



**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Consolidated Financial Statements and Schedules

September 30, 2019 and 2018

(With Independent Auditors' Report Thereon)



KPMG LLP  
Suite 1100  
One Jackson Place  
188 East Capitol Street  
Jackson, MS 39201-2127

## Independent Auditors' Report

The Board of Directors  
North Mississippi Health Services, Inc.:

We have audited the accompanying consolidated financial statements of North Mississippi Health Services, Inc. and its subsidiaries (the System), which comprise the consolidated balance sheets as of September 30, 2019 and 2018, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### *Management's Responsibility for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free 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 audits 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 auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of North Mississippi Health Services, Inc. and its subsidiaries as of September 30, 2019 and 2018, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.



*Emphasis of Matter*

As discussed in note 1(t) to the consolidated financial statements, in fiscal year 2019, the System adopted new accounting guidance in connection with its implementation of Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (Topic 606), and FASB ASU No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities* (Topic 958). Our opinion is not modified with respect to this matter.

*Other Matter*

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The information included in schedules 1 and 2 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Jackson, Mississippi  
December 20, 2019

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Consolidated Balance Sheets

September 30, 2019 and 2018

(In thousands)

Assets	2019	2018
Current assets:		
Cash and cash equivalents	\$ 67,548	32,249
Investments	601,214	608,392
Net patient accounts receivable	96,344	148,628
Other current assets	44,282	38,896
Total current assets	809,388	828,165
Assets limited as to use	97,223	92,745
Property and equipment, net	256,097	260,995
Other assets	56,662	50,914
Total assets	\$ 1,219,370	1,232,819
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable	\$ 51,091	50,270
Accrued expenses and other current liabilities	90,327	91,552
Current installments of long-term debt	73,482	77,685
Total current liabilities	214,900	219,507
Estimated professional and general liability costs	17,792	18,287
Long-term debt, excluding current installments	83,819	77,987
Fair value of interest rate swaps	6,405	3,710
Accrued pension cost	113,294	73,258
Other long-term liability	1,249	—
Total liabilities	437,459	392,749
Net assets:		
Without donor restrictions	775,822	833,944
With donor restrictions	3,223	3,188
Total net assets attributable to North Mississippi Health Services, Inc.	779,045	837,132
Noncontrolling interests	2,866	2,938
Total net assets	781,911	840,070
Commitments and contingencies		
Total liabilities and net assets	\$ 1,219,370	1,232,819

See accompanying notes to consolidated financial statements.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Consolidated Statements of Operations

Years ended September 30, 2019 and 2018

(In thousands)

	<u>2019</u>	<u>2018</u>
Operating revenue:		
Net patient service revenue	957,004	910,119
Other revenue	23,422	29,159
Total operating revenue	<u>980,426</u>	<u>939,278</u>
Operating expenses:		
Salaries and employee benefits	516,166	504,246
Supplies and other	393,401	366,571
Interest	4,671	4,641
Depreciation and amortization	48,004	48,212
Total operating expenses	<u>962,242</u>	<u>923,670</u>
Operating income before electronic medical record costs	18,184	15,608
Electronic medical records implementation costs	4,267	—
Operating income	13,917	15,608
Nonoperating gains:		
Investment return	23,546	8,170
Other nonoperating gains	908	5,089
Total nonoperating gains, net	24,454	13,259
Revenue, gains, and other support in excess of expenses and losses, before noncontrolling interests	38,371	28,867
Noncontrolling interests	<u>(4,680)</u>	<u>(3,766)</u>
Revenue, gains, and other support in excess of expenses and losses attributable to North Mississippi Health Services, Inc.	33,691	25,101
Other changes in net assets without donor restrictions:		
Pension-related changes other than net periodic pension cost	(50,407)	38,226
Cumulative effect of adopting new accounting guidance	(41,486)	—
Other	80	109
Change in net assets without donor restrictions	<u>\$ (58,122)</u>	<u>63,436</u>

See accompanying notes to consolidated financial statements.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Consolidated Statements of Changes in Net Assets

Years ended September 30, 2019 and 2018

(In thousands)

	<u>Net assets without donor restrictions</u>	<u>Net assets with donor restrictions</u>	<u>Noncontrolling interests</u>	<u>Total</u>
Balances at September 30, 2017	\$ 770,508	3,037	3,951	777,496
Revenue, gains, and other support in excess of expenses and losses	25,101	—	3,766	28,867
Distributions to noncontrolling interests	—	—	(4,779)	(4,779)
Pension-related changes other than net periodic pension cost	38,226	—	—	38,226
Other	109	—	—	109
Increase in interest in net assets of affiliated foundation	—	151	—	151
Change in net assets	<u>63,436</u>	<u>151</u>	<u>(1,013)</u>	<u>62,574</u>
Balances at September 30, 2018	<u>833,944</u>	<u>3,188</u>	<u>2,938</u>	<u>840,070</u>
Revenue, gains, and other support in excess of expenses and losses	33,691	—	4,680	38,371
Distributions to noncontrolling interests	—	—	(4,752)	(4,752)
Pension-related changes other than net periodic pension cost	(50,407)	—	—	(50,407)
Other	80	—	—	80
Cumulative effect of adopting new accounting guidance	(41,486)	—	—	(41,486)
Increase in interest in net assets of affiliated foundation	—	35	—	35
Change in net assets	<u>(58,122)</u>	<u>35</u>	<u>(72)</u>	<u>(58,159)</u>
Balances at September 30, 2019	\$ <u>775,822</u>	<u>3,223</u>	<u>2,866</u>	<u>781,911</u>

See accompanying notes to consolidated financial statements.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Consolidated Statements of Cash Flows

Years ended September 30, 2019 and 2018

(In thousands)

	<u>2019</u>	<u>2018</u>
Cash flows from operating activities:		
Change in net assets	\$ (58,159)	62,574
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Unrealized and realized investment losses (gains), net	(10,172)	3,660
Amortization of net premium/discount on bond issue	(3)	8
Change in fair value of interest rate swaps	2,695	(1,953)
Increase in interest in net assets of affiliated foundation	(35)	(151)
Pension-related changes other than net periodic pension cost	50,407	(38,226)
Equity in net income of equity investees	(3,321)	(1,128)
Depreciation and amortization	48,004	48,212
Distributions to noncontrolling interests	4,752	4,779
Loss on disposal of assets	(24)	(307)
Cumulative effect of adopting new accounting guidance	41,486	—
Changes in operating assets and liabilities, net of acquisition:		
Net patient accounts receivable	10,798	12,889
Other current assets	(4,040)	(7,125)
Other assets	(1,182)	(2,874)
Accrued pension cost	(10,371)	(5,380)
Accounts payable, accrued expenses, and other current liabilities	7,103	17,913
Estimated professional and general liability costs	(495)	(537)
Net cash provided by operating activities	<u>77,443</u>	<u>92,354</u>
Cash flows from investing activities:		
Capital expenditures	(36,923)	(33,397)
Sales of investments and assets limited as to use	1,384,790	798,471
Purchases of investments and assets limited as to use	(1,371,918)	(858,595)
Proceeds from sale of assets	102	519
Acquisition of Amory Regional Medical Center, Inc.	(14,692)	—
Net cash used in investing activities	<u>(38,641)</u>	<u>(93,002)</u>
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	6,194	6,707
Proceeds from line of credit	1,100	1,350
Repayment of line of credit	(1,350)	(450)
Repayment of long-term debt	(4,110)	(3,930)
Payment on other long-term liability	—	(2,239)
Repayment of capital lease obligations	(585)	(428)
Distributions to noncontrolling interests	(4,752)	(4,779)
Net cash used in financing activities	<u>(3,503)</u>	<u>(3,769)</u>
Net increase (decrease) in cash and cash equivalents	35,299	(4,417)
Cash and cash equivalents, beginning of year	<u>32,249</u>	<u>36,666</u>
Cash and cash equivalents, end of year	\$ <u>67,548</u>	\$ <u>32,249</u>
Supplemental disclosures of cash flow information:		
Noncash additions to property, plant, and equipment	\$ 1,853	8,059

See accompanying notes to consolidated financial statements.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

### (1) Summary of Significant Accounting Policies

North Mississippi Health Services, Inc. and its subsidiaries (the System) is a not-for-profit, nonstock, multidimensional provider of healthcare services with corporate headquarters located in Tupelo, Mississippi. The significant accounting policies used by the System in preparing and presenting its consolidated financial statements follow:

#### (a) Principles of Consolidation

The consolidated financial statements include the accounts of the System and its controlled subsidiaries. The following corporations are the more significant of the System's subsidiaries:

- North Mississippi Medical Center, Inc. (NMMC), a tertiary care hospital complex in Tupelo
- Corporations that operate acute care hospital facilities of various sizes in West Point, Iuka, Pontotoc, Amory and Eupora, Mississippi, and Hamilton, Alabama
- North Mississippi Medical Clinics, Inc. (NMMCI), which operates 34 clinics
- Tupelo Service Finance, Inc. (TSF), a collection agency for not-for-profit and charitable institutions
- Acclaim, Inc., which provides healthcare claims processing, claims payment and utilization management services
- North Mississippi Joint Ventures, LLC (NMJV), which serves as a holding company for the System's interests in North Mississippi Ambulatory Surgery Center, LLC (ASC); Medical Imaging, LLC (MI); and Center for Digestive Health, LLC (CDH). All of the listed ventures are consolidated subsidiaries of NMJV. NMJV is the 51% controlling investor of ASC and CDH and the 72% controlling investor of MI.

All significant intercompany accounts and transactions have been eliminated in consolidation.

#### (b) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires that management make estimates and assumptions affecting the reported amounts of assets, liabilities, revenue, and expenses, as well as disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

Significant items subject to such estimates and assumptions include the determination of the allowances for implicit and explicit price concessions, liabilities for general and professional liability claims, liabilities for workers' compensation claims, liabilities for employee healthcare claims, estimated third-party payor settlements, and the actuarially determined accrued pension cost related to the System's pension plan. In particular, laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates related to these programs will change by a material amount in the near-term.

#### (c) Cash Equivalents

The System considers investments in highly liquid debt instruments with an original maturity of three months or less to be cash equivalents.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

### **(d) Investments and Investment Income**

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheets.

The System also has investments in alternative funds, which represent investments in hedge funds through fund-of-funds structures generally organized as corporations. The System's investments in alternative funds are recorded at net asset value (NAV) as a practical expedient to fair value. The estimated fair value of these alternative funds is based on the most recent valuations by external investment managers. The System reviews and evaluates the values provided by the managers and the valuation methods and assumptions used to determine those values. Therefore, the System believes the carrying amount of these financial instruments is a reasonable estimate of fair value. Because these assets are not readily marketable, their estimated fair value is subject to uncertainty and, therefore, may differ from the fair value that would have been used had a ready market for such investments existed.

