
ProMedica Health System and Subsidiaries

**Consolidated Financial Report
with Supplemental Information
December 31, 2018 and 2017**

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Independent Auditor's Report

To the Board of Trustees
ProMedica Health System and Subsidiaries

We have audited the accompanying consolidated financial statements of ProMedica Health System and Subsidiaries (the "System"), which comprise the consolidated balance sheet as of December 31, 2018 and 2017 and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of ProMedica Health System and Subsidiaries as of December 31, 2018 and 2017 and the results of their operations and changes in net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 2 to the consolidated financial statements, the System adopted Accounting Standards Codification (ASC) Topic 606, *Revenue from Contracts with Customers*, using the modified retrospective adoption method, as of January 1, 2018 and ASC (Topic 958), *Presentation of Financial Statements of Not-for-Profit Entities*, using the retrospective adoption method, as of December 31, 2018. Our opinion is not modified with respect to these matters.

To the Board of Trustees
ProMedica Health System and Subsidiaries

Report on Summarized Comparative Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements that collectively comprise ProMedica Health System's consolidated financial statements. The consolidating balance sheet and consolidating statement of operations and changes in net assets are presented for the purpose of additional analysis and are not a required part of the consolidated financial statements. The consolidating balance sheet and consolidating statement of operations and changes in net assets are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audit 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 consolidating balance sheet and consolidating statement of operations and changes in net assets are fairly stated in all material respects in relation to the consolidated financial statements as a whole

Plante & Moran, PLLC

April 23, 2019

ProMedica Health System and Subsidiaries

Consolidated Balance Sheet

December 31, 2018 and 2017
(In Thousands)

	2018	2017
Assets		
Current Assets		
Cash and cash equivalents	\$ 325,496	\$ 294,030
Marketable securities (Note 18)	307,237	295,433
Assets limited as to use or restricted (Notes 6 and 18)	12,887	4,335
Accounts receivable - Net (Note 3)	642,307	255,472
Estimated third-party payor receivable	36,708	9,493
Supplies	31,812	26,247
Other current assets	146,448	122,158
Total current assets	1,502,895	1,007,168
Noncurrent Assets Limited as to Use or Restricted - Net of amount required to meet current obligations (Notes 6 and 18)		
Restricted funds	128,407	135,010
Bond indenture agreement funds	62,278	12
Professional liability and workers' compensation insurance funds	61,688	65,120
Internally designated for capital acquisition	633,726	1,111,149
Other segregated investments	251,206	254,826
Total noncurrent assets limited as to use or restricted	1,137,305	1,566,117
Property and Equipment - Net (Note 7)	1,608,895	1,345,046
Other Assets		
Goodwill (Note 8)	1,283,780	70,077
Pension (Note 14)	-	25,326
Intangible assets (Note 8)	69,785	55,081
Investments in affiliated companies (Note 23)	635,441	85,429
Other	94,026	62,899
Total other assets	2,083,032	298,812
Total assets	\$ 6,332,127	\$ 4,217,143

ProMedica Health System and Subsidiaries

Consolidated Balance Sheet (Continued)

December 31, 2018 and 2017
(In Thousands)

	2018	2017
Liabilities and Net Assets		
Current Liabilities		
Accounts payable and accrued expenses	\$ 435,845	\$ 207,503
Contractual current installments of long-term debt (Note 9)	23,203	96,350
Contingent current installments of long-term debt (Note 9)	446,444	457,409
Estimated third-party payor settlements	34,434	28,523
Accrued liabilities and other:		
Compensation and benefits	316,877	138,624
Professional liability and workers' compensation (Note 11)	111,535	7,353
Claims expense (Note 12)	108,562	81,423
Other current liabilities	8,385	3,664
Total current liabilities	1,485,285	1,020,849
Long-term Debt - Less current installments (Note 9)	1,902,158	429,012
Other Liabilities		
Accrued professional liability and workers' compensation - Less current portion (Note 11)	312,822	49,144
Deferred compensation (Note 14)	38,620	41,569
Pension (Note 14)	24,462	20,938
Other	70,786	67,187
Total other liabilities	446,690	178,838
Total liabilities	3,834,133	1,628,699
Net Assets		
Net assets without donor restrictions:		
Controlling interest	2,319,062	2,444,330
Noncontrolling interest	50,525	9,104
Total net assets without donor restrictions	2,369,587	2,453,434
Net assets with donor restrictions (Note 15)	128,407	135,010
Total net assets	2,497,994	2,588,444
Total liabilities and net assets	<u><u>\$ 6,332,127</u></u>	<u><u>\$ 4,217,143</u></u>

ProMedica Health System and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets

Years Ended December 31, 2018 and 2017

(In Thousands)

	2018	2017
Unrestricted Revenue, Gains, and Other Support		
Patient service revenue - Net of contractual and other allowances		\$ 1,655,458
Provision for bad debts		(96,233)
Net patient service revenue (Note 5)	\$ 2,991,905	1,559,225
Premium revenue	1,802,508	1,515,145
Other	122,948	64,817
Net assets released for use in operations	13,711	11,293
Total unrestricted revenue, gains, and other support	4,931,072	3,150,480
Expenses		
Salaries, wages, and employee benefits	1,949,787	1,068,022
Food and drugs	251,958	190,724
Medical expenses	1,317,511	1,004,059
Contracted fees	429,467	303,748
Supplies	241,227	198,138
Insurance	36,919	15,843
Utilities	57,561	26,016
Other	455,615	205,404
Total expenses (Note 17)	4,740,045	3,011,954
Operating Income before Depreciation and Amortization Expense	191,027	138,526
Depreciation and Amortization (Note 7)	147,732	130,897
Operating Income	43,295	7,629
Other (Loss) Income		
Interest expense	(48,324)	(34,423)
Investment (loss) income (Note 18)	(32,040)	210,787
Income tax expense (Note 16)	(7,519)	(4,458)
Inherent contribution (Note 24)	14,639	-
Loss on extinguishment of debt	(87)	(39,365)
Other	(6,198)	9,440
Total other (loss) income - Net	(79,529)	141,981
Excess of Revenue (Under) Over Expenses before Unusual Items	(36,234)	149,610
Restructuring, Severance, and Acquisition Costs (Note 2)	(30,237)	(15,085)
Excess of Revenue (Under) Over Expenses	\$ (66,471)	\$ 134,525

ProMedica Health System and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets (Continued)

Years Ended December 31, 2018 and 2017
(In Thousands)

	Net Assets without Donor Restrictions - Controlling Interest	Net Assets without Donor Restrictions - Noncontrolling Interest	Total Net Assets without Donor Restrictions	Net Assets with Donor Restrictions	Total
Net Assets - January 1, 2017	\$ 2,277,182	\$ 9,768	\$ 2,286,950	\$ 110,419	\$ 2,397,369
Excess of revenue over expenses	133,974	551	134,525	-	134,525
Restricted investment income	-	-	-	11,101	11,101
Restricted contributions and transfers - Net	-	-	-	32,303	32,303
Net assets released from restrictions for operations	-	-	-	(11,096)	(11,096)
Net assets released from restrictions for fixed assets	7,717	-	7,717	(7,717)	-
Noncontrolling interest in consolidated subsidiaries	273	(360)	(87)	-	(87)
Distributions to noncontrolling interests	-	(855)	(855)	-	(855)
Pension and other postretirement adjustments	25,184	-	25,184	-	25,184
Increase (decrease) in net assets	167,148	(664)	166,484	24,591	191,075
Net Assets - December 31, 2017	2,444,330	9,104	2,453,434	135,010	2,588,444
Excess of revenue (under) over expenses	(67,721)	1,250	(66,471)	-	(66,471)
Restricted investment loss	-	-	-	(6,545)	(6,545)
Restricted contributions and transfers - Net	-	-	-	17,611	17,611
Net assets released from restriction for operations	-	-	-	(13,711)	(13,711)
Net assets released from restriction for fixed assets	3,958	-	3,958	(3,958)	-
Capital contributions by noncontrolling members	-	41,173	41,173	-	41,173
Distributions to noncontrolling interests	-	(1,002)	(1,002)	-	(1,002)
Pension and other postretirement adjustments	(39,570)	-	(39,570)	-	(39,570)
Loss on discontinued operations (Note 25)	(21,935)	-	(21,935)	-	(21,935)
(Decrease) increase in net assets	(125,268)	41,421	(83,847)	(6,603)	(90,450)
Net Assets - December 31, 2018	\$ 2,319,062	\$ 50,525	\$ 2,369,587	\$ 128,407	\$ 2,497,994

ProMedica Health System and Subsidiaries

Consolidated Statement of Cash Flows

Years Ended December 31, 2018 and 2017

(In Thousands)

