

(Continued)

MIDMICHIGAN HEALTH
CONSOLIDATING SCHEDULE - STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS INFORMATION
FOR THE YEAR ENDED JUNE 30, 2019
(Dollars In thousands)

	Midland	Alpena	Gratiot	Clare	Gladwin	West Branch	MPG	Foundation	Tolfree Foundation	MHC	Hospice of Helping Hands, Inc.	MHDA	MCCO	MidMichigan Health Pain Management	MidMichigan Health	Total	Eliminations	Consolidated
NET ASSETS WITHOUT DONOR RESTRICTIONS:																		
Excess (deficiency) of revenue over expenses	\$ 82,246	\$ 19,736	\$ 5,789	\$ 6,035	\$ 2,936	\$ (4,021)	\$ (29,689)	\$ -	\$ (372)	\$ (155)	\$ (291)	\$ 185	\$ 93	\$ (53)	\$ (18,213)	\$ 64,226	\$ -	\$ 64,226
Net assets released from restrictions — capital acquisitions	-	-	-	-	-	-	-	352	-	-	-	-	-	-	-	352	-	352
Net cumulative unrealized gains on equity investments due to adoption of ASU No. 2016-01	92,901	9,202	5,486	4,708	10,734	-	-	7,659	-	1,347	-	-	-	-	13,711	145,748	-	145,748
Change in unrealized investment return	(92,901)	(9,202)	(5,486)	(4,708)	(10,734)	-	-	(7,659)	-	(1,347)	-	-	-	-	(13,711)	(145,748)	-	(145,748)
Equity earnings from subsidiaries	-	-	-	-	-	(27)	-	-	-	-	-	-	-	-	62,872	62,845	(62,845)	-
Contributions from noncontrolling interests	-	-	-	-	-	-	-	-	-	-	-	-	-	49	-	49	-	49
Transfers to/from subsidiaries	(20,619)	(2,971)	(3,745)	(3,963)	(1,000)	9,127	29,204	(352)	352	10	-	3,435	-	51	-	9,529	(9,529)	-
Postretirement-related liability adjustments	601	(15,990)	-	-	-	(3,287)	-	-	-	-	-	-	-	-	(3,731)	(22,407)	-	(22,407)
Increase (decrease) in net assets without donor restrictions	<u>62,228</u>	<u>775</u>	<u>2,044</u>	<u>2,072</u>	<u>1,936</u>	<u>1,792</u>	<u>(485)</u>	<u>-</u>	<u>(20)</u>	<u>(145)</u>	<u>(291)</u>	<u>3,620</u>	<u>93</u>	<u>47</u>	<u>40,928</u>	<u>114,594</u>	<u>(72,374)</u>	<u>42,220</u>
NET ASSETS WITH DONOR RESTRICTIONS:																		
Pledges, contributions, grants, and interest income	-	-	-	-	-	-	-	5,862	(1,265)	-	-	-	-	-	-	4,597	-	4,597
Net assets released from restrictions	-	-	-	-	-	-	-	(1,946)	(4)	-	-	-	-	-	-	(1,950)	-	(1,950)
Investment losses	-	-	-	-	-	-	-	(131)	-	-	-	-	-	-	-	(131)	-	(131)
Increase (decrease) in net assets with donor restrictions	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,785</u>	<u>(1,269)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,516</u>	<u>-</u>	<u>2,516</u>
INCREASE (DECREASE) IN NET ASSETS	62,228	775	2,044	2,072	1,936	1,792	(485)	3,785	(1,289)	(145)	(291)	3,620	93	47	40,928	117,110	(72,374)	44,736
NET ASSETS — Beginning of year	477,658	74,693	46,053	33,452	49,597	14,375	36	45,600	1,289	12,082	291	56,588	977	-	751,195	1,563,886	(767,091)	796,795
NET ASSETS — End of year	\$ 539,886	\$ 75,468	\$ 48,097	\$ 35,524	\$ 51,533	\$ 16,167	\$ (449)	\$ 49,385	\$ -	\$ 11,937	\$ -	\$ 60,208	\$ 1,070	\$ 47	\$ 792,123	\$ 1,680,996	\$ (839,465)	\$ 841,531

(Concluded)