All investment income or loss (including realized and unrealized gains and losses, interest, and dividends) is included in the determination of revenue, gains, and other support in excess of expenses and losses, unless restricted by the donor. The System considers all of its investments to be trading securities.

Investment income from assets that are held by trustees is reported as other revenue. Investment income or loss from investments is reported as nonoperating gains or losses.

### **(e) Equity Investments**

Investments in jointly owned companies in which the System exercises significant influence are accounted for using the equity method.

### **(f) Inventories**

Inventories, consisting primarily of medical supplies and pharmaceuticals, are stated at the lower of cost (first-in, first-out method) or net realizable value.

### **(g) Assets Limited as to Use**

Assets limited as to use include assets set aside by the board of directors for future capital improvements, over which the board retains control and may at its discretion subsequently use for other purposes, and assets held by trustees under indenture and self-insurance funding agreements. Trusteed amounts required to meet current liabilities are classified as current assets.

### **(h) Costs of Borrowing**

Bond issuance costs and bond premiums and discounts are being amortized over the terms of the related bond issues using the effective interest method.

Bond issuance costs related to recognized debt liabilities are presented in the accompanying consolidated balance sheets as a direct deduction from the carrying amount of that debt liability.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The System capitalizes interest costs on qualified construction expenditures, net of income earned on related trusteed assets as a component of the cost of related projects.

#### **(i) Property and Equipment**

Property and equipment are stated at cost at the date of acquisition or fair value at the date of donation. Provisions for depreciation are computed using the straight-line method based on the estimated useful lives of the assets.

Gifts of long-lived assets, such as land, buildings, or equipment are reported as support without donor restrictions, unless explicit donor stipulations specify how the donated assets must be used, and are excluded from revenue, gains, and other support in excess of expenses and losses. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used, and gifts of cash or other assets that must be used to acquire long-lived assets, are reported as support with donor restrictions. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed into service. Contributions restricted to the purchase of property and equipment for which restrictions are met within the same year as received are reported as increases in net assets without donor restrictions in the accompanying consolidated financial statements.

#### **(j) Impairment of Long-lived Assets**

Long-lived assets, such as property and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the use and eventual disposal of the asset, excluding interest. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized to the extent the carrying amount of the asset exceeds its fair value. Assets to be disposed of are separately presented in the consolidated balance sheets and reported at the lower of the carrying amount or fair value less costs to sell and are no longer depreciated. The assets and liabilities of a disposal group classified as held-for-sale are presented separately in the asset and liability sections of the consolidated balance sheets.

No impairment adjustments were necessary in 2019 or 2018.

In addition to consideration of impairment upon the events or changes in circumstances described above, management regularly evaluates the remaining lives of its long-lived assets. If estimates are revised, the carrying value of affected assets is depreciated or amortized over remaining lives.

#### **(k) Derivative Instruments and Hedging Activities**

The System applies Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 815, *Derivatives and Hedging*, which requires that all derivative instruments be recorded on the consolidated balance sheets at their respective fair values.

All of the System's interest rate swaps are carried in the System's consolidated balance sheets at fair value, with related changes in fair value included in nonoperating gains or losses in the consolidated statements of operations. The System does not apply hedge accounting with respect to any of its derivatives.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

### **(l) Consolidated Statements of Operations**

For purposes of presentation, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenue and expenses. Peripheral or incidental transactions are reported as nonoperating gains and losses.

### **(m) Revenue, Gains, and Other Support in Excess of Expenses and Losses**

The consolidated statements of operations include revenue, gains, and other support in excess of expenses and losses. Changes in net assets without donor restrictions which are excluded from revenue, gains, and other support in excess of expenses and losses, consistent with relevant accounting literature, include pension-related changes other than net periodic pension cost and adjustments that may from, time to time, be required to apply new accounting standards.

### **(n) Net Patient Service Revenue and Accounts Receivable**

Net patient service revenue is reported at the amount that reflects the consideration to which the System expects to be entitled for providing patient care. These amounts are due from patients, third-party payors, and others and include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. Generally, the System bills the patients and third-party payors several days after the services are performed or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services provided by the System. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. The System believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients receiving inpatient acute care services or patients receiving services in outpatient centers. The System measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge or completion of outpatient services. Revenue for performance obligations satisfied at a point in time is generally recognized when goods are provided and the System does not believe it is required to provide additional goods or services related to that sale.

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

## **NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The System has agreements with third-party payors that generally provide for payments to the System at amounts different from its established rates. For uninsured patients who do not qualify for charity care, the System recognizes revenue based on established rates, subject to certain discounts and implicit price concessions as determined by the System.

The System is utilizing the portfolio approach practical expedient in ASC Topic 606 for contracts related to net patient service revenue. The System accounts for the contracts within each portfolio as a collective group rather than individual contracts based on the payment pattern expected in each portfolio category and the similar nature and characteristics of the patients within each portfolio. The portfolios consist of major payor classes for inpatient revenue and outpatient revenue. Based on historical collection trends and other analyses, the System has concluded that revenue for a given portfolio would not be materially different than if accounting for revenue on a contract by contract basis.

The System determines the transaction price based on standard charges for goods and services provided, reduced by explicit price concessions provided to third-party payors, discounts provided to uninsured patients in accordance with the System's policy, and implicit price concessions provided to uninsured patients. Explicit price concessions are based on contractual agreements, discount policies, and historical experience. Implicit price concessions represent differences between amounts billed and the estimated consideration the System expects to receive from patients, which are determined based on historical collection experience by payor class, current market conditions, and other factors.

Consistent with the System's mission, care is provided to patients regardless of their ability to pay. Therefore, the System has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (e.g., co-pays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts the System expects to collect based on its collection history with those patients.

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

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. The System also provides services to uninsured patients and offers those uninsured patients a discount, either by policy or law, from standard charges. The System estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. For the year ended September 30, 2019, additional revenue recognized due to changes in its estimates of implicit price concessions, discounts, and contractual adjustments for performance obligations satisfied in prior years was not material. The additional revenue primarily represents patient account recoveries that were previously written off as uncollectible. 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.

#### **(o) Charity Care**

The System provides services to patients who meet the criteria of its charity care policy without charge or at amounts less than its established rates. The criteria for charity care considers household income in relation to the federal poverty guidelines and the equity value of real property assets. The System provides qualifying services without charge for patients with adjusted gross income equal to or less than 100% of the poverty guidelines. If the patient's household income exceeds 100% of the poverty guidelines, the patient may still receive charity care services under the System's catastrophic medical policies.

The System maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy.

#### **(p) Income Taxes**

The System and most of its subsidiaries qualify as tax-exempt under Internal Revenue Code (IRC) Section 501(a) as organizations described in IRC Section 501(c)(3), and their income is generally not subject to federal or state income taxes. Three of the System's subsidiaries are subject to such income taxes, which have been recognized in the accompanying consolidated financial statements. The amount of income tax expense is not significant.

The System applies FASB ASC Topic 740, *Income Taxes*, which clarifies the accounting for uncertainty in income tax positions and provides guidance on when tax positions are recognized in an entity's financial statements and how the values of these positions are determined. There has been no impact on the System's consolidated financial statements as a result of applying Topic 740.

#### **(q) Components of Net Assets**

Net assets, revenue, and other support and expenses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the System and changes therein are classified and reported as follows:

*Net assets without donor restrictions* – Net assets that are not subject to donor-imposed stipulations

*Net assets with donor restrictions* – Net assets subject to donor-imposed stipulations that are available for use either by the passage of time or for specific purposes; certain of these net assets are subject to donor-imposed stipulations that they be maintained permanently by the System. Generally, the donors of these assets permit the System to use all or part of the income earned on related investment for general or specific purposes.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

Revenue is reported as increases in net assets without donor restrictions, unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in net assets without donor restrictions. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in net assets without donor restrictions, unless their use is restricted by explicit donor stipulation or by law. Expirations of donor restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications from net assets with donor restrictions to net assets without donor restrictions. Donor-restricted contributions, whose restrictions are met in the same reporting period as the contributions are recorded, are reported as increases in net assets without donor restrictions.

The System applies the provisions of FASB ASC Subtopic 958-205, *Classification of Donor-Restricted Endowment Funds Subject to the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA)*. Subtopic 958-205 provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of UPMIFA. The State of Mississippi enacted a version of UPMIFA effective July 1, 2012.

#### **(r) Pension Accounting Standard**

The System applies the recognition and disclosure provisions of FASB ASC Subtopic 715-20, *Defined Benefit Plans*. Subtopic 715-20 requires (among other things) that a plan sponsor recognize the unfunded status of its defined benefit pension plan on its consolidated balance sheet. The System measures the plan at September 30 each year.

Subtopic 715-20 requires enhanced disclosures related to pension plan assets, including disclosures related to the fair value of plan assets. These enhanced disclosures are included in these consolidated financial statements.

#### **(s) Fair Value Measurement**

The System applies FASB ASC Topic 820, *Fair Value Measurement*, which establishes an enhanced framework for measuring fair value and expands disclosures about fair value measurements.

#### **(t) Recent Accounting Pronouncements**

In June 2018, the FASB issued ASU No. 2018-08: *Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made* (ASU 2018-08). ASU 2018-08 requires an entity to evaluate whether transactions should be accounted for as contributions (nonreciprocal transactions) within the scope of Topic 958 or as exchange (reciprocal) transactions subject to other guidance. Additionally, an entity must determine whether a contribution is conditional and the related impact on revenue recognition. The new standard is effective for annual reporting periods beginning after June 15, 2018 for contributions received and after December 15, 2018 for contributions made, with early adoption permitted. The System adopted the new standard for contributions received on its consolidated financial statements effective October 1, 2018 using a modified approach. The adoption of ASU 2018-08 did not have a material impact on the System's consolidated financial statements. The System plans to adopt ASU 2018-08 for contributions made as of its fiscal year beginning October 1, 2019. The System does not expect ASU 2018-08 to have a material impact on the consolidated financial statements.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

In May 2014, the FASB issued Topic 606, *Revenue from Contracts with Customers*. ASC Topic 606 outlines a single comprehensive model for recognizing revenue as performance obligations, defined in a contract with a customer as goods or services transferred to the customer in exchange for consideration, are satisfied. As a result, amounts previously classified as the provision for bad debts in the consolidated statement of operations are now reflected as implicit price concessions and therefore included as a reduction to net patient services revenue. For the years ended September 30, 2019 and 2018, the System recorded approximately \$142,065,000 and \$122,511,000, respectively, of implicit price concessions as a direct reduction of patient service revenue that would have been recorded as provision for bad debt prior to the adoption of ASC Topic 606. For the years ended September 30, 2019 and 2018, the System recorded approximately \$173,228,000 and \$199,186,000, respectively, as a direct reduction of patient accounts receivable that would have been reflected as allowance for uncollectible accounts prior to the adoption of ASC Topic 606. Topic 606 also requires expanded disclosures regarding the System's revenue recognition policies and significant judgments employed in the determination of revenue. The System adopted ASC Topic 606 with a modified retrospective approach in 2019, which resulted in a \$41,486,000 decrease to net assets without donor restrictions reflected as the cumulative effect of new accounting guidance in the 2019 consolidated statement of operations.