	2018	2017
Cash Flows from Operating Activities		
(Decrease) increase in net assets	\$ (90,450)	\$ 191,075
Adjustments to reconcile (decrease) increase in net assets to net cash from operating activities:		
Depreciation and amortization	147,732	130,897
Loss on sale of equipment	1,852	2,069
Loss on extinguishment of debt	87	39,365
Provision for bad debts	-	96,233
Asset impairment	1,958	616
Noncontrolling interests in acquisitions	(6,689)	87
Investment income including realized and unrealized gains	81,169	(186,424)
Distributions to noncontrolling interests	1,002	855
Restricted contributions and other	(17,611)	(32,303)
Changes in operating assets and liabilities that provided (used) cash - Net of business combinations:		
Accounts receivable and estimated third-party payor receivables	22,866	(119,850)
Supplies and other current assets	123,108	(21,995)
Other assets	(9,168)	18,224
Accounts payable and accrued expenses	(150,138)	(9,177)
Estimated third-party payor settlements	(26,012)	(10,115)
Pension	28,850	(45,401)
Other liabilities	70,866	(7,941)
Net cash provided by operating activities	179,422	46,215
Cash Flows from Investing Activities		
Acquisition of property and equipment	(310,279)	(341,638)
Proceeds from sale of equipment	1,078	3,248
Payments for business combinations - Net of cash acquired	(1,550,384)	(69,861)
Investments in joint ventures	(21,214)	(4,767)
Distributions from joint ventures	-	1,327
Purchase of investments	(2,653,009)	(3,009,559)
Proceeds from sale of investments	3,039,657	3,400,125
Decrease in total assets limited as to use or restricted	(59,361)	(39,651)
Net cash used in investing activities	(1,553,512)	(60,776)
Cash Flows from Financing Activities		
Proceeds from long-term debt	1,477,415	465,760
Repayment of long-term debt	(9,996)	(18,533)
Extinguishment of long-term debt	(75,090)	(389,100)
Payments on capital lease obligations	(3,382)	(3,657)
Distributions to noncontrolling interests	(1,002)	(855)
Restricted contributions and other	17,611	32,303
Net cash provided by financing activities	1,405,556	85,918
Net Increase in Cash and Cash Equivalents	31,466	71,357
Cash and Cash Equivalents - Beginning of year	294,030	222,673
Cash and Cash Equivalents - End of year	\$ 325,496	\$ 294,030
Supplemental Cash Flow Information		
Cash paid for interest - Net of amount capitalized	\$ 31,987	\$ 36,709
Cash paid for taxes	7,048	9,949
Acquisition of property through accounts payable	3,076	11,176

December 31, 2018 and 2017

Note 1 - Basis of Presentation and Affiliated Entities

ProMedica Health System (ProMedica), an Ohio not-for-profit corporation, and its subsidiaries (collectively, the "System") constitute a comprehensive healthcare system offering medical, surgical, psychiatric, rehabilitative, skilled nursing, home health, and hospice services across 27 states. The System includes a large employed physician group, practices, and insurance for health and dental coverage. ProMedica is the sole member or parent of the sole member of the following subsidiaries:

- The Toledo Hospital (Toledo), includes the accounts of Toledo Children's Hospital, Wildwood Orthopedic and Spine Hospital, and Flower Hospital (Flower)
- Fostoria Hospital Association (Fostoria)
- Defiance Hospital, Inc. (Defiance)
- Bay Park Community Hospital (Bay Park)
- Emma L. Bixby Medical Center (Bixby)
- Herrick Memorial Hospital, Inc. (Herrick)
- Lenawee Long Term Care
- Memorial Hospital (Memorial)
- Mercy Memorial Hospital Corporation (Monroe)
- ProMedica Physician Group (PPG)
- ProMedica Continuum Services (PCS)
- ProMedica Continuing Care Services Corp. (PCCSC)
- ProMedica Indemnity Corporation (Indemnity)
- ProMedica Foundation (Foundation)
- ProMedica Insurance Corporation (PIC)
- ProMedica Coldwater Regional Hospital (formerly Community Health Center of Branch County) (Coldwater)
- HCR ManorCare, Inc., and Subsidiaries (HCR)

Note 2 - Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the System and its controlled subsidiaries. Investments in entities not controlled by the System are reflected in the accompanying consolidated financial statements on the equity method. All significant intercompany transactions have been eliminated in the consolidated financial statements.

Investments in Affiliated Companies

Under the equity method, the investment is originally recorded at cost and is adjusted to recognize the System's share of the net earnings or losses of the affiliate as they occur. Losses are limited to the extent of the System's investments in, advances to, and guarantees for the entity.

Cash Equivalents

The System considers liquid investments, including money market accounts, with an original maturity of three months or less, exclusive of those whose use is limited or restricted, to be cash equivalents.

Investments

Marketable securities and assets limited as to use (held by trustees) primarily represent cash equivalents, commercial paper, bank notes, certificates of deposit, governmental securities, real estate, and equity securities. Marketable securities include cash and cash equivalents held by investment custodians, fixed-income securities, and equity securities.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheet. Purchases and sales of investments are accounted for as of the trade date, and sales are accounted for using the first-in, first-out method. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in the excess of revenue (under) over expenses, unless the income or loss is restricted by donor or law.

Based on the System's investment strategy and philosophies, management has elected to classify substantially all of its investments in equity securities with readily determinable fair values and investments in debt securities as trading securities.

Investment Risks

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

Derivative Financial Instruments

The System has limited involvement with derivative financial instruments and uses them only to manage well-defined interest rate risks.

Assets Limited as to Use or Restricted

Assets limited as to use or restricted include the restricted assets of the foundations and other subsidiaries of the System, assets held by trustees under indenture agreements and self-insurance trust arrangements, and assets set aside by the board of trustees for future capital improvements and other designated purposes.

Fair Value of Financial Instruments

The System follows the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820, *Fair Value Measurement*. This guidance defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The fair value hierarchy is as follows:

Level 1 - Quoted (unadjusted) prices for identical assets in active markets

Level 2 - Other observable inputs, either directly or indirectly, including:

- Quoted prices for similar assets in active markets
- Quoted prices for identical or similar assets in nonactive markets (few transactions, limited information, noncurrent prices, high variability over time, etc.)
- Inputs other than quoted prices that are observable for the asset (interest rates, yield curves, volatilities, default rates, etc.)
- Inputs that are derived principally from or corroborated by other observable market data

Level 3 - Unobservable inputs that cannot be corroborated by observable market data

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

Fair values of trading securities are based on quoted market prices, where available. The System obtains pricing for each security from investment managers and the custodian or a third-party pricing service (the "pricing service"), which generally uses Level 1 or Level 2 inputs for the determination of fair value in accordance with the fair value hierarchy. Security prices are normally derived through recently reported trades for identical or similar securities, making adjustments through the reporting date based upon available observable market information. For securities not actively traded, the pricing service may use quoted market prices of comparable instruments or discounted cash flow analyses, incorporating inputs that are currently observable in the markets for similar securities. Inputs that are often used in the valuation methodologies include, but are not limited to, nonbinding broker quotes, benchmark yields, credit spread, default rates, and prepayment spreads. As the System is responsible for the determination of fair value, it performs analyses on the prices received from the pricing service relative to the prices expected by the investment managers to determine whether the prices are reasonable estimates of fair value. As a result of these reviews, the System has not adjusted the prices obtained from the pricing service.

In instances where the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The System's assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including consideration of inputs specific to the asset. Investments measured at fair value using net asset value (NAV) per share practical expedient are not categorized within the fair value hierarchy.

Concentrations of Credit Risk

Financial instruments, which potentially subject the System to concentrations of credit risk, consist principally of cash and cash equivalents, marketable securities, patient accounts receivable, and assets limited as to use or restricted.

The System places its cash and cash equivalents with high-quality financial institutions. Concentration of credit risk with respect to marketable securities and assets limited as to use is restricted so that no one investment or group of similar investments, outside of those backed by the U.S. government, creates a significant concentration.

Concentration of credit risk relating to patient accounts receivable is limited to some extent by the diversity and number of the System's patients and payors. Patient accounts receivable consist of amounts due from governmental programs, commercial insurance companies, self-pay patients, and other group insurance programs. Excluding governmental programs, no one payor source represents more than 10 percent of the System's patient accounts receivable.

The U.S. Department of Justice and other federal agencies are increasing resources dedicated to regulatory investigations and compliance audits of healthcare providers. The System is subject to these regulatory efforts. Management is currently unaware of any regulatory matters that may have a material adverse effect on the System's consolidated financial position or results of operations.

Supplies

Supplies (e.g., drugs, medical, and surgical supplies) are stated at the lower of cost (average cost) and net realizable value.

Property and Equipment

Property and equipment acquisitions (including capitalized internal-use software) are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment under capital leases is amortized using the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the consolidated financial statements. Estimated useful lives for each of the categories of assets are as follows:

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

Land improvements	2-25 years
Buildings and improvements	2-40 years
Equipment	2-20 years

Impairment of Long-lived Assets and Long-lived Assets to be Disposed of

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell.

Asset Retirement Obligations

The fair value of the liability for legal obligations associated with asset retirements is recorded in the period in which it is incurred. When the liability is initially recorded, the cost of the asset retirement obligation is capitalized by increasing the carrying amount of the related long-lived asset. Over time, the liability, which is included in other long-term liabilities, is accreted to its present value, and the associated capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the consolidated statement of operations and changes in net assets.

Goodwill

The excess of purchase price over the fair value of net tangible and intangible assets of an entity acquired in a business combination is recorded as goodwill. The System tests goodwill annually for impairment as of December 31.

Intangible Assets

Intangible assets that have finite useful lives are amortized over said useful lives on a straight-line basis over periods ranging from 1 to 50 years. The System tests intangible assets, determined to have an indefinite useful life, annually for impairment as of December 31.

Accrued Claims

Accrued claims include estimates of the ultimate costs for both reported claims and claims incurred but not reported (IBNR).

Premium Deficiency Reserves

The reserve for premium deficiency, included in accrued claims, and the related expense are recognized when it is probable that expected future healthcare costs, under a group of existing contracts, will exceed future premiums and stop-loss coverage recoveries anticipated over the remaining term of the contract. The methods for making such estimates and for establishing the resulting reserves are periodically reviewed and updated. Any adjustments resulting therein are reflected in current operations. Estimates in reserves are subject to the impact of changes in the regulatory environment and economic conditions. Given the inherent variability of such estimates, the actual liability could differ significantly from the amounts provided. The System had no premium deficiency reserves accrued at December 31, 2018 and 2017.

Note 2 - Summary of Significant Accounting Policies (Continued)

Centers for Medicare & Medicaid Services (CMS) Payable

The System, through its wholly owned subsidiary, PIC, serves as a plan sponsor offering Medicare Part D prescription drug insurance coverage under a contract with CMS. In general, pharmacy benefits under Medicare Part D plans may vary in terms of coverage levels and out-of-pocket costs for beneficiary premiums, deductibles, and coinsurance. However, all Medicare Part D plans must offer either "standard coverage" or its actuarial equivalent (with out-of-pocket threshold and deductible amounts that do not exceed those of standard coverage). These "defined standard" benefits represent the minimum level of benefits required under law. Depending on the insurance risk, payments received by PIC for coverage under the Medicare Part D plan are recorded as net premium revenue or accrued claims.

In addition to defined standard plans, other prescription drug plans are offered containing benefits in excess of the standard coverage limits, in many cases, for an additional beneficiary premium. Pharmacy benefit costs and administrative costs under the contract are expensed as incurred and are recognized in medical expenses in the consolidated statement of operations and changes in net assets.

Accounts Receivable

Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges, reduced by explicit price concessions provided to third-party payors, discounts provided to qualifying individuals as part of our financial assistance policy, and implicit price concessions provided primarily to self-pay patients. Estimates for explicit price concessions are based on provider contracts, payment terms for relevant prospective payment systems, and historical experience adjusted for economic conditions and other trends affecting the System's ability to collect outstanding amounts.

For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the System records significant implicit price concessions in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

Revenue Recognition - Patient Service Revenue

Patient care service revenue is reported at the amount that reflects the consideration to which the System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others. The System determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payers, discounts provided to uninsured patients in accordance with the System's policy, and implicit price concessions provided to uninsured patients. The System determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. The System determines its estimate of implicit price concessions based on its historical collection experience with this class of patients. 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.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

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 an accurate depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in our hospitals receiving inpatient acute services or patients receiving services in our outpatient centers, senior living facilities, or other clinical settings. The System measures the performance obligation from admission into the hospitals, or the commencement of an outpatient service, senior living facilities, or other visit, to the point when it is no longer required to provide services to that patient under the contract, which is generally at the time of discharge or completion of the outpatient services, day of services at the senior living facilities, or other visit. Revenue for performance obligations satisfied at a point in time is generally recognized when goods are provided to patients and customers in a retail setting (for example, pharmaceuticals and medical equipment), and the System does not believe it is required to provide additional goods or services related to that sale.

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

Other Operating Revenue

Nonpatient service revenue consists of retail pharmacy, cafeteria, and other sales to patients, employees, and visitors; grants; gifts; rental income; unrestricted contributions; and other miscellaneous income.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management of the System to make assumptions, estimates, and judgments that affect the amounts reported in the consolidated financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. The System considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its consolidated financial statements, including, but not limited to, the following: recognition of net patient service revenue, which includes contractual allowances; provisions for bad debts and charity care; recorded values of investments and goodwill; reserves for losses and expenses related to healthcare professional and general liability; and risks and assumptions for measurement of pension and retiree medical liabilities. Management relies on historical experience and other assumptions believed to be reasonable in making its judgments and estimates. Actual results could differ materially from those estimates.

Charity Care

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

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

Premium Revenue and Medical Expenses

The System has certain agreements with various HMOs or through its wholly owned subsidiary, PIC, to provide medical services to subscribing participants. Premiums are recognized as income in the month that subscribing participants and enrollees are eligible to receive healthcare services. Medical expenses represent expenses incurred under contracts with healthcare providers; such costs are charged to expense in the month in which the service is rendered. These expenses include liabilities for reported claims and an estimate of IBNR claims using past experience adjusted for current trends.

CMS deploys a risk-adjustment model that apportions premiums paid to all health plans according to health severity and certain demographic factors. The CMS risk adjustment model pays more for members whose medical history indicates they have certain medical conditions. Under this risk adjustment methodology, CMS calculates the risk-adjusted premium payment using diagnosis data from hospital inpatient, hospital outpatient, and physician treatment settings. PIC and healthcare providers collect, capture, and submit the necessary and available diagnosis data to CMS within prescribed deadlines. PIC estimates risk adjustment revenue based upon the diagnosis data submitted and expected to be submitted to CMS.

Cost of Borrowing

Interest cost incurred on borrowed funds during the period of construction of capital assets, net of applicable interest income for tax-exempt borrowed funds, is capitalized as a component of the costs of acquiring those assets. Net capitalized interest was \$10,405,000 and \$7,077,000 in 2018 and 2017, respectively. Deferred debt financing costs are expensed over the life of the bonds using the bonds outstanding method.

Sick Pay Benefit

The System provides a sick time benefit to certain employees of Toledo, Bay Park, PCCSC, HCR, and the System's corporate staff. The benefit generally includes a capped payout provision at retirement or after attainment of a specified age or attendance level. The liability is an estimate based on the accrued benefits at year end, adjusted for expected employee turnover, and a discount rate of 3.25 percent and 2.75 percent for 2018 and 2017, respectively. At December 31, 2018 and 2017, the System recorded a liability of \$1,948,000 and \$2,333,000, respectively. Payments made under the program amounted to \$295,000 and \$865,000 for the years ended December 31, 2018 and 2017, respectively.

Income Taxes

Income taxes for the for-profit entities are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the consolidated financial statement carrying amounts of existing assets and liabilities and their respective tax basis, and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The System is subject to audit by various taxing authorities, and such audits could result in additional taxes. The System may, from time to time, engage in transactions in which the tax consequences are subject to uncertainty. Significant judgment is required in assessing and estimating the tax consequences of any such transactions. The System determines whether it is more likely than not that a tax position will be sustained upon examination based on the technical merits of the position. The System believes that the tax positions of its entities comply, in all material respects, with applicable tax law and that they have adequately provided for any reasonably foreseeable outcome related to these matters.

Note 2 - Summary of Significant Accounting Policies (Continued)

Excess of Revenue (Under) Over Expenses

The System's consolidated statement of operations and changes in net assets includes the performance indicator of excess of revenue (under) over expenses. Changes in net assets without donor restriction, which are excluded from excess of revenue (under) over expenses, consistent with industry practice, include contributions and investment income on restricted funds; pension and other postretirement adjustments; transfers of assets to and from affiliates for other than goods and services; contributions of long-lived assets (including assets acquired using contributions, which, by donor restriction, were to be used for the purposes of acquiring such assets); and changes in noncontrolling interests in consolidated subsidiaries.

Gifts and Net Assets with Donor Restrictions

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as net asset activity restricted by donors if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a purpose restriction is accomplished, net assets with donor restrictions are reclassified as net assets and reported in the consolidated statement of operations and changes in net assets. Donor-restricted contributions whose restrictions are met within the same year as received are also reported as net assets released from restrictions.

Regulatory Risk-based Capital and Statutory Deposit

PIC is subject to minimum risk-based capital and dividend approval requirements that were developed by the National Association of Insurance Commissioners (NAIC) and imposed by the Ohio Department of Insurance, Michigan Department of Insurance and Financial Services, and Indiana Department of Insurance. The formulas for determining the amounts of risk-based capital specify various weighting factors that are applied to financial balances or various levels of activity based on the perceived degree of risk. Regulatory compliance is determined by a ratio of the System's regulatory total adjusted capital, as defined by the NAIC, to its authorized control-level risk-based capital. Companies below specific trigger points or ratios are classified within certain levels, each of which requires specified corrective action. As of December 31, 2018 and 2017, it is management's opinion that PIC exceeds all required risk-based capital levels.

Cash and securities of PIC with a carrying value of \$9,412,000 and \$5,462,000 were on deposit with regulatory authorities at December 31, 2018 and 2017, respectively, and included in other assets in the consolidated balance sheet.

Related Party Transactions

Certain board members of the System own or manage corporations that provide services to the System. The System enters into transactions with related parties only upon terms comparable to those that would be available from unaffiliated third parties. Related party transactions are reviewed on a sample basis for fair market value by the audit and compliance department.