In August 2016, the FASB issued ASU No 2016-14, *Presentation of Financial Statements of Non-for-Profit Entities*. ASU No. 2016-14 (1) reduces the number of net asset classes presented from three to two, (2) requires the presentation of expenses by functional and natural classification in one location, and (3) requires quantitative and qualitative disclosures about liquidity and availability of financial assets. The ASU is effective for annual financial statements issued for fiscal years beginning after December 15, 2017. The System implemented the provisions of ASU No. 2016-14 effective October 1, 2018 and has included the required disclosures in notes 18 and 19. Prior to the adoption of ASU No. 2016-14, the System previously presented \$3,167,000 and \$21,000 as temporarily and permanently restricted net assets, respectively, for the year ended September 30, 2018. Upon adoption of ASU No. 2016-14, the System presents these items as with donor restrictions in the consolidated financial statements. The System's implementation of the ASU did not have a material impact on its consolidated financial statements.

The FASB issued ASU No. 2016-02, *Leases (Topic 842)*, in February 2016, which supersedes FASB ASC Topic 840, *Leases*, and makes other conforming amendments to U.S. GAAP. ASU No 2016-02 requires, among other changes to the lease accounting guidance, lessees to recognize most leases on its balance sheet through both a right-of-use asset and a corresponding lease obligation liability and additional qualitative and quantitative disclosures. Early adoption is permitted and ASU No 2016-02 mandates a modified retrospective transition method. Management plans to adopt the provisions of ASU No 2016-02 in its fiscal year 2020. The System does not expect ASU No. 2016-02 to have a material impact on the 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 – a consensus of the FASB Emerging Issues Task Force*. ASU No 2016-15 amends ASC Topic 230, *Statement of Cash Flows*, to add or clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows with the intent of reducing diversity in practice with respect to eight types of cash flows. ASU No 2016-15 is effective for fiscal years beginning after December 15, 2018 and interim periods within

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

fiscal years beginning after December 15, 2019. Early adoption is permitted, and entities must apply the guidance retrospectively to all periods presented. The System plans to adopt ASU No 2016-15 for its fiscal year beginning October 1, 2019. The System does not expect ASU No. 2016-15 to have a material impact on the consolidated financial statements.

In November 2016, the FASB issued ASU No 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*, which requires companies to present amounts generally described as restricted cash and restricted cash equivalents in cash and cash equivalents on the statement of cash flows. ASU No 2016-18 is effective for annual periods in fiscal years beginning after December 15, 2018 and requires retrospective application. The System plans to adopt ASU No. 2016-18 for its fiscal year beginning October 1, 2019. The System does not expect ASU No. 2016-18 to have a material impact in the consolidated financial statements.

In March 2017, the FASB issued ASU No 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, which requires companies to present the service cost component of net benefit cost in the income statement line items where they report compensation cost, and all other components of net benefit cost in the income statement separately from the service cost component and outside of operating income, if this subtotal is presented. Additionally, the service cost component will be the only component that can be capitalized. ASU No 2017-07 is effective in annual periods in fiscal years beginning after December 15, 2018. The standard requires retrospective application for the amendments related to the presentation of the service cost component and other components of net benefit cost and prospective application for the amendments related to the capitalization requirements for the service cost components of net benefit cost. The System plans to implement ASU No 2017-07 for its fiscal year beginning October 1, 2019. The System does not expect ASU No 2017-07 to have a material effect on the consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Recognition and Measurement of Financial Assets and Liabilities*. ASU No. 2016-01 addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The ASU is effective for not-for-profit entities for fiscal years beginning after December 15, 2018, with early adoption restricted to certain provisions and within certain time periods. Under ASU No. 2016-01, not-for-profit entities are no longer required to disclose fair value information concerning financial instruments measured at amortized cost, such as long-term debt. This provision of ASU No. 2016-01 may be early adopted for financial statements, which have not yet been issued or made available for issuance. The System is currently evaluating the impact of the provisions of the new standard on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-13, *Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*. ASU No. 2018-13 is intended to improve the effectiveness of fair value measurement disclosures. ASU No. 2018-13 is effective for all entities for annual periods beginning after December 15, 2019 and interim periods within those fiscal years; early adoption is permitted. Management plans to adopt the provisions of ASU No. 2018-13 in its fiscal year 2021. The System is still evaluating the impact ASU No. 2018-13 will have on its consolidated financial statements.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

In August 2018, the FASB issued ASU No. 2018-14, *Disclosure Framework Changes to the Disclosure Requirements for Defined Benefit Plans*. ASU No. 2018-14 is intended to improve the effectiveness of defined-benefit pension plan disclosures. ASU No. 2018-14 is effective in annual periods ending after December 15, 2021, with early adoption permitted. Management plans to adopt the provisions of ASU No. 2018-14 in its fiscal year 2022. The System has not yet determined the impact of ASU No. 2018-14 on its consolidated financial statements.

#### **(u) Reclassifications**

Certain 2018 amounts have been reclassified to conform to the 2019 consolidated financial statement presentation. These reclassifications have not changed the results of operations or cash flows of prior periods.

#### **(2) Investments and Assets Limited as to Use**

The composition of investments follows (in thousands):

	<u>2019</u>	<u>2018</u>
Obligations of the U.S. government and its agencies	\$ 256,621	229,124
Corporate debt securities	170,200	174,735
Corporate equity securities	4,014	5,580
Mutual funds	150,178	178,755
Certificates of deposit	404	404
Hedge funds	18,534	18,615
Interest in Mississippi Hospital Association pooled investments	1,263	1,179
	<u>\$ 601,214</u>	<u>608,392</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The composition of assets limited as to use follows (in thousands):

	<u>2019</u>	<u>2018</u>
Under indenture agreements – held by trustee:		
Obligations of the U.S. government and its agencies	\$ 921	928
Less deposits classified as other current assets	<u>9</u>	<u>10</u>
	<u>912</u>	<u>918</u>
Under professional and general liability funding arrangement – held by trustee:		
Cash and cash equivalents	681	1,490
Obligations of the U.S. government and its agencies	10,924	6,727
Corporate debt securities	5,135	5,302
Mutual funds	4,791	6,619
Accrued interest receivable	<u>133</u>	<u>475</u>
	<u>21,664</u>	<u>20,613</u>
By board for capital improvements:		
Cash and cash equivalents	3,625	331
Obligations of the U.S. government and its agencies	30,318	26,697
Corporate debt securities	20,108	20,360
Corporate equity securities	474	650
Mutual funds	17,742	20,828
Hedge funds	2,190	2,169
Interest in Mississippi Hospital Association pooled investments	149	137
Accrued interest receivable	<u>41</u>	<u>42</u>
	<u>74,647</u>	<u>71,214</u>
Total noncurrent assets limited as to use	\$ <u>97,223</u>	<u>92,745</u>

The funds held by trustee under indenture agreements were established in accordance with the requirements of the indentures related to the various Mississippi Hospital Equipment and Facilities Authority revenue bond issues discussed in note 8. Deposits classified as current assets will be used to relieve obligations classified as current liabilities at September 30.

**(3) Investment in Equity Investees**

The System's investment in Healthcare Providers Insurance Company (HPIC), a reciprocal insurance exchange, is accounted for using the equity method and consists of a subscriber interest of approximately 44% and 41% for the years ended September 30, 2019 and 2018, respectively. The System recorded year-end investment activity related to HPIC based on financial data as of December 31, 2018 and 2017, respectively, which is the latest available data.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

HPIC provides the System with a claims-made policy covering certain layers of general and professional liability risks, as described in note 14. The costs associated with the policy were approximately \$1,975,000 and \$1,987,000 in 2019 and 2018, respectively, and were charged to supplies and other expenses in the accompanying consolidated statements of operations.

The carrying amount of the investment in HPIC was approximately \$24,009,000 and \$20,688,000 at September 30, 2019 and 2018, respectively, and is recorded in other assets in the accompanying consolidated balance sheets. The System's equity in the net income of HPIC was approximately \$3,321,000 and \$1,128,000 for the years ended September 30, 2019 and 2018, respectively.

Summary unaudited financial information for HPIC as of and for the years ended December 31, 2018 and 2017 follows (in thousands):

	<u>2018</u>	<u>2017</u>
Cash and invested assets	\$ 77,944	79,879
Other assets	1,817	1,628
	<u>79,761</u>	<u>81,507</u>
Total liabilities	25,630	30,662
Accumulated surplus	54,131	50,845
	<u>79,761</u>	<u>81,507</u>
Net underwriting gain	7,787	2,873
Investment gain	2,769	2,136
Other changes in accumulated surplus	<u>(7,270)</u>	<u>(1,481)</u>
Change in accumulated surplus	\$ <u>3,286</u>	<u>3,528</u>

The System's other equity investees were insignificant at September 30, 2019 and 2018.

**(4) Other Current Assets**

The composition of other current assets follows (in thousands):

	<u>2019</u>	<u>2018</u>
Assets limited as to use – required for current liabilities	\$ 9	10
Due from third-party payors	1,484	207
Other receivables	5,927	3,580
Inventories	26,023	26,650
Prepaid expenses and other current assets	<u>10,839</u>	<u>8,449</u>
	\$ <u>44,282</u>	<u>38,896</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

**(5) Other Assets**

The composition of other assets follows (in thousands):

	<u>2019</u>	<u>2018</u>
Investment in equity investees	\$ 24,009	20,688
Interest in net assets of affiliated foundation	3,223	3,188
Insurance receivables	2,180	2,426
Deferred compensation 457(b) assets	21,790	20,817
Other	<u>5,460</u>	<u>3,795</u>
	<u>\$ 56,662</u>	<u>50,914</u>

**(6) Property and Equipment**

A summary of property and equipment follows (in thousands):

	<u>2019</u>	<u>2018</u>
Land and improvements	\$ 35,303	33,282
Buildings and improvements	395,258	385,183
Fixed equipment	134,721	135,340
Movable equipment, including computer hardware and software	497,436	460,831
Construction in progress	<u>4,263</u>	<u>18,888</u>
	1,066,981	1,033,524
Less accumulated depreciation	<u>810,884</u>	<u>772,529</u>
	<u>\$ 256,097</u>	<u>260,995</u>

Construction in progress at September 30, 2019 principally comprises costs incurred for renovations of the Monroe Health Services, Inc. (MHS) main hospital facility acquired during the current year (note 20), with the most significant portions of the renovation and construction projects planned for completion through September 30, 2020. The estimated total remaining cost to complete renovation and construction projects at September 30, 2019 is approximately \$4,500,000. The System expects to fund a portion of the projects through operations and net assets without donor restrictions.