Unusual Items

The System has embarked on a cross-functional effort to improve and enhance its operating model, achieve long-term strategic objectives, and gain greater efficiencies. Costs related to this effort of \$16,814,000 and \$15,085,000 for the years ended December 31, 2018 and 2017, respectively, are included in restructuring, severance, and acquisition costs in the consolidated statement of operations and changes in net assets.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

The System acquired HCR ManorCare in a debt financed acquisition. Certain costs associated with the acquisition of \$13,423,000 for the year ended December 31, 2018 are included in restructuring, severance, and acquisition costs in the consolidated statement of operations and changes in net assets. There were no debt financed acquisition costs in 2017.

Adopted Accounting Pronouncement

Effective January 1, 2018, the System adopted FASB Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (ASU 2014-09), using a modified retrospective method of application to all contracts existing on January 1, 2018. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The adoption of ASU 2014-09 resulted in changes to the System's presentation for disclosure of revenue primarily related to uninsured or underinsured patients. Prior to the adoption of ASU 2014-09, a significant portion of the System's provision for doubtful accounts related to self-pay patients, as well as co-pays, co-insurance, and amounts and deductibles owed by patients with insurance. Under ASU 2014-09, the estimated uncollectable amounts due from these patients are generally considered implicit price concessions that are a direct reduction to operating revenue, with a corresponding material reduction in the amounts presented separately as provision for doubtful accounts. For the year ended December 31, 2018, the System recorded approximately \$154,583,000 of implicit price concessions as a direct reduction of patient service revenue that would have been recorded as provision for doubtful accounts prior to the adoption of ASU 2014-09. The adoption of ASU 2014-09 also resulted in changes to the System's presentation and disclosure of customer contract assets and liabilities and the assessment of variable consideration under customer contracts, which are further discussed in Note 3.

As of December 31, 2018, the System adopted ASU No. 2016-14, *Not-for-Profit Entities*. This standard requires net assets to be classified in two categories, net assets without donor restrictions and net assets with donor restrictions, rather than the three previous classifications. In addition, the underwater portion of donor-restricted endowments is now reported as net assets with donor restrictions. This standard also requires changes in the way certain information is aggregated and reported by the System, including disclosures of quantitative and qualitative information about the liquidity and availability of resources and the presentation of expenses by both functional and natural classification. The standard also clarifies the definition of management and general and prohibits certain expenses from being allocated out of management and general. As a result of the adoption of this standard, the financial information for the year ended December 31, 2017 has been restated, as follows: management and general expenses has increased \$62,362,000 from the amount previously reported, fundraising increased by \$5,466,000, with a corresponding decrease in program expenses. Additionally, net assets of \$39,660,000 previously reported as permanently restricted net assets and net assets of \$95,350,000 previously reported as temporarily restricted net assets have been combined into net assets with donor restrictions.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 2 - Summary of Significant Accounting Policies (Continued)

Upcoming Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which will supersede the current lease requirements in ASC 840. This guidance requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the consolidated statement of operations and changes in net assets. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The guidance in ASU No. 2016-02 will be effective for the System beginning January 1, 2019 and will be applied using a modified retrospective transition method to either the beginning of the earliest period presented or the year of adoption. The new lease standard is expected to have a significant impact on the System's consolidated balance sheet resulting from the System's operating leases, as disclosed in Note 20, which will be reported on the consolidated balance sheet upon adoption. At adoption, the System will recognize a lease liability and corresponding right-to-use asset based on the present value of the minimum lease payments. The effects on the results of operations are not expected to be significant, as recognition and measurement of expenses and cash flows for leases will generally be consistent with current guidance.

In March 2017, the FASB issued ASU No. 2017-07, *Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This guidance requires the presentation of the service cost component of net benefit cost to be in the same line item as other compensation costs arising from services rendered by the pertinent employees during the period. All other components of net benefit cost should be presented separately from the service cost component and outside of income from operations. The guidance in ASU No. 2017-07 is effective for the System beginning January 1, 2019. The System is currently evaluating the impact this guidance may have on its consolidated financial statements.

Note 3 - Accounts Receivable

The aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period is \$11,482,000 at December 31, 2018, which would be classified as a contract asset. These amounts are reported as a component of accounts receivable. 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.

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

	2018	2017
Commercial and other payors	27 %	41 %
Medicare	34	25
Self-pay	14	18
Medicaid	25	16
Total	100 %	100 %

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 4 - Charity Care

The System maintains records to identify and monitor the level of direct patient charity care it provides. These records include the charges forgone for services and supplies furnished under its charity care policy and equivalent service statistics. During 2018 and 2017, gross charges forgone, based on established rates, approximated \$61,397,000 and \$59,804,000, respectively. The cost of charity care provided approximated \$9,989,000 and \$11,076,000 in 2018 and 2017, respectively.

The System calculates a cost-to-charge ratio of adjusted total costs to gross charges for each subsidiary then reduces this by supplemental payments to determine the aggregate System cost of charity care.

In addition to providing direct patient charity care, the System demonstrates its exempt purpose to benefit the community by operating emergency rooms that are open to the public, regardless of ability to pay, 24 hours a day, seven days per week. Additionally, ProMedica offers urgent care facilities for non-life threatening emergencies and a telehealth option for patients to speak to a physician using their computer or mobile device. Through its academic affiliation, the System provides facilities for the education and training of healthcare professionals and the development of an academic medical center, while maintaining research programs for the study of new patient procedures, drugs, and innovative medical devices that offer the promise of improving health care. The System also provides community health services, such as free or low-cost clinics, including the Hemophilia Clinic and the Heart Failure Clinic; women's health programs, such as free or low-cost mammograms; and multiple health promotion and wellness programs, such as lectures at local senior centers, free public health and infant mortality screenings; and services to combat hunger, including food reclamation and food clinic program for patients who screen positive for food insecurity. The ProMedica Ebeid Institute for Population Health (the "Institute") is committed to building healthy communities and includes Market on the Green, a full-service grocery that provides nutritious meal options to residents in a designated food desert. The Institute also provides cooking and nutrition classes as well as financial counseling services through its financial opportunity center. As part of its efforts to combat food insecurity, the System also partners with the Lenawee Health Network to bring fresh produce to Lenawee County, Michigan residents from August through October with the Veggie Mobile. Additionally, the ProMedica Ebeid Promise initiative has been developed to address social determinants of health and create a model for neighborhood revitalization. This model focuses on improving health outcomes, providing stable housing, increasing access to educations opportunities and offering job training opportunities. At HCR ManorCare, through grants from the Hospice Memorial Fund, grief camps for children and adults are offered, as well as educational sessions and life celebration events. The Fund also provides stabilizing resources for hospice patients and families in financial distress due to the lack of or reduction in income from a terminal illness or disease. Skilled nursing and rehabilitation facilities provide home assessments and community resources for safe and healthy living for older adults. In some markets, the centers also partner with local food organizations to ensure patients return home with a healthy meal. The System also subsidizes necessary health services, including emergency and medically necessary care, Neonatal Intensive Care, Children's Safe Harbor, the Cystic Fibrosis Center, and Autism Center, as well as diabetes treatment and support services at the ProMedica Mary Ellen Falzone Diabetes Center.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 5 - Net Patient Service Revenue

Patient service revenue, net of contractual allowances, discounts and the provision for bad debts, generated by major payor source for the years ended December 31, 2018 and 2017 is as follows (in thousands):

	<u>2018</u>	<u>2017</u>
Medicare	\$ 1,343,791	\$ 640,614
Medicaid	721,349	329,305
Commercial and other payors	771,786	566,078
Self-pay	154,979	23,228
	<u>\$ 2,991,905</u>	<u>\$ 1,559,225</u>
Total	<u>\$ 2,991,905</u>	<u>\$ 1,559,225</u>

The composition of patient care service revenue based on its lines of business and timing of revenue recognition for the year ended December 31, 2018 and 2017 (in thousands):

	<u>2018</u>	<u>2017</u>
Service lines:		
Hospital	\$ 1,372,776	\$ 1,262,388
Nursing home and senior care	986,497	17,205
Physician services	203,988	185,443
Home health and hospice	310,186	36,522
Other	118,458	57,667
	<u>\$ 2,991,905</u>	<u>\$ 1,559,225</u>
Total	<u>\$ 2,991,905</u>	<u>\$ 1,559,225</u>
Timing of revenue recognition:		
At time services are rendered	\$ 56,396	\$ 62,787
Over time services are transferred	2,935,509	1,496,438
	<u>\$ 2,991,905</u>	<u>\$ 1,559,225</u>
Total	<u>\$ 2,991,905</u>	<u>\$ 1,559,225</u>

Certain subsidiaries of the System have agreements with third-party payors that provide for payment to the System at amounts different from its established rates. A summary of the payment arrangements with major third-party payors is as follows:

Commercial and other - Certain subsidiaries of the System have also entered into payment agreements with certain commercial insurance carriers, HMOs, and preferred provider organizations. The basis for payment under these agreements includes capitation fees, prospectively determined rates per discharge or per diem, and discounts from established charges.