Depreciation expense was approximately \$47,877,000 in 2019 and \$48,066,000 in 2018. The System capitalized approximately \$432,000 and \$230,000 of interest expense in 2019 and 2018, respectively.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

**(7) Accrued Expenses and Other Current Liabilities**

The composition of accrued expenses and other current liabilities follows (in thousands):

	<u>2019</u>	<u>2018</u>
Accrued payroll costs	\$ 21,818	23,789
Accrued compensated absences	20,475	19,000
Deferred compensation 457(b)	21,790	20,817
Accrued workers' compensation costs	3,337	3,463
Due to third-party payors	11,076	10,045
Accrued interest	1,307	1,311
Current portion of other long-term liability	—	6,493
Other	10,524	6,634
	<u>\$ 90,327</u>	<u>91,552</u>

**(8) Long-term Debt**

A summary of long-term debt follows (in thousands):

	<u>2019</u>	<u>2018</u>
Notes payable	\$ 525	670
Mississippi Hospital Equipment and Facilities Authority		
Revenue Bonds:		
2017 Series 1, due in October 2020	50,000	43,806
2010 Series 1, due in variable amounts through October 2039	34,130	34,130
2003 Series 2, due in variable amounts through May 2033	29,175	29,175
2001 Series 1, due in variable amounts through May 2030	33,175	35,540
1997 Series 1, due in variable amounts through May 2025	10,790	12,390
	<u>157,795</u>	<u>155,711</u>
Unamortized discount/premium, net	(50)	(53)
Unamortized debt issuance costs	(669)	(796)
	<u>157,076</u>	<u>154,862</u>
Capital lease obligations of NMJV and its subsidiaries, payable in monthly installments at varying amounts through September 2020, at interest rates ranging from 0% to prime plus 3%, secured by leased equipment	225	810
	<u>157,301</u>	<u>155,672</u>
Less current installments	<u>73,482</u>	<u>77,685</u>
	<u>\$ 83,819</u>	<u>77,987</u>

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

In September 2017, the 2017 Series 1 revenue bonds were authorized in an amount not to exceed \$50,000,000. The bond indenture is between North Mississippi Medical Center, Clay County Medical Center, and Webster Health Services, Inc. (collectively, the Obligated Group) and Mississippi Hospital Equipment and Facilities Authority. The 2017 Series 1 revenue bonds are secured by a pledge of the net revenue of the Obligated Group as established under the Obligated Group's Master Trust Indenture. The 2017 Series 1 revenue bonds are tax-exempt variable rate debt and were placed directly with Bank of America Public Capital Corp.

In September 2017, the Obligated Group drew down approximately \$37,889,000 of the available 2017 Series 1 revenue bonds and used \$37,500,000 of these proceeds to advance refund \$37,500,000 of principal maturity of the 2010 Series 1 revenue bonds, which was due on October 1, 2017. Of the remaining \$389,000 of proceeds received, approximately \$218,000 were used for debt issuance costs, with the remaining amount used to reimburse NMMC for eligible project costs.

The remaining \$34,130,000 of the 2010 Series 1 revenue bonds will mature in accordance with the original bond agreement.

In fiscal years 2019 and 2018, the Obligated Group drew down approximately \$6,194,000 and \$5,917,000, respectively, of the 2017 Series 1 revenue bonds and used these proceeds to purchase medical equipment. The interest rate on all issued debt under the 2017 Series 1 revenue bonds is 70% of LIBOR plus 40 basis points.

In July 2003, the Obligated Group issued the 2003 Series 2 revenue bonds for \$98,400,000. A portion of the 2003 Series 2 revenue bonds was used to refund the outstanding bonds from the 1993 bond series. The bond indenture related to the 1993 bond series between the Obligated Group and Mississippi Hospital Equipment and Facilities Authority has been released and the Obligated Group no longer has any obligations associated with the refunded issue.

In April 2008, the Obligated Group converted, as permitted under the original indenture agreement, the 2003 Series 2 revenue bonds through a mandatory tender option from auction rate securities to variable rate demand obligations. Since the market liquidity of the 2003 Series 2 revenue bonds is supported solely by the Obligated Group, the bonds are classified as current installments of long-term debt in the accompanying consolidated balance sheets.

In December 2008, the outstanding portions of the 1997 Series 1 and 2001 Series 1 revenue bonds of \$26,795,000 and \$40,000,000, respectively, were remarketed by the Obligated Group due to the expiration of the original Liquidity Facility on December 29, 2008. The revenue bonds, as currently structured, are not supported by an external liquidity facility or a financial institution credit facility but are secured solely by the Obligated Group through notes issued between the Obligated Group and The Bank of New York Mellon Trust Company, N.A., trustee for the bondholders. The notes are the joint and several obligations of the Obligated Group and are secured by the pledge of the net revenue of each Obligated Group member, subject to permitted liens. The notes are equal to the principal amounts of the 1997 Series 1 and 2001 Series 1 revenue bonds and have terms and conditions requiring payments thereon sufficient to pay the contractual maturities of the bonds when due. Since the market liquidity of the 1997 Series 1 and 2001 Series 1 revenue bonds is supported solely by the Obligated Group, the bonds are classified as current installments of long-term debt in the accompanying consolidated balance sheets.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

In August 2010, the System issued the 2010 Series 1 revenue bonds for \$71,630,000 (interest fixed at coupon rates ranging from 4.75% to 5.00%) with an original issue net premium of \$4,388,658. Proceeds from the bonds were used for certain renovations of the NMMC main hospital facility and for the payment of costs incurred in connection with the issuance of the bonds.

Certain trusted assets, as described in note 2, and the future net revenue of the Obligated Group are pledged as security for payment of the various revenue bonds. Additionally, the Obligated Group is required to comply with certain financial and nonfinancial covenants customary of such obligations.

Except for the 2010 Series 1 fixed rate bonds and 2017 Series 1 revenue bonds, all other currently outstanding revenue bonds bear interest at variable rates and are supported by remarketing agreements and the Obligated Group's institutional commitment to provide market liquidity. Interest rates are periodically adjusted based upon prevailing rates for the contract period related to the remarketed tranche. In the event a market for variable rate instruments is not sustained, the Obligated Group would be required, if necessary, to provide sustaining liquidity to honor the "put" feature of the then-existing bondholders. The maximum annual interest rate that the 2003, 2001, and 1997 bonds may bear is 13%. The average annual interest rate paid on the 2003, 2001, 1997, and 2017 revenue bonds approximated 2.2% and 1.9% for the years ended September 30, 2019 and 2018, respectively.

Interest is periodically due on the variable rate revenue bonds at the end of related contract periods, while interest on the fixed rate bonds is due semiannually.

The notes payable are guaranteed by the System and the other members of each respective joint venture at their proportionate interests in each entity.

The System paid interest on long-term debt of approximately \$4,675,000 in 2019 and \$3,424,000 in 2018.

Principal is due in varying amounts each May 15 or October 1 until the year 2039. Future maturities of long-term debt, excluding the capital lease obligations and assuming the demand bonds are not called prior to the stated maturities, by year and in the aggregate, follow (in thousands):

2020	\$	4,277
2021		54,452
2022		4,622
2023		4,673
2024		4,825
Thereafter		<u>84,946</u>
	\$	<u>157,795</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

**(9) Derivative Financial Instruments**

The Obligated Group has executed interest rate swap agreements for the purpose of synthetically converting certain variable rate debt obligations to fixed rate instruments. Accordingly, notional swap amounts are tied to related revenue bond principal balances. A summary of information related to these instruments at September 30, 2019 and 2018 follows:

<b>2019</b>						
<u>Related bond issuance</u>	<u>Notional amount (in thousands)</u>	<u>Maturity date</u>	<u>Rate paid</u>	<u>Average rate received</u>	<u>Net settlement amount (in thousands)</u>	<u>Swap fair value liability (in thousands)</u>
2003 Series 2	\$ 23,875	May 15, 2033	3.437 %	1.6168 %	\$ (430)	(6,405)

  

<b>2018</b>						
<u>Related bond issuance</u>	<u>Notional amount (in thousands)</u>	<u>Maturity date</u>	<u>Rate paid</u>	<u>Average rate received</u>	<u>Net settlement amount (in thousands)</u>	<u>Swap fair value liability (in thousands)</u>
2003 Series 2	\$ 23,875	May 15, 2033	3.437 %	1.1750 %	\$ (537)	(3,710)

The Obligated Group's interest rate swaps are executed over the counter and are valued using the net present value of cash flow streams, adjusted for risk associated with credit default, as no quoted market prices exist for such instruments. The System also employs an independent third party to perform mark to market valuation assessments on the swaps to assess the valuations otherwise received by MHS. The Obligated Group has categorized its interest rate swap fair value estimates as Level 2, as defined in note 17, in the fair value hierarchy.

**(10) Net Patient Service Revenue**

The System has determined that the nature, amount, and uncertainty of revenue and cash flows are affected by the following factors: payors and service lines. The following tables provide details of these factors.

The composition of net patient service revenue by primary payor for the years ended September 30, 2019 and 2018 is as follows (dollars in thousands):

	<u>2019</u>	<u>Percent</u>	<u>2018</u>	<u>Percent</u>
Medicare	\$ 406,360	42 %	\$ 374,804	41 %
Medicaid	141,644	15	133,505	15
Blue Cross	150,036	16	147,248	16
Self-pay	5,313	1	5,854	1
Commerical and other	253,651	26	248,708	27
	<u>\$ 957,004</u>	<u>100 %</u>	<u>\$ 910,119</u>	<u>100 %</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The revenue generated by the System is primarily generated within the North Mississippi Medical Center (Tupelo location) and throughout the northern Mississippi region, with limited revenue being generated in West Alabama.