Medicare - Inpatient acute care, psychiatric, and rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Critical Access Hospitals (Defiance, Fostoria, and Herrick) and medical education costs are reimbursed at prospective rates, but traditional Medicare payments are later settled during the annual cost reporting process. Outpatient services are paid based upon either the Ambulatory Payment Classification (APC) methodology or a prospectively determined fee schedule for therapy and laboratory services. Under APCs, the hospital is paid a prospectively determined rate based on the procedures provided to patients. Outpatient services are reimbursed based upon either the Enhanced Ambulatory Payment Group (EAPG) methodology or prospectively determined fee schedules.

Medicaid - Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. Outpatient services are reimbursed based upon prospectively determined fee schedules.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 5 - Net Patient Service Revenue (Continued)

Program examination of cost reports has been finalized for various facilities with dates ranging from 2015 to 2017 for the Medicare program and with dates ranging from 2011 to 2017 for the Medicaid program. Cost reports for the Blue Cross Blue Shield program (Michigan providers only) have been finalized through 2017. Provisions for estimated reimbursement adjustments have been made in the accompanying consolidated financial statements.

System hospitals participate in various state supplemental payment programs designed to assist hospitals that have a disproportionate amount of uncompensated care. Ohio hospitals (Toledo, Defiance, Fostoria, Bay Park, Flower, and Memorial) participate in the Hospital Care Assurance and Medicaid Supplemental Payments programs. Michigan hospitals (Bixby, Herrick, Monroe, and Coldwater) participate in the Disproportionate Share Hospital Payment and Quality Assurance Assessment programs. During 2018 and 2017, the System received distributions of approximately \$56,013,000 and \$51,308,000, respectively. All hospitals are subject to assessments used to fund state supplemental payment programs. During 2018 and 2017, the System incurred assessments of approximately \$38,062,000 and \$35,396,000, respectively.

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

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 (that is, new information becomes available), or as years are settled or are no longer subject to such audits, reviews, and investigations. As a result, there is at least a reasonable possibility that recorded estimates could change in the near term. In 2018 and 2017, such changes in estimates increased patient service revenue, net of contractual and other allowances, by approximately \$13,006,000 and \$17,349,000, respectively.

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. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. For the years ended December 31, 2018 and 2017, changes in its estimates of implicit price concessions, discounts, and contractual adjustments for performance obligations satisfied in prior years were not significant. 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.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 5 - Net Patient Service Revenue (Continued)

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 (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts the System expects to collect based on its collection history with those patients.

Note 6 - Assets Limited as to Use or Restricted

As of December 31, 2018 and 2017, restricted assets of the foundations and other subsidiaries of the System, assets held by trustees under indenture agreements and self-insurance trust arrangements, and assets set aside by the board of trustees for future capital improvements and other designated purposes consisted of the following (in thousands):

	2018	2017
Cash and cash equivalents	\$ 88,252	\$ 6,019
Equity securities	401,188	769,962
Fixed-income securities	487,826	572,270
Long-short equity hedge funds	56,133	72,920
Real return strategy funds	47,791	79,355
Real estate	13,581	8,428
Beneficial interest in perpetual trusts	29,788	32,096
Other	25,633	29,402
Total	<u>\$ 1,150,192</u>	<u>\$ 1,570,452</u>

Assets limited as to use, which are required for obligations classified as current liabilities, are reported in current assets.

Note 7 - Property and Equipment

Property and equipment as of December 31, 2018 and 2017 consisted of the following (in thousands):

	2018	2017
Land and improvements	\$ 157,037	\$ 149,717
Building and improvements	1,469,007	1,331,801
Equipment	1,015,045	883,743
Construction in progress	388,817	277,785
Total cost	3,029,906	2,643,046
Less accumulated depreciation and amortization	1,421,011	1,298,000
Property and equipment - Net	<u>\$ 1,608,895</u>	<u>\$ 1,345,046</u>

Property and equipment includes assets recorded under capital leases of \$38,826,000 and \$18,820,000 with accumulated amortization for such assets of \$9,917,000 and \$6,514,000 as of December 31, 2018 and 2017, respectively. The associated charges to income are recorded in depreciation and amortization expense.

As of December 31, 2018 and 2017, construction contract commitments of \$134,285,000 and \$182,434,000, respectively, exist for the construction and remodeling of System facilities.

ProMedica Health System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 8 - Goodwill and Intangible Assets

Intangibles as of December 31, 2018 and 2017 consisted of the following (in thousands):

	Average Life (Years)	2018 Gross			2017 Gross		
		Carrying Amount	Accumulated Amortization	Net	Carrying Amount	Accumulated Amortization	Net
Amortized intangible assets:							
Physician charts	10	\$ 1,446	\$ (1,214)	\$ 232	\$ 1,446	\$ (1,078)	\$ 368
Customer relationships	5-50	58,442	(6,925)	51,517	40,147	(4,213)	35,934
Other	1-15	7,738	(3,669)	4,069	7,671	(2,840)	4,831
Total		<u>\$ 67,626</u>	<u>\$ (11,808)</u>	<u>\$ 55,818</u>	<u>\$ 49,264</u>	<u>\$ (8,131)</u>	<u>\$ 41,133</u>

	2018	2017
	Gross Carrying Amount	Gross Carrying Amount
Carrying amount of intangible assets not subject to amortization:		
Goodwill	\$ 1,283,780	\$ 70,077
Intangibles not subject to amortization	13,967	13,948
Total	<u>\$ 1,297,747</u>	<u>\$ 84,025</u>

During 2018, the System recorded provisional goodwill of \$1,184,364,000 related to acquisition of HCR. The goodwill amount is provisional pending the finalization of the fair value of certain acquired intangible assets, as described in Note 24. Additionally, during 2018, the System recorded goodwill of \$30,060,000 related to ProMedica Pathology Labs, LLC.

Aggregate amortization expense for the years ended December 31, 2018 and 2017 was \$3,748,000 and \$924,000, respectively.

Estimated amortization expense for each of the next five years and thereafter are as follows (in thousands):

Years Ending	Amount
2019	\$ 4,273
2020	3,362
2021	3,216
2022	2,900
2023	2,900
Thereafter	39,167
Total	<u>\$ 55,818</u>

Note 9 - Debt

Long-term debt as of December 31, 2018 and 2017, net of unamortized bond discount, premium, and debt issuance costs, consisted of the following (in thousands):

	2018	2017
Hospital Revenue Bonds - Series 2018A, interest at 2.72 to 5.25 percent payable semiannually	\$ 259,055	\$ -
Taxable Bonds - Series 2018B, interest at 5.33 to 6.02 percent payable semiannually	1,202,276	-
Hospital Revenue Bonds - Series 2017A, interest at 2.72 percent payable monthly	54,594	54,554

ProMedica Health System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 9 - Debt (Continued)

	2018	2017
Hospital Revenue Bonds - Series 2017B, interest at 2.72 percent payable monthly	\$ 119,897	\$ 119,858
Hospital Revenue Bonds - Series 2017C, interest at 2.90 percent payable monthly	84,867	84,828
Hospital Revenue Bonds - Series 2017D, interest at 3.12 percent payable monthly	39,670	39,648
Hospital Revenue Bonds - Series 2017F, based on the 30-day London InterBank Offered Rate (LIBOR) index and interest payable monthly. (2.93 percent as of December 31, 2018)	62,413	62,383
Hospital Revenue Bonds - Series 2017G, interest based on Securities Industry and Financial Market Association (SIFMA) and payable monthly (1.72 percent as of December 31, 2017)	-	79,883
Hospital Refunding Revenue Bonds - Series 2017H, interest at 3.02 percent payable monthly	24,837	24,809
Taxable Bonds - Series 2015A, interest at 4.98 percent payable semiannually	270,483	270,389
Hospital Revenue Bonds - Series 2015B, interest at 4.00 percent payable semiannually	45,222	45,165
Taxable Hospital Refunding Revenue Bonds - Series 2015C, based on the 30-day LIBOR index and interest payable monthly (3.08 percent as of December 31, 2018)	14,506	19,125
Taxable Bonds - Series 2015E, based on the 30-day LIBOR index and interest payable monthly (3.13 percent as of December 31, 2018)	32,978	34,912
Hospital Refunding Revenue Bonds - Series 2011D, interest at 4.00 to 5.25 percent payable semiannually	96,089	97,309
Qualified Low-Income Community Investment Loans - 2015, interest at 1.00 to 2.58 percent, payable quarterly	14,379	14,365
Capital lease obligations	29,357	14,663
Other	21,182	20,880
Total	2,371,805	982,771
Less current installments of long-term debt, net of current portion of unamortized bond discount, premium, and debt issuance costs - Contractual current installments	23,203	96,350
Contingent current installments	446,444	457,409
Total	\$ 1,902,158	\$ 429,012

Certain subsidiaries of the System are participants in a Master Trust Indenture (the "Indenture"), amended and restated as of October 1, 2018, pursuant to which the System's revenue bonds are general obligations of the ProMedica Healthcare Obligated Group (the "Obligated Group"). The Obligated Group consists of the following subsidiaries: Toledo, Bay Park, Defiance, Fostoria, Bixby, Herrick, Memorial, Monroe, PCCSC, and Lenawee Long Term Care.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 9 - Debt (Continued)

The bonds were issued by the County of Lucas, Ohio (Lucas County) and the County of Lenawee, Michigan and are payable solely pursuant to related loan agreements or leases between the borrowing subsidiaries and the issuing authority. The Indenture and related loan agreements and leases require compliance with certain financial covenants each year by the Obligated Group. The Obligated Group has complied with the requirements of the financial covenants each year.