The composition of net patient service revenue based on the System's lines of business for the years ended September 30, 2019 and 2018 is as follows (in thousands):

	<u>2019</u>	<u>2018</u>
Service lines:		
Hospitals	\$ 689,689	666,066
Medical clinics	200,554	180,261
Joint ventures	30,902	30,397
Nursing homes	21,409	20,030
Other	<u>14,450</u>	<u>13,365</u>
	<u>\$ 957,004</u>	<u>910,119</u>

Certain subsidiaries of the System have agreements with government and other third-party payors that provide for reimbursement to such subsidiaries at amounts different from established rates. Contractual adjustments under third-party reimbursement programs represent the difference between billings at established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursement with major third-party payors follows:

- Medicare – Substantially all acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Certain types of exempt services and other defined payments related to Medicare program beneficiaries are paid based upon cost reimbursement or other retroactive-determination methodologies. As applicable, subsidiaries of the System are paid for retroactively determined items at a tentative rate with final settlement determined after submission of annual cost reports by the related subsidiaries and audits by the Medicare fiscal intermediary. Related cost reports have been audited and substantially settled for all fiscal years through September 30, 2016.
- Medicaid – Inpatient and outpatient services rendered to Medicaid program beneficiaries are generally paid based upon prospective reimbursement methodologies established by the State of Mississippi and the State of Alabama.

The System participates in certain supplemental Medicaid reimbursement programs for the purpose of offsetting the cost of providing care to Medicaid patients. These programs are funded with a combination of state and federal resources, including fees or taxes paid by the providers. Amounts received by certain subsidiaries of the System in excess of amounts paid into the programs were approximately \$28,262,000 and \$24,063,000 for the years ended September 30, 2019 and 2018, respectively, and have been recognized as reductions in related explicit price concessions in the accompanying consolidated statements of operations. There can be no assurance that applicable subsidiaries of the System will continue to qualify for future participation in these programs or that the programs will not ultimately be discontinued or materially modified.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

- Blue Cross and Blue Shield of Mississippi (Blue Cross) – All acute care services rendered to Blue Cross program beneficiaries are reimbursed at prospectively determined rates.

Related subsidiaries of the System have also entered into other reimbursement arrangements providing for payment methodologies which include prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

Net patient service revenue increased by approximately \$2,707,000 and \$810,000 in 2019 and 2018, respectively, due to final settlements and revised estimated settlements in excess of amounts previously recorded, removal of allowances previously estimated that are no longer necessary as a result of final settlements, and years that are no longer subject to audits, reviews, and investigations.

The System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of the System's net patient accounts receivable from patients and third-party payors at September 30, 2019 and 2018 was as follows (in thousands):

	<u>2019</u>	<u>2018</u>
Medicare	38 %	28 %
Medicaid	10	12
Blue Cross	18	13
Self-pay	9	23
Managed care/other	25	24
	<u>100 %</u>	<u>100 %</u>

**(11) Service to the Community**

The mission of the System is to continuously improve the health of its service population. In carrying out its mission and in being an active, caring member of the community, the System serves the community in a variety of ways.

One of the primary ways the System serves the community is by providing care to various populations for which it receives little or no compensation or for which it receives compensation at rates significantly less than established rates. This is a critical matter of community service which is further described below.

Based on gross charges, approximately 7% of the System's total services and 20% of total emergency room services were provided to patients, with no insurance for both of the years ended September 30, 2019 and 2018. Historically, the System collects only a small percentage of amounts otherwise due from uninsured patients; a significant portion of these uncollectible accounts ultimately meet the charity requirements described below, and the remaining uncollectible accounts result in implicit price concessions.

The System applies the community benefit reporting guidance provided in *A Guide for Planning and Reporting Community Benefit* published by the Catholic Health Association of the United States in 2006 and, therefore, does not formally consider implicit price concessions to uninsured patients and bad debt to

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

be a part of the community benefit it provides. Nevertheless, implicit price concessions to uninsured patients and bad debt are important components of the System's overall uncompensated care burden.

The board of directors of the System has established a policy under which the System provides care, without charge, to needy members of its community. The charity care policy states that the System will provide necessary hospital services free of charge to patients at threshold household income levels, which are based on the federal poverty guidelines. The policy applies to individuals who reside in the System's 24-county service area, as defined by the policy. Patients from outside the service area may also be granted charity care based on the judgment of System management and depending on individual circumstances. The policy also requires patients to cooperate fully with the System's requests for information to verify patient eligibility.

Following that policy, the System maintains records to identify and monitor the level of charity care it provides. The estimated cost of charity care provided by the System was approximately \$15,675,000 and \$15,803,000 in 2019 and 2018, respectively, calculated based on the ratio of total direct and indirect costs to established charges, applied to the charges forgone under the charity care policy. The total cost estimate is based on the ratio of operating costs, less adjustments for non-patient care activities, community benefits expense, and Medicaid provider taxes to charges. In addition to this level of charity care, the System also foregoes collection on a portion of all self-pay gross charges, which is known as the uninsured upfront discount. The uninsured upfront discount was approximately \$99,704,000 and \$98,988,000 in 2019 and 2018, respectively.

In addition to community services directly associated with providing clinical care, the System seeks to strengthen community relationships through developing and maintaining a proactive involvement and outreach program aimed at creating an inclusive and lasting relationship with the community. Examples of the System's community involvement include the following:

*Athletic trainers* – The System employs certified athletic trainers who provide services to high schools in its service area at no cost. The trainers work with the sports teams at these schools on a daily basis during practice and training, as well as at in-season competitions. The cost of providing these services was approximately \$734,000 and \$713,000 for the years ended September 30, 2019 and 2018, respectively.

*Nurse Link* – Nurse Link is a free community telephone service that assists callers with health information, offers triage for symptom-based calls, and makes recommendations for care by utilizing a physician approved, computerized protocol system and reference materials. Nurse Link is staffed by registered nurses and is available from 4 p.m. until midnight on weekdays and from 8 a.m. until midnight on weekends and holidays, and also includes The Appointment Desk and Physician Consult Line. The Appointment Desk is a free community health information and physician referral service. Physician Consult Line is a free service that provides regional physicians and their staff access to all the System's departments, specialists and clinics. In addition, Nurse Link provides after-hours coverage for physician clinics throughout northeast Mississippi and for the branch offices of NMMC Home Health Agency and Hospice. Nurse Link has also teamed with various System clinical services departments to provide a call-back service to their discharged patients. The cost of providing these services was approximately \$705,000 and \$547,000 for the years ended September 30, 2019 and 2018, respectively.

*Donations to charitable organizations* – The System makes cash donations to a wide variety of community charitable organizations involved in local schools, the arts, public health, and community development

## **NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

activities. The System contributed approximately \$177,000 and \$178,000 in charitable corporate donations to these organizations for the years ended September 30, 2019 and 2018, respectively.

Although the System has estimated the cost of each of these efforts to serve north Mississippi and the surrounding area, management and the board of directors believe that such costs represent only one facet of the many ways the System serves the community. The above examples relate only to certain measurable benefits that the System provides to its service area. This presentation is not intended to measure all such community benefits, many of which are intangible in nature or otherwise not quantifiable.

### **(12) Leases**

Rental expense for all operating leases was approximately \$4,366,000 and \$3,970,000 in 2019 and 2018, respectively. There were no significant noncancelable operating leases at September 30, 2019.

### **(13) Employee Benefit Plans**

#### **(a) Pension Plan**

The System sponsors a defined-benefit pension plan (the Plan) covering all permanent employees who make application to become participants, have attained the age of 21, and completed one year of services as defined in the Plan. Participants are required to contribute 1% of their annual compensation. The System contributes an amount equal to the difference between employees' contributions and the amount required to fund the Plan, as determined by consulting actuaries. Effective March 31, 2014, the Plan was closed to new participants. Effective January 1, 2016, the Plan was frozen.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The Plan's funded status (measured at September 30, 2019 and 2018) and amounts recognized in the System's consolidated financial statements follow (in thousands):

	<u>2019</u>	<u>2018</u>
Change in projected benefit obligation:		
Projected benefit obligation at the beginning of year	\$ 486,173	516,698
Service cost	8,439	10,967
Interest cost	19,840	18,590
Plan participants' contributions	617	684
Benefits paid	(14,515)	(11,969)
Actuarial loss (gain)	<u>78,962</u>	<u>(48,797)</u>
Projected benefit obligation at the end of year	<u>\$ 579,516</u>	<u>486,173</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ 412,915	399,834
Actual return on plan assets	54,205	11,366
Employer contributions	13,000	13,000
Plan participants' contributions	617	684
Benefits paid	<u>(14,515)</u>	<u>(11,969)</u>
Fair value of plan assets at end of year	<u>\$ 466,222</u>	<u>412,915</u>
Funded status:		
Projected benefit obligation	\$ 579,516	486,173
Fair value of plan assets	<u>466,222</u>	<u>412,915</u>
Funded status at end of year	<u>\$ (113,294)</u>	<u>(73,258)</u>
Accumulated benefit obligation	\$ 528,231	464,437

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Amounts recognized in the consolidated balance sheets consist of:		
Accrued pension cost	\$ (113,294)	(73,258)
Net assets without donor restrictions	(130,522)	(80,115)
Amounts not yet reflected in net periodic benefit cost and included in net assets without donor restrictions:		
Prior service cost	\$ —	—
Accumulated loss	<u>(130,522)</u>	<u>(80,115)</u>
	\$ <u>(130,522)</u>	<u>(80,115)</u>
Components of net periodic pension cost:		
Service cost	\$ 8,439	10,967
Interest cost	19,840	18,590
Expected return on plan assets	(28,848)	(28,093)
Amortization of net loss	<u>3,198</u>	<u>6,156</u>
Net periodic pension cost	\$ <u>2,629</u>	<u>7,620</u>
Other changes recognized in net assets without donor restrictions:		
Net loss (gain) arising during period	\$ 53,605	(32,070)
Amortization of net loss	<u>(3,198)</u>	<u>(6,156)</u>
Total recognized in net assets without donor restrictions	\$ <u>50,407</u>	<u>(38,226)</u>

The following are the estimated amounts that will be amortized from net assets without donor restrictions over the next fiscal year:

Amortization of prior service cost	\$ —
Amortization of loss	<u>7,544</u>
	\$ <u>7,544</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Weighted average assumptions used to determine benefit obligations in the accompanying consolidated balance sheets at September 30:		
Discount rate	3.36 %	4.36 %
Rate of compensation increase	3.00	3.00
Measurement date	September 30, 2019	September 30, 2018
Weighted average assumptions used to determine net periodic benefit cost:		
Discount rate	4.36 %	4.06 %
Expected long-term rate of return on plan assets	7.00	7.00
Rate of compensation increase	3.00	3.00

The Plan's expected long-term rate of return on assets is determined by reviewing the historical returns of each asset category comprising the Plan's target asset allocation. This review produces an annual return assumption for each asset category. The product of the annual return assumption and the Plan's target asset allocation percentage for each asset category equals the annual return attribution by asset category. The asset allocation for the portfolio is based on the long-term funding goals of the Plan and the desired risk levels of the Plan's asset investments. The target allocation is monitored and is adjusted as the funded status of the Plan changes.