In connection with the issuance of the revenue bonds through Lucas County, the Ohio members of the Obligated Group have entered into a lease agreement (the "Lease") to lease its hospital facilities to, and lease back its hospital facilities from, Lucas County. Pursuant to the Lease, the Obligated Group agrees to make payments of basic rent in amounts sufficient to pay the principal and interest on the Lucas County revenue bonds issued for the benefit of the Obligated Group.

Hospital Revenue Bonds - 2018A

In October 2018, the Obligated Group issued \$253,315,000 of tax-exempt fixed rate bonds, Series 2018A through Lucas County. At December 31, 2018, outstanding bonds consist of \$8,825,000 serial bonds that matures on November 15, 2019, \$24,915,000 term bonds that mature on November 15, 2042, and \$219,575,000 term bonds that mature on November 15, 2048. The proceeds of the Series 2018A bonds were used to refinance the 2011C and 2017G bonds with the remainder used for the construction and equipping certain healthcare facilities of the Obligated Group located in Ohio. Balances reported at December 31, 2018 include unamortized bond premium of \$8,125,000 and unamortized debt issuance costs of \$2,385,000.

Taxable Bonds - 2018B

In October 2018, the Obligated Group issued \$1,219,845,000 in fixed rate taxable bonds, Series 2018B. The bonds mature \$319,845,000 on November 15, 2028, \$500,000,000 on November 15, 2038, and \$400,000,000 on November 15, 2048. The proceeds of the Series 2018B bonds were used to refinance the 2018 bridge loan used to finance the HCR ManorCare acquisition and for other authorized corporate purposes of the System's subsidiaries. Balances reported at December 31, 2018 include unamortized bond premium of \$16,615,000 and unamortized debt issuance costs of \$34,185,000.

Hospital Revenue Bonds - 2017A

In December 2017, the Obligated Group issued \$54,710,000 in fixed rate bonds, Series 2017A, through Lucas County with a direct placement bank loan with a base term of four years. The Series 2017A bond direct loan is included in contingent current installments of long-term debt at December 31, 2018 based on certain subjective acceleration definitions within the agreement. The proceeds from the 2017A bonds were used to advance refund the Series 2008D bonds. At December 31, 2018, outstanding bonds consist of \$54,710,000 that mature in increasing amounts from \$6,480,000 on November 15, 2035 to \$6,970,000 on November 15, 2040. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$116,000 and \$156,000, respectively.

Hospital Revenue Bonds - 2017B

In December 2017, the Obligated Group issued \$120,010,000 in fixed rate bonds, Series 2017B, through Lucas County with a direct placement bank loan with a base term of four years. The Series 2017B bond direct loan is included in contingent current installments of long-term debt at December 31, 2018 based on certain subjective acceleration definitions within the agreement. The proceeds from the 2017B bonds were used to advance refund a portion of the Series 2011A bonds. At December 31, 2018, outstanding bonds consist of \$120,010,000 that mature in increasing amounts from \$2,385,000 on November 15, 2022 to \$19,080,000 on November 15, 2041. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$113,000 and \$152,000, respectively.

Note 9 - Debt (Continued)

Hospital Revenue Bonds - 2017C

In December 2017, the Obligated Group issued \$84,980,000 in fixed rate bonds, Series 2017C, through Lucas County with a direct placement bank loan with a base term of four years. The Series 2017C bond direct loan is included in contingent current installments of long-term debt at December 31, 2018 based on certain subjective acceleration definitions within the agreement. The proceeds from the 2017C bonds were used to advance refund a portion of the Series 2011A bonds. At December 31, 2018, outstanding bonds consist of \$84,980,000 that mature in increasing amounts from \$1,685,000 on November 15, 2022 to \$13,520,000 on November 15, 2041. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$113,000 and \$152,000, respectively.

Hospital Revenue Bonds - 2017D

In December 2017, the Obligated Group issued \$39,800,000 in fixed rate bonds, Series 2017D, through Lucas County with a direct placement bank loan with a base term of seven years. The Series 2017D bond direct loan is included in contingent current installments of long-term debt at December 31, 2018 based on certain subjective acceleration definitions within the agreement. The proceeds from the 2017D bonds were used to advance refund a portion of the Series 2011D bonds. At December 31, 2018, outstanding bonds consist of \$39,800,000 that mature in increasing amounts from \$820,000 on November 15, 2022 to \$6,090,000 on November 15, 2029. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$130,000 and \$152,000, respectively.

Hospital Revenue Bonds - 2017F

In December 2017, the Obligated Group issued \$62,500,000 in variable rate bonds, Series 2017C, through Lucas County with a direct placement bank loan with a base term of four years. The Series 2017F bond direct loan is included in contingent current installments of long-term debt at December 31, 2018 based on certain subjective acceleration definitions within the agreement. The proceeds from the 2017F bonds were used to refinance the Series 2008A bonds. At December 31, 2018, outstanding bonds consist of \$62,500,000 that mature in increasing amounts from \$11,600,000 on November 15, 2030 to \$13,450,000 on November 15, 2034. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$87,000 and \$117,000, respectively.

Hospital Revenue Bonds - 2017G

Series 2017G were extinguished in October 2018 using proceeds from the Series 2018A Bonds. In December 2017, the Obligated Group issued \$80,000,000 in variable rate bonds, Series 2017G, through Lucas County with a direct placement bank loan with a base term of one year. The Series 2017G bonds are included in contractual current installments of long-term debt at December 31, 2017. The proceeds from the 2017G bonds were used to finance the construction of certain healthcare facilities of the Obligated Group located in Ohio. Balances reported at December 31, 2017 include unamortized debt issuance costs of \$117,000.

Hospital Refunding Revenue Bonds - 2017H

In December 2017, the Obligated Group issued \$24,945,000 in fixed rate bonds, Series 2017H, through the County of Lenawee Hospital Financing Authority with a direct placement bank loan with a base term of four years. The Series 2017H bond direct loan is included in contingent current installments of long-term debt at December 31, 2018 based on certain subjective acceleration definitions within the agreement. The proceeds from the 2017H bonds were used to advance refund a portion of the Series 2011B and 2011E bonds. At December 31, 2018, outstanding bonds consist of \$24,945,000 that mature in increasing amounts from \$690,000 on November 15, 2022 to \$6,450,000 on November 15, 2035. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$108,000 and \$136,000, respectively.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 9 - Debt (Continued)

Taxable Bonds

Series 2015A, with an outstanding principal of \$273,000,000 at December 31, 2018, was issued in September 2015. The taxable fixed rate bonds mature on November 15, 2045 and are subject to optional redemption prior to maturity. The proceeds of the Series 2015A bonds were used for authorized corporate purposes of the System's subsidiaries, including financing or refinancing capital expenditures and paying current operating expenditures. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$2,517,000 and \$2,611,000, respectively.

Hospital Revenue Bonds

Series 2015B, with an outstanding principal of \$46,755,000 at December 31, 2018, was issued in September 2015 and consists of tax-exempt fixed rate bonds. The bonds mature on November 15, 2045 and are subject to optional redemption prior to maturity. The proceeds of the Series 2015B bonds were used for acquiring and improving healthcare facilities in Ohio. Balances reported at December 31, 2018 and 2017 include unamortized bond discount of \$1,047,000 and \$1,086,000, respectively, and debt issuance costs of \$486,000 and \$504,000, respectively.

Taxable Hospital Revenue Refunding Bonds

Series 2015C, with an outstanding principal of \$14,550,000 at December 31, 2018, was issued in November 2015 as a taxable directly placed bank loan with a base term of six years. Principal payments are due annually and range from \$4,740,000 due on November 15, 2019 to \$4,960,000 due in 2021. The contractual current portion of the Series 2015C bonds is \$4,740,000 at December 31, 2018 with the remaining \$9,810,000 included in contingent current installments of long-term debt based on certain subjective acceleration definitions within the agreement. The proceeds of the Series 2015C bonds were used to extinguish the Hospital Refunding Revenue Bonds - Series 2005B. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$44,000 and \$60,000, respectively.

Taxable Bonds

Series 2015E, with an outstanding principal of \$33,055,000 as of December 31, 2018, was issued in November 2015 as a taxable directly placed bank loan with a base term of 10 years. Principal payments range from \$1,945,000 due on November 15, 2019 to \$21,385,000 in 2025. The contractual current portion of the Series 2015E bonds is \$1,945,000 at December 31, 2018, with the remaining \$31,110,000 included in contingent current installments of long-term debt based on certain subjective acceleration definitions within the agreement. The proceeds of the Series 2015E bonds were used to pay off a temporary bank line of credit that was used to extinguish the Monroe Hospital Finance Authority 2006 Revenue and Refunding bonds. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$77,000 and \$88,000, respectively.