(i) *Plan Assets*

The System's pension plan weighted average asset allocations follow:

	<u>Plan assets at September 30,</u>	
	<u>2019</u>	<u>2018</u>
Asset category:		
Equities:		
Large-cap equity securities	13 %	13 %
Small- and -mid cap equity securities	1	2
International equity securities	12	11
Global equity securities	13	13
Debt securities	55	52
Cash and cash equivalents	1	1
Alternative investments	5	8
Total	<u>100 %</u>	<u>100 %</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The Plan's investment objectives are to protect long-term asset values by applying prudent, low-risk, high-quality investment disciplines and to enhance the values by maximizing investment returns through active security management within the framework of the investment policy. Asset allocation strategies and investment management structure are designed to meet the Plan's investment objectives.

(ii) *Cash Flows*

The System expects to contribute approximately \$13,000,000 to the Plan in 2020.

(iii) *Expected Future Benefit Payments*

The following benefit payments, which reflect future services as appropriate, are expected to be paid (in thousands):

	<b>Pension benefits</b>	
	<hr/>	
2020	\$	17,744
2021		19,137
2022		20,797
2023		22,479
2024		24,179
2025–2029		145,912

(iv) *Fair Value of Plan Assets*

The composition of plan assets follows (in thousands):

	<b>2019</b>		<b>2018</b>	
	<hr/>		<hr/>	
Mutual funds:				
Large-cap equity securities	\$	58,950		53,634
Small- and -mid cap equity securities		5,791		6,693
International equity securities		53,671		47,354
Global equity securities		59,563		55,607
Debt securities		258,448		215,263
Cash and cash equivalents		3,581		2,985
Hedge funds		26,218		31,379
		<hr/>		<hr/>
	\$	466,222		412,915
		<hr/>		<hr/>

All of the Plan assets are categorized as Level 1 in the fair value hierarchy, as described in note 17, except hedge funds, which are not categorized because fair value is measured using the net asset value practical expedient.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

### **(b) Defined-Contribution Plans**

The System also sponsors a contributory savings plan, North Mississippi Health Services, Inc. Employer Savings Plan, which covers most employees aged 21 and older who have completed one year of service, as defined in the plan. Eligible employees may contribute up to 20% of compensation in any one year, subject to a regulatory limit. The System makes matching contributions equal to 50% of the employees' contributions, not to exceed 2% of total compensation. Effective April 1, 2014, employees hired on or after April 1, 2013 are eligible for a supplemental employer contribution ranging from 5% to 200% (based on years of service) of the employee's contribution to the contributory savings plan, not to exceed 6% of compensation. The System contributed approximately \$15,830,000 and \$13,479,000 to this plan during the years ended September 30, 2019 and 2018, respectively.

NMMCI sponsored a defined-contribution retirement plan covering all of its employees. Participants were not eligible to make contributions to this plan. NMMCI made contributions equal to 5.7% of each participant's base compensation, plus 11.4% of each participant's excess compensation, as defined in the plan. Contributions were subject to regulatory limits. Effective January 1, 2017, the assets of this plan were merged into The North Mississippi Health Services, Inc. Employer Savings Plan, which is described above.

NMMCI also sponsored a contributory savings plan covering all of its employees. Participating employees were able to contribute up to 20% of compensation in any one year, subject to regulatory limits. While NMMCI may make discretionary contributions to this plan, no such contributions were made during the year ended September 30, 2019 or 2018. Effective January 1, 2017, the assets of this plan were merged into The North Mississippi Health Services, Inc. Employer Savings Plan, which is described above.

### **(14) Insurance Programs**

The System has substantial claims-made basis excess insurance coverage in place for general and professional liability risks. The insurance program is made up of a combination of self-insurance retention and claims-made excess insurance coverage. As of and for the year ended September 30, 2019, the self-insurance retention was \$5 million per claim for professional liability and \$2 million per occurrence for general liability, subject to a combined \$7 million aggregate. Effective October 1, 2019, the System's excess insurance coverage was renewed at the same levels of retention.

The System's employed physicians are covered by a first-dollar, claims-made physician liability policy with a \$1 million per professional incident limit and a \$3 million aggregate limit.

Incurred losses identified under the System's incident reporting system and incurred but not reported losses are accrued based on estimates that incorporate the System's past experience, as well as other considerations such as the nature of each claim or incident, relevant trend factors, and advice from consulting actuaries. Because the terms of the System's general and professional liability program provide for first-dollar, claims-made coverage at the affiliate level, reserves and related insurance receivables related to general and professional liability exposures are held at the System consolidated level and not allocated to individual affiliates.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The System has established a self-insurance trust fund for payment of liability claims and makes deposits to the fund in amounts determined by consulting actuaries. The System also has substantial excess liability coverage available under the provisions of certain claims-made policies, currently expiring on October 1, 2020. To the extent that any claims-made coverage is not renewed or replaced with equivalent insurance, claims based on occurrences during the term of such coverage, but reported subsequently, would be uninsured. Management believes, based on incidents identified through the System's incident reporting system, that any such claims would not have a material effect on the System's results of operations or financial position. In any event, management anticipates that the claims-made coverage currently in place will be renewed or replaced with equivalent insurance as the term of such coverage expires.

The System is also self-insured with respect to employee health coverage and workers' compensation (up to a limit of \$1,000,000 per individual claim, \$300,000 prior to October 1, 2012). Substantial excess insurance coverage is maintained for potential excess losses under the workers' compensation program.

#### (15) Net Assets With Donor Restrictions

Net assets with donor restrictions (currently held at Health Care Foundation of North Mississippi, an affiliated foundation) are available for the following purposes at September 30, 2019 and 2018 (in thousands):

	<u>2019</u>	<u>2018</u>
Patient assistance	\$ 1,166	1,102
Purchase of equipment and other property	227	231
Education	441	407
Employee benevolent fund	42	38
Time restricted	<u>1,347</u>	<u>1,410</u>
	<u>\$ 3,223</u>	<u>3,188</u>

#### (16) Information Technology Contract

NMMC has entered into a 10-year software and services agreement with a major information technology vendor. The agreement generally commits NMMC to the purchase of a variety of information technology products and services from this vendor for a defined payment stream over the term of the contract. Certain software license and support fees and related implicit maintenance and training costs (totaling approximately \$37,670,000) were capitalized during fiscal year 2010 with recognition of an associated liability related to NMMC's acquisition of these intangible assets. The agreement expired in fiscal year 2019 and the System entered into a 5-year service contract to extend its use of the software. Costs under the new agreement are related to maintenance and will be expensed as incurred.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The following table summarizes the future payment commitments under the contract as of September 30, 2019 (in thousands):

	<b>Maintenance costs</b>
2020	\$ 5,768
2021	5,748
2022	6,054
2023	6,014
2024	6,191
Thereafter	
Total	\$ <u>29,775</u>

**(17) Fair Value Hierarchy of Investments and Assets Limited as to Use**

In accordance with Topic 820, the System has categorized its financial instruments based on the priority of inputs used in related valuation techniques into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets (Level 1), inputs other than quoted market prices that are observable, either directly or indirectly (Level 2), and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within multiple levels of the hierarchy, the categorization is based on the lowest-level input that is significant to the fair value measurement of the instrument.

When available, the System uses quoted market prices to determine fair value and classifies such items as Level 1. The System's Level 2 securities are bonds whose fair values are determined by independent vendors, or nontraded funds whose underlying securities would otherwise be considered Level 1. The vendors compile prices from various sources and may apply matrix pricing for similar bonds or loans where no price is observable in an actively traded market. If available, the vendor may also use quoted prices for recent trading activity of assets with similar characteristics to the bond being valued.

The System's alternative investments are not categorized within the fair value hierarchy because fair value is measured using the NAV per share practical expedient. The System's alternative investments' NAVs are obtained from the fund manager. For the System's hedge funds, the manager receives account statements directly from independent administrators or the underlying hedge funds managers, who are responsible for the valuation of these funds. Before reliance on these valuations, the managers evaluate the investee fund's fair value estimation processes and control environment, the investee fund's policies and procedures for estimating fair value of underlying investments, the investee fund's use of independent third-party valuation experts, the portion of the underlying securities traded on active markets, and the professional reputation and standing of the investee fund's auditor.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The System is subject to limitation on redemption of their hedge fund investments and assets limited as to use as follows:

	<b>Fair value at September 30, 2019 (in thousands)</b>	<b>Unfunded commitment</b>	<b>Redemption frequency</b>	<b>Redemption notice period</b>
Hedge fund – Fund of funds (a)	\$ 10,459	—	Three-year lock-up	95 days
Hedge fund – Fund of funds (b)	10,265	—	One-year lock-up	90 days
	<u>\$ 20,724</u>	<u>—</u>		

	<b>Fair value at September 30, 2018 (in thousands)</b>	<b>Unfunded commitment</b>	<b>Redemption frequency</b>	<b>Redemption notice period</b>
Hedge fund – Fund of funds (a)	\$ 10,336	—	Three-year lock-up	95 days
Hedge fund – Fund of funds (b)	10,448	—	One-year lock-up	90 days
	<u>\$ 20,784</u>	<u>—</u>		

- (a) This category includes investments in hedge funds that invest primarily in a diversified group of long/short equity investment funds. The underlying investment funds may invest in U.S. and non-U.S. equity securities, debt securities, derivatives, and other financial instruments, in both long and short positions. The hedge funds investments in investment funds comprise funds with various investment strategies.
- (b) This category includes investments in hedge funds that invest primarily all of its assets into the Master Feeder Fund. The Master Feeder Fund invests primarily through pooled investment vehicles and assets to reduce volatility and enhance return by allocating primarily to fundamental long/short equity managers with a diversifying component in opportunistic managers.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The fair value hierarchy of investments at September 30, 2019 and 2018 follows (in thousands):

	<b>2019</b>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
Obligations of the U.S. government and its agencies	\$ —	256,621	256,621
Corporate debt securities:			
Corporate bonds:			
Financials	\$ —	48,049	48,049
Industrials	—	64,594	64,594
Utilities	—	12,758	12,758
Other	—	22,190	22,190
Foreign bonds and notes	—	22,609	22,609
Corporate equity securities:			
Consumer discretionary	814	—	814
Financial services	552	—	552
Industrials	1,289	—	1,289
Information technology	785	—	785
Materials and processing	101	—	101
Telecommunication services	203	—	203
Real Estate	270	—	270
Mutual funds:			
Large-cap equity securities	23,173	—	23,173
Small- and -mid cap equity securities	4,268	—	4,268
International equity securities	22,679	—	22,679
Debt securities	96,549	—	96,549
Other	3,509	—	3,509
Interest in Mississippi Hospital Association pooled investments	—	1,263	1,263
Certificates of deposit	—	404	404
Hedge funds at net asset value	—	—	18,534
	<u>154,192</u>	<u>171,867</u>	<u>326,059</u>
	<u>\$ 154,192</u>	<u>428,488</u>	<u>582,680</u>
		<u>\$ 601,214</u>	

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

	<b>2018</b>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
Obligations of the U.S. government and its agencies	\$ —	229,124	229,124
Corporate debt securities:			
Corporate bonds:			
Financials	—	51,811	51,811
Industrials	—	80,503	80,503
Utilities	—	6,411	6,411
Other	—	9,057	9,057
Foreign bonds and notes	—	26,953	26,953
Corporate equity securities:			
Consumer discretionary	1,334	—	1,334
Financial services	632	—	632
Foreign equities	696	—	696
Health care	142	—	142
Industrials	1,946	—	1,946
Information technology	184	—	184
Materials and processing	83	—	83
Telecommunication services	563	—	563
Mutual funds:			
Large-cap equity securities	23,352	—	23,352
Small- and -mid cap equity securities	5,967	—	5,967
Core value equity securities	7,451	—	7,451
International equity securities	26,922	—	26,922
Debt securities	101,673	—	101,673
Other	13,390	—	13,390
Interest in Mississippi Hospital Association pooled investments	—	1,179	1,179
Certificates of deposit	—	404	404
Hedge funds at net asset value	—	—	18,615
	<u>184,335</u>	<u>176,318</u>	<u>360,653</u>
	<u>\$ 184,335</u>	<u>405,442</u>	<u>589,777</u>
		\$	<u>608,392</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The fair value hierarchy of assets limited as to use at September 30, 2019 and 2018 follows (in thousands):

	<b>2019</b>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
Under indenture agreements – held by trustee:			
Obligations of the U.S. government and its agencies	\$ —	921	921
Under professional and general liability funding arrangement – held by trustee:			
Cash and cash equivalents	681	—	681
Obligations of the U.S. government and its agencies	—	10,924	10,924
Corporate debt securities:			
Corporate bonds:			
Financials	—	2,165	2,165
Industrials	—	1,462	1,462
Utilities	—	689	689
Other	—	549	549
Foreign bonds and notes	—	270	270
Mutual funds:			
Large-cap equity securities	966	—	966
Small- and -mid cap equity securities	422	—	422
International equity securities	742	—	742
Debt securities	1,790	—	1,790
Other	871	—	871
Accrued interest receivable	133		133
Subtotal	<u>5,605</u>	<u>16,059</u>	<u>21,664</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

	<b>2019</b>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
By board for capital improvements:			
Cash and cash equivalents	\$ 3,625	—	3,625
Obligations of the U.S. government and its agencies	—	30,318	30,318
Corporate debt securities:			
Corporate bonds:			
Financials	—	5,677	5,677
Industrials	—	7,630	7,630
Utilities	—	1,507	1,507
Other	—	2,622	2,622
Foreign bonds and notes	—	2,672	2,672
Corporate equity securities:			
Consumer discretionary	96	—	96
Financial services	65	—	65
Industrials	152	—	152
Information technology	93	—	93
Materials and processing	12	—	12
Telecommunication services	24	—	24
Real estate	32	—	32
Mutual funds:			
Large-cap equity securities	2,738	—	2,738
Small- and -mid cap equity securities	504	—	504
Core value equity securities	2,679	—	2,679
International equity securities	11,406	—	11,406
Debt securities	415	—	415
Interest in Mississippi Hospital Association pooled investments	—	149	149
Accrued interest receivable	41	—	41
Hedge funds at net asset value	—	—	2,190
Subtotal	<u>21,882</u>	<u>50,575</u>	<u>72,457</u>
Total	<u>\$ 27,487</u>	<u>67,555</u>	<u>97,232</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

	<b>2018</b>		
	<b>Level 1</b>	<b>Level 2</b>	<b>Total</b>
Under indenture agreements – held by trustee:			
Obligations of the U.S. government and its agencies	\$ —	928	928
Under professional and general liability funding arrangement – held by trustee:			
Cash and cash equivalents	1,490	—	1,490
Obligations of the U.S. government and its agencies	—	6,727	6,727
Corporate debt securities:			
Corporate bonds:			
Financials	—	2,077	2,077
Industrials	—	1,343	1,343
Utilities	—	393	393
Other	—	1,081	1,081
Foreign bonds and notes	—	408	408
Mutual funds:			
Large-cap equity securities	856	—	856
Small- and -mid cap equity securities	488	—	488
Core value equity securities	281	—	281
International equity securities	902	—	902
Debt securities	2,111	—	2,111
Other	1,981	—	1,981
Accrued interest receivable	475	—	475
Subtotal	<u>8,584</u>	<u>12,029</u>	<u>20,613</u>

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

	<b>2018</b>		
	<b>Level 1</b>	<b>Level 2</b>	<b>Total</b>
By board for capital improvements:			
Cash and cash equivalents	\$ 331	—	331
Obligations of the U.S. government and its agencies	—	26,697	26,697
Corporate debt securities:			
Corporate bonds:			
Financials	—	6,037	6,037
Industrials	—	9,380	9,380
Utilities	—	747	747
Other	—	1,055	1,055
Foreign bonds and notes	—	3,141	3,141
Corporate equity securities:			
Consumer discretionary	155	—	155
Financial services	74	—	74
Foreign equities	81	—	81
Health care	17	—	17
Industrials	227	—	227
Information technology	21	—	21
Materials and processing	10	—	10
Telecommunication services	65	—	65
Mutual funds:			
Large-cap equity securities	2,721	—	2,721
Small- and -mid cap equity securities	695	—	695
Core value equity securities	868	—	868
International equity securities	3,137	—	3,137
Debt securities	11,847	—	11,847
Other	1,560	—	1,560
Interest in Mississippi Hospital Association pooled investments	—	137	137
Accrued interest receivable	42	—	42
Hedge funds at net asset value	—	—	2,169
	Subtotal	47,194	69,045
	Total	60,151	92,755

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

**(18) Functional Expenses**

The System provides healthcare and other services to residents within its service area. Expenses related to providing these services for the years ended September 30, 2019 and 2018 are as follows (in thousands):

	Program Activities				Supporting Activities			Total
	Hospitals	Physicians	Other healthcare	Total program	General and administrative	Non-healthcare services	Total supporting	
Salaries and benefits	\$ 253,935	106,426	9,536	369,897	143,882	3,443	147,325	517,222
Supplies and other *	198,204	90,589	23,114	311,907	83,220	1,485	84,705	396,612
Depreciation and amortization	30,769	749	1,586	33,104	14,838	62	14,900	48,004
Interest	—	—	—	—	4,671	—	4,671	4,671
Total functional expenses	\$ 482,908	197,764	34,236	714,908	246,611	4,990	251,601	966,509

The consolidated financial statements report certain categories of expenses that are attributable to more than one function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The allocations are primarily based on total revenue and full-time equivalent employees of the related program activities and supporting activities.

\* The functional expense amounts for supplies and other presented above includes operating expenses and costs relating to the electronic medical records implementation presented on the statement of operations.

For the year ended September 30, 2018, expenses related to program activities and support activities were \$667,423,000 and \$256,247,000, respectively.

**(19) Availability of Resources and Liquidity**

The System has approximately \$771,236,000 of financial assets available to meet cash needs for general expenditures within one year of the consolidated balance sheet date. Available financial assets consist of cash and cash equivalents of approximately \$67,548,000, short-term investments of approximately \$601,214,000, and patient accounts receivable, collectible within one year, of approximately \$102,474,000. None of these financial assets are subject to donor or other contractual restrictions that make them unavailable for expenditure within one year of the balance sheet date. The System has a goal to maintain cash and investments sufficient to cover operating expenses at levels that meet or exceed standards established by rating agencies for similar organizations.

**(20) Acquisitions**

On December 31, 2018, the System acquired certain assets of Amory Regional Medical Center, Inc., an acute care hospital in Amory, Mississippi, for a purchase price of \$14,692,000. The purchase price was paid with cash on hand on the date of the transaction. Transaction costs of approximately \$1,400,000 were recorded in supplies and other expenses in the accompanying 2019 consolidated statement of operations. Such costs were expensed as incurred.

**NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2019 and 2018

The results of that business' operations from the date of acquisition are included in the System's accompanying 2019 consolidated statement of operations. Allocation of the purchase price is as follows (in thousands):

Current assets	\$	1,346
Property, plant and equipment, net		12,339
Other assets		1,210
Accrued expenses and other current liabilities		<u>(203)</u>
	\$	<u>14,692</u>

**(21) Subsequent Events**

The System has evaluated subsequent events from the consolidated balance sheet date through December 20, 2019, the date the consolidated financial statements were issued, and determined there are no additional subsequent events to be recognized in the consolidated financial statements and related notes, except as follows:

The System is evaluating a potential refinancing to close in fiscal year 2020.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Consolidating Schedule – Balance Sheet Information

September 30, 2019

(with comparative 2018 consolidated information)

(In thousands)