Hospital Refunding Revenue Bonds

Series 2011D was partially refunded in December 2017 using the proceeds from the Series 2017D bonds. The remaining outstanding principal of \$93,895,000 at December 31, 2018 consists of bonds, which mature in varying amounts from \$1,090,000 due on November 15, 2019 to \$880,000 in 2030. Balances reported at December 31, 2018 and 2017; include unamortized bond premium of \$2,829,000 and \$3,067,000, respectively, and debt issuance costs of \$635,000 and \$688,000, respectively. In December 2011, the Obligated Group issued the fixed rate bonds through Lucas County. The proceeds from the Series 2011D Bonds were used to extinguish the remaining maturities of Series 1999 Hospital Revenue Bonds that were not refunded with Series 2011C issuance.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 9 - Debt (Continued)

Qualified Low-income Community Investment (QLICI) Loans

The 2015 loans, with an outstanding principal balance of \$14,740,000 at December 31, 2018, mature in December 2045 and were issued to finance the acquisition and rehabilitation of the System’s corporate headquarters. The loans require quarterly interest-only payments through December 2022, with principal and interest payments beginning thereafter until the loans mature. The loans are included in contingent current installments of long-term debt based on certain subjective acceleration definitions within the loan agreement. Balances reported at December 31, 2018 and 2017 include unamortized debt issuance costs of \$361,000 and \$375,000, respectively.

Capital Lease

Capital lease obligations consist of property, equipment, and information technology leases.

Other

Other long-term debt consists of additional bonds, a Jobs Ohio Revitalization loan, an equipment loan and a note payable.

The table below indicates the future maturities on long-term debt at December 31, 2018. While presentation in the consolidated balance sheet of current maturities of long-term debt includes certain amounts contingently payable, the schedule below has been prepared based on contractual maturities of the debt outstanding at December 31, 2018. Accordingly, if covenants are violated, debt repayments may become more accelerated than presented below (in thousands):

Years Ending	Amount
2019	\$ 23,203
2020	19,771
2021	18,832
2022	26,311
2023	23,068
Thereafter	2,260,620
Total	<u>\$ 2,371,805</u>

Note 10 - Derivatives

In 2004, the System entered into a forward starting interest rate swap agreement with an outstanding notional amount of \$62,500,000. The swap originally effectively converted a portion of the Series 2005A auction rate securities to a synthetic fixed rate of 3.643 percent. The swap converted \$62,500,000 of the Series 2017F debt to synthetic fixed and has an expiration date of November 15, 2034. This variable-to-fixed swap arrangement was not designated as a hedge. The swap was terminated in July 2018. The fair value of this derivative at December 31, 2017 was \$17,332,000.

The System also had an interest rate swap agreement, not designated as a hedge, which was terminated in 2017. The interest rate swap was scheduled to mature on January 1, 2019. During the term of the agreement, the swap in effect converted variable rate debt to fixed rate debt. The agreement entitled Toledo, on a monthly basis, to pay a fixed rate of 5.765 percent, in return for receiving a rate based upon a 30-day commercial paper index. The gain recognized during the year ended December 31, 2017 was \$113,000.

Any gains or losses recognized on derivatives that are not designated as hedging instruments are recognized in current year earnings.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 11 - Estimated Self-insurance Costs

Certain subsidiaries of the System are self-insured or are insured by Indemnity up to certain amounts for the purpose of providing for workers' compensation, medical malpractice claims, general liability, and property coverage. There are known claims and incidents that may result in the assertion of additional claims, as well as claims from unknown incidents. Professional insurance consultants have been retained to determine appropriate funding requirements and medical malpractice and workers' compensation liabilities. The amounts funded have been placed in self-insurance fund accounts, which are reported in assets limited as to use or restricted in the accompanying consolidated balance sheet.

The System has recorded a medical malpractice liability of \$365,304,000 and \$48,549,000 at December 31, 2018 and 2017, respectively. The workers' compensation liability was \$59,053,000 and \$7,948,000 in 2018 and 2017, respectively. The recorded liability for workers' compensation and medical malpractice represents anticipated losses stated at their present value. The increase in the recorded medical malpractice liability and workers' compensation liability during 2018 relate largely to the System's acquisition of HCR ManorCare, as described in Note 24.

The System is also self-insured for the purpose of providing medical health insurance benefits for certain employees. An accrual of \$25,711,000 and \$13,002,000 has been recorded for claims that have been incurred, but not yet received, at December 31, 2018 and 2017, respectively, and is included in accounts payable and accrued liabilities in the consolidated balance sheet.

It is the opinion of management that estimated self-insurance cost accrued as of December 31, 2018 and 2017 are adequate to provide for potential losses resulting from pending or threatened litigation.

Note 12 - Accrued Claims

PIC contracts with various healthcare providers for the provision of certain medical care related to its members. PIC compensates those providers on a variety of bases, including capitation, fixed fee for service, and discounted charges. Medical expenses include all amounts incurred by PIC under membership contracts with individual members and employer groups. Contracts with providers for medical services are executed between the providers and PIC.

Cost of medical claims represents expenses incurred under contracts with healthcare providers; such costs are charged to expense in the month in which the service is rendered. These expenses include liabilities for incurred and reported claims and an estimate of incurred, but not reported, claims using past experience adjusted for current trends.

Activity in accrued claims expense for the years ended December 31, 2018 and 2017 is summarized as follows (in thousands):

	2018	2017
Balance - Beginning of year	\$ 81,423	\$ 92,439
Incurred related to:		
Current year	1,299,084	1,024,822
Prior years	18,427	(2,312)
Total incurred	1,317,511	1,022,510
Paid related to:		
Current year	(1,193,619)	(963,199)
Prior years	(96,753)	(71,427)
Total paid	(1,290,372)	(1,034,626)
Purchased through HRI acquisition	-	1,100
Balance - End of year	<u>\$ 108,562</u>	<u>\$ 81,423</u>

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 12 - Accrued Claims (Continued)

PIC estimates the amount of the accrued claims liability costs IBNR in accordance with GAAP and using standard actuarial developmental methodologies based upon historical data, including the period between the date services are rendered and the date claims are received and paid, denied claim activity, expected medical cost inflation, seasonality patterns, and changes in membership, among other things. PIC's IBNR best estimate also includes a provision for adverse deviation, which is an estimate for known environmental factors that are reasonably likely to affect the required level of IBNR reserves. This provision for adverse deviation is intended to capture the potential adverse development from factors, such as changes in current payment patterns versus historical payment patterns, potential unknown high cost cases, increased usage of higher cost services, accelerated utilization of services, and/or exceptional situations that require judgmental adjustments in setting the reserves for claims.

PIC consistently applies the IBNR estimation methodology from period to period. The IBNR best estimate is made on an accrual basis and adjusted in future periods as required. Any adjustments to the prior-period estimates are included in the current period. As additional information becomes known, assumptions are adjusted accordingly to change the estimate of IBNR. The degree of uncertainty in the estimates of incurred claims is greater for the most recent months' incurred services. Revised estimates for prior periods are determined in each year based on the most recent updates of paid claims for prior periods. Estimates for service costs IBNR are subject to the impact of changes in the regulatory environment, economic conditions, changes in claims trends, and numerous other factors. Given the inherent variability of such estimates, the actual liability could differ significantly from the amounts estimated. Management believes that the liability for accrued claims expenses is adequate to cover the ultimate net cost of medical expenses.

Note 13 - Liability for Unpaid Claims and Claim Adjustment Expenses

The following presents information about incurred and paid claims development as of December 31, 2018, net of reinsurance, as well as IBNR and cumulative reported claims by loss year for ProMedica Insurance Corporation (health insurance). The information relates to incurred and paid claims development and is presented as supplemental information.

Incurred Claims and Claims Adjustment Expenses - Net of Reinsurance for the Years Ended December 31 (in thousands)					As of December 31, 2018	
Accident Year	2015	2016	2017	2018	Total IBNR and Bulk Reserves (in thousands)	Cumulative Number of Reported Claims
2015	\$ 861,930	\$ 848,047	\$ 848,047	\$ 848,047	\$ -	4,181,000
2016		956,941	954,629	954,629	968	4,428,000
2017			1,024,822	1,043,249	2,129	4,461,000
2018				1,299,084	105,465	5,210,000
Total				\$ 4,145,009		
Cumulative Paid Claims and Allocated Claims Adjustment Expenses - Net of Reinsurance, for the Years Ended December 31 (in thousands)						
Accident Year	2015	2016	2017	2018		
2015	\$ 774,082	\$ 845,493	\$ 845,493	\$ 848,047		
2016		867,056	938,483	953,661		
2017			962,099	1,041,120		
2018				1,193,619		
Total				\$ 4,036,447		
Total liability for claims and claim adjustment expenses - Net of reinsurance					\$ 108,562	

Note 14 - Pension

Noncontributory Defined Benefit Pension Plans (Pension Plans)

The System sponsors a noncontributory qualified defined benefit pension plan, which covers certain full-time and part-time employees of the System who have more than 1,000 hours of service during the year. Benefits are based on each employee's compensation and length of service. The System makes contributions to the plan required to satisfy the Employee Retirement Income Security Act of 1974 (ERISA) funding standards. The System is not required to make a plan contribution in 2019 and reserves the right to make contributions that exceed ERISA funding standards.