	North Mississippi Health Services, Inc.	North Mississippi Medical Center, Inc.	North Mississippi Medical Clinics, Inc. and subsidiaries	Tupelo Service Finance, Inc.	Clay County Medical Corporation	Webster Health Services, Inc.	Marion Regional Medical Center, Inc.	Tishomingo Health Services, Inc.	North Mississippi Joint Ventures, LLC and subsidiaries
<b>Assets</b>									
Current assets:									
Cash and cash equivalents	\$ 1,229	54,971	1,666	183	1,969	286	422	414	1,701
Investments	—	600,810	—	—	—	—	—	—	—
Net patient accounts receivable	—	69,713	2,139	15,216	3,976	1,900	1,569	1,152	3,679
Other current assets	1,566	32,204	914	—	1,047	817	563	373	1,594
Total current assets	2,795	757,698	4,719	15,399	6,992	3,003	2,554	1,939	6,974
Assets limited as to use	21,664	75,559	—	—	—	—	—	—	—
Property and equipment, net	1,239	199,678	14,619	—	10,379	3,264	3,132	4,863	4,016
Other assets	35,422	89,181	6,090	—	4,297	1,112	1,598	218	988
Total assets	61,120	1,122,116	25,428	15,399	21,668	7,379	7,284	7,020	11,978
<b>Liabilities and Net Assets</b>									
Current liabilities:									
Accounts payable	1,481	39,379	1,525	56	2,005	645	580	867	902
Accrued expenses and other current liabilities	27,458	47,804	34,744	9,700	4,045	5,071	22,270	13,147	2,437
Current installments of long-term debt	—	64,813	—	—	2,769	5,676	—	—	224
Total current liabilities	28,939	151,996	36,269	9,756	8,819	11,392	22,850	14,014	3,563
Estimated professional and general liability costs	17,792	—	—	—	—	—	—	—	—
Long-term debt, excluding current installments	—	83,819	—	—	—	—	—	—	—
Fair value of interest rate swaps	—	6,405	—	—	—	—	—	—	—
Accrued pension cost	12,970	80,841	—	500	6,128	2,381	3,522	3,068	—
Other long-term liability	—	1,249	—	—	—	—	—	—	—
Deferred collection fee revenue	—	—	—	1,681	—	—	—	—	—
Total liabilities	59,701	324,310	36,269	11,937	14,947	13,773	26,372	17,082	3,563
Common stock	—	—	—	1	—	—	—	—	—
Net assets (deficit):									
Without donor restrictions	1,417	795,195	(11,038)	3,461	6,671	(6,486)	(19,183)	(10,114)	5,549
With donor restrictions	2	2,611	197	—	50	92	95	52	—
Total net assets (deficit) attributable to North Mississippi Health Services, Inc.	1,419	797,806	(10,841)	3,462	6,721	(6,394)	(19,088)	(10,062)	5,549
Noncontrolling interests	—	—	—	—	—	—	—	—	2,866
Total net assets (deficit)	1,419	797,806	(10,841)	3,462	6,721	(6,394)	(19,088)	(10,062)	8,415
Commitments and contingencies									
Total liabilities and net assets	\$ 61,120	1,122,116	25,428	15,399	21,668	7,379	7,284	7,020	11,978

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Consolidating Schedule – Balance Sheet Information

September 30, 2019

(with comparative 2018 consolidated information)

(In thousands)

Assets	Pontotoc	Acclaim,	North	North	Connected	North	Monroe	Eliminations	Total	
	Health Services, Inc.	Inc.	Mississippi Enterprises, Inc.	Mississippi Emergency Services, Inc.	Care, LLC	Mississippi Grand Ambulance	Health Services, Inc.		2019	2018
<b>Current assets:</b>										
Cash and cash equivalents	\$ 1,064	657	84	627	—	836	1,439	—	67,548	32,249
Investments	—	404	—	—	—	—	—	—	601,214	608,392
Net patient accounts receivable	2,287	—	—	229	—	1,091	7,919	(14,526)	96,344	146,628
Other current assets	479	198	1,844	36	—	72	2,575	—	44,282	38,896
Total current assets	3,830	1,259	1,928	892	—	1,999	11,933	(14,526)	809,388	828,165
Assets limited as to use	—	—	—	—	—	—	—	—	97,223	92,745
Property and equipment, net	1,418	7	—	23	—	1,623	11,836	—	256,097	260,995
Other assets	3,198	205	—	6	—	—	120	(85,774)	56,662	50,914
Total assets	8,446	1,471	1,928	921	—	3,623	23,889	(100,300)	1,219,370	1,232,819
<b>Liabilities and Net Assets</b>										
<b>Current liabilities:</b>										
Accounts payable	737	2	—	311	26	708	1,867	—	51,091	50,270
Accrued expenses and other current liabilities	3,102	281	917	89	1,127	3,082	13,660	(98,607)	90,327	91,552
Current installments of long-term debt	—	—	—	—	—	—	—	—	73,482	77,685
Total current liabilities	3,839	283	917	400	1,153	3,790	15,527	(98,607)	214,900	219,507
Estimated professional and general liability costs	—	—	—	—	—	—	—	—	17,792	18,287
Long-term debt, excluding current installments	—	—	—	—	—	—	—	—	83,819	77,987
Fair value of interest rate swaps	—	—	—	—	—	—	—	—	6,405	3,710
Accrued pension cost	2,779	—	—	—	—	1,105	—	—	113,294	73,258
Other long-term liability	—	—	—	—	—	—	—	—	1,249	—
Deferred collection fee revenue	—	—	—	—	—	—	—	(1,681)	—	—
Total liabilities	6,618	283	917	400	1,153	4,895	15,527	(100,288)	437,459	392,749
Common stock	—	1	10	—	—	—	—	(12)	—	—
Net assets (deficit):										
Without donor restrictions	1,704	1,187	1,001	521	(1,153)	(1,272)	8,362	—	775,822	833,944
With donor restrictions	124	—	—	—	—	—	—	—	3,223	3,188
Total net assets (deficit) attributable to North Mississippi Health Services, Inc.	1,828	1,188	1,011	521	(1,153)	(1,272)	8,362	(12)	779,045	837,132
Noncontrolling interests	—	—	—	—	—	—	—	—	2,866	2,938
Total net assets (deficit)	1,828	1,188	1,011	521	(1,153)	(1,272)	8,362	(12)	781,911	840,070
Commitments and contingencies										
Total liabilities and net assets	\$ 8,446	1,471	1,928	921	—	3,623	23,889	(100,300)	1,219,370	1,232,819

See accompanying independent auditors' report.

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Consolidating Schedule – Revenues and Expenses Information

September 30, 2019

(with comparative 2018 consolidated information)

(In thousands)

	North Mississippi Health Services, Inc.	North Mississippi Medical Center, Inc.	North Mississippi Medical Clinics, Inc. and subsidiaries	Tupelo Service Finance, Inc.	Clay County Medical Corporation	Webster Health Services, Inc.	Marion Regional Medical Center, Inc.	Tishomingo Health Services, Inc.	North Mississippi Joint Ventures, LLC and subsidiaries
Operating revenue:									
Net patient service revenue	\$ —	717,543	41,732	—	41,788	23,031	18,098	13,972	30,902
Other revenue	34,424	15,345	6,331	(27)	486	619	110	535	(88)
Total operating revenue	34,424	732,888	48,063	(27)	42,274	23,650	18,208	14,507	30,814
Operating expenses:									
Salaries and employee benefits	23,084	341,428	53,378	781	20,626	15,577	12,712	8,573	—
Supplies and other	7,391	317,721	17,580	804	17,263	7,133	7,026	5,873	20,415
Interest	—	4,439	—	—	41	94	—	—	97
Depreciation and amortization	254	38,425	1,760	1	1,410	927	903	657	905
Total operating expenses	30,729	702,013	72,718	1,586	39,340	23,731	20,641	15,103	21,417
Income from operations before electronic medical record costs	3,694	30,875	(24,655)	(1,613)	2,934	(81)	(2,433)	(595)	9,397
Electronic medical records implementation costs	—	1,891	1,763	—	177	175	118	8	—
Operating income	3,694	28,984	(26,418)	(1,613)	2,757	(256)	(2,551)	(603)	9,397
Nonoperating gains (losses):									
Investment return (loss)	—	25,777	—	—	—	—	—	—	—
Other nonoperating gains	102	(859)	756	1	470	17	41	10	84
Total nonoperating gains, net	102	24,918	756	1	470	17	41	10	84
Revenue, gains, and other support in excess of (less than) expenses and losses, before noncontrolling interests	3,796	53,902	(25,662)	(1,612)	3,227	(239)	(2,510)	(593)	9,481
Noncontrolling interests	—	—	—	—	—	—	—	—	(4,680)
Revenue, gains, and other support in excess of (less than) expenses and losses attributable to North Mississippi Health Services, Inc.	\$ 3,796	53,902	(25,662)	(1,612)	3,227	(239)	(2,510)	(593)	4,801

## NORTH MISSISSIPPI HEALTH SERVICES, INC. AND SUBSIDIARIES

Consolidating Schedule – Revenues and Expenses Information

September 30, 2019

(with comparative 2018 consolidated information)

(In thousands)

	Pontotoc Health Services, Inc.	Acclaim, Inc.	North Mississippi Enterprises, Inc.	North Mississippi Emergency Services, Inc.	Connected Care, LLC	North Mississippi Grand Ambulance	Monroe Health Services, Inc.	Eliminations	Total	
									2019	2018
Net patient service revenue	25,337	—	—	2,938	—	11,623	30,040	—	957,004	910,119
Other revenue	322	2,593	12,489	—	—	229	286	(50,232)	23,422	29,159
Total operating revenue	25,659	2,593	12,489	2,938	—	11,852	30,326	(50,232)	980,426	939,278
Operating expenses:										
Salaries and wages	16,226	1,058	107	841	90	7,886	15,744	(1,945)	516,166	504,246
Supplies	6,964	1,072	12,212	1,924	489	2,698	17,354	(50,518)	393,401	366,571
Interest	—	—	—	—	—	—	—	—	4,671	4,641
Depreciation and amortization	543	1	—	4	—	718	1,496	—	48,004	48,212
Total expenses	23,733	2,131	12,319	2,769	579	11,302	34,594	(52,463)	962,242	923,670
Income from operations before electronic medical record costs	1,927	462	170	169	(579)	550	(4,268)	2,231	18,184	15,608
Electronic medical records implementation costs	135	—	—	—	—	—	—	—	4,267	—
Operating income	1,792	462	170	169	(579)	550	(4,268)	2,231	13,917	15,608
Nonoperating gains (losses):										
Investment return (loss)	—	—	—	—	—	—	—	(2,231)	23,546	8,170
Other nonoperating gains	23	—	5	—	—	11	247	—	908	5,089
Total nonoperating gains, net	23	—	5	—	—	11	247	(2,231)	24,454	13,259
Revenue, gains, and other support in excess of (less than) expenses and losses, before noncontrolling interests	1,815	462	175	169	(579)	561	(4,021)	—	38,371	28,867
Noncontrolling interests	—	—	—	—	—	—	—	—	(4,680)	(3,766)
Revenue, gains, and other support in excess of (less than) expenses and losses attributable to North Mississippi Health Services, Inc.	\$ 1,815	463	175	169	(579)	561	(4,021)	—	33,691	25,101

See accompanying independent auditors' report.