The System froze plan participation effective December 31, 2014 for all plan participants and froze benefit accruals for all plan participants as of December 31, 2016.

During 2016, the System offered an early retirement incentive to a specific class of employees who met certain age and service requirements. The special termination benefits included one-time supplemental benefits and pension additions.

The System also sponsors a noncontributory qualified defined benefit pension plan, which covers certain eligible employees of Monroe. Participation in the plan was frozen effective June 30, 2005 and benefit accruals were frozen effective September 30, 2009. Effective December 31, 2018, this plan merged into the System sponsored noncontributory qualified defined benefit pension plan defined above. The System is not required to make a plan contribution in 2019 and reserves the right to make contributions that exceed ERISA funding standards.

The System also participates in a supplemental defined benefit plan (the "supplemental plan") for a small group of retirees. Participation in the supplemental plan and determination of benefits is at the discretion of the System. The pension costs for this plan are not prefunded.

Defined Contribution Benefits

The System sponsors defined contribution pension plans established under Section 401(k) and Section 403(b) of the IRC, which covers certain full-time and part-time employees. Employer contributions are based upon each employee's deferrals and service-based accruals. The pension expense under these plans for 2018 and 2017 was approximately \$40,494,000 and \$35,027,000, respectively.

Deferred Compensation

The System sponsors deferred compensation plans established under Section 457 of the IRC. The System's liability under the plans is primarily funded with assets held in a grantor trust and by an insurance company.

The System has nonqualified deferred compensation plans that permit eligible employees to defer a portion of their compensation. The deferred amounts are distributable in cash based on completion of length of service requirements, retirement, or termination of employment. At December 31, 2018 and 2017, the assets and liabilities under these plans totaled \$38,620,000 and \$41,569,000, respectively.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 14 - Pension (Continued)

The changes in projected benefit obligations, changes in plan assets, and funded status for the pension plans for the years ended December 31, 2018 and 2017 are as follows (in thousands):

	Pension Plans	
	2018	2017
Change in benefit obligation:		
Benefit obligation - Beginning of year	\$ 496,530	\$ 519,791
Benefit obligation assumed from HCR acquisition	1,694	-
Service cost	2,393	2,942
Interest cost	16,942	18,693
Actuarial (gain) loss	(12,117)	4,973
Benefits paid	(13,639)	(49,869)
Settlements	(17,521)	-
Benefit obligation - End of year	474,282	496,530
Change in plan assets:		
Fair value of plan assets - Beginning of year	500,855	478,707
Fair value of plan assets assumed from HCR acquisition	1,105	-
Actual return on plan assets	(23,530)	65,018
Employer contributions	2,487	6,999
Benefits paid	(13,639)	(49,869)
Settlements	(17,521)	-
Fair value of plan assets - End of year	449,757	500,855
Funded status	(24,525)	4,325
Net (liability) asset recognized	\$ (24,525)	\$ 4,325

Amounts recognized in the consolidated balance sheet (in thousands):

	Pension Plans	
	2018	2017
Other assets - Long term	\$ -	\$ 25,326
Other liabilities - Current	(63)	(63)
Other liabilities - Long term	(24,462)	(20,938)
Net (liability) asset	(24,525)	4,325
Amounts recognized in unrestricted net assets	147,716	108,695
Net amount recognized	\$ 123,191	\$ 113,020

Amounts recognized in net assets without donor restriction as of December 31, 2018 and 2017 consist of the following (in thousands):

	Pension Plans	
	2018	2017
Beginning balance	\$ 108,695	\$ 133,922
Recognized in net periodic benefit cost - Amortization of net loss	(1,637)	(1,612)
Settlement cost	(6,291)	-
Net loss (gain)	46,949	(23,615)
Ending balance	\$ 147,716	\$ 108,695

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 14 - Pension (Continued)

Amount included in net assets without donor restriction under FASB ASC Topic 715 consists of (in thousands):

	Pension Plans	
	2018	2017
Net actuarial loss (gain)	\$ 46,949	\$ (23,615)

Components of net periodic benefit cost for the years ended December 31, 2018 and 2017 consisted of the following (in thousands):

	Pension Plans	
	2018	2017
Service cost	\$ 2,393	\$ 2,942
Interest cost	16,942	18,693
Expected return on plan assets	(35,537)	(36,431)
Recognized net actuarial loss	1,637	1,612
Settlement costs	6,291	-
Net benefit	\$ (8,274)	\$ (13,184)

During 2019, \$1,616,000 is expected to be amortized from net assets without donor restriction into net periodic benefit cost.

	Pension Plans	
	2018	2017
Benefit obligations:		
Discount rate	4.00%	3.50%
Rate of compensation increase	3.00%	3.00%
Net periodic benefit cost:		
Discount rate	3.50%-4.00%	3.75%-4.00%
Expected long-term return on plan assets	7.25%	7.50%
Rate of compensation increase	3.00%	3.00%

For 2018 and 2017, the System assumed a long-term asset rate of 7.25 and 7.50 percent, respectively. In developing the expected long-term rate of return assumption, the System evaluated input from investment advisers, including a review of asset class return expectations based on historical compounded returns for such asset classes.

For the years ended December 31, 2018 and 2017, the total accumulated benefit obligation for the pension was \$473,964,000 and \$491,623,000, respectively.

Plan Assets

Assets of the defined benefit plans, which consist primarily of U.S. government and corporate obligations, listed common stocks, and money market funds, are held in a separate trust with investment management provided by various outside managers. The System invests the assets of the plans in a diversified portfolio consisting of an array of asset classes that attempt to maximize returns while minimizing volatility. The System targets to hold two years of beneficiary payments in short-term securities with the balance in a longer duration allocation.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 14 - Pension (Continued)

The System's overall investment strategy is to maximize total return while providing for expected retirement payments over a two-year horizon utilizing a wide diversification of asset types, fund strategies, and fund managers. The target allocations for plan assets are 51 percent equity securities, 43 percent fixed-income securities, and 6 percent real return strategy funds. Equity securities primarily include investments in large-cap and mid-cap companies, located in the United States as well as global and international strategies, and a long-short equity manager. Fixed-income securities include investment grade corporate bonds of companies from diversified industries, and U.S. Treasuries and agencies. Real return strategy funds include all asset mutual funds and a private capital investment.

The fair values of the System's pension plan assets at December 31, 2018 and 2017 by major asset classes are as follows (in thousands):

Asset Category	Fair Value Measurements at December 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Cash and cash equivalents	\$ 350	\$ 3,785	\$ -	\$ 4,135
U.S. equity securities:				
U.S. equity mutual funds	33,726	-	-	33,726
Marketable equity securities	43,501	-	-	43,501
International equity securities:				
International equity mutual fund	10,616	-	-	10,616
Marketable international securities	25,690	-	-	25,690
Fixed-income securities:				
U.S. Treasuries and agencies	-	67,314	-	67,314
Corporate obligations	-	72,808	-	72,808
Domestic fixed-income mutual funds	75,846	-	-	75,846
International fixed-income mutual funds	10,346	-	-	10,346
Real return strategy funds:				
All asset mutual funds	17,715	-	-	17,715
Private capital	-	-	4,663	4,663
Total investments at fair value	<u>\$ 217,790</u>	<u>\$ 143,907</u>	<u>\$ 4,663</u>	366,360
Investments measured at net asset value:				
International equity commingled fund				56,392
Long-short equity hedge funds				<u>27,005</u>
Total				<u>\$ 449,757</u>

ProMedica Health System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 14 - Pension (Continued)

Asset Category	Fair Value Measurements at December 31, 2017			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Cash and cash equivalents	\$ 1,661	\$ 8,137	\$ -	\$ 9,798
U.S. equity securities - Marketable equity securities	92,572	-	-	92,572
International equity securities:				
International equity mutual fund	16,071	-	-	16,071
Marketable international securities	49,113	-	-	49,113
Fixed-income securities:				
U.S. Treasuries and agencies	-	61,162	-	61,162
Corporate obligations	-	75,483	-	75,483
Domestic fixed-income mutual funds	57,262	-	-	57,262
International fixed-income mutual funds	10,137	-	-	10,137
Real return strategy funds:				
All asset mutual funds	18,644	-	-	18,644
Private capital	-	-	7,079	7,079
Total investments at fair value	\$ 245,460	\$ 144,782	\$ 7,079	397,321
Investments measured at net asset value:				
International equity commingled fund				75,133
Long-short equity hedge funds				28,401
Total				\$ 500,855

Cash Flow

Expected contributions - The System expects to contribute \$66,000 to its pension plans to pay anticipated benefit payments in 2019. The System may elect to make additional contributions.

Required contributions - The System, with the benefit obligation of HCR, is required to contribute approximately \$63,000 to its pension plan in 2019.

Expected benefit payments - The System expects to pay the following for pension benefits, which reflect expected future service, as appropriate, net of participant contributions (in thousands):

Years Ending December 31	Pension Plans
2019	\$ 27,603
2020	33,785
2021	37,384
2022	38,044
2023	39,998
Thereafter	162,006

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 15 - Net Assets with Donor Restrictions

As of December 31, 2018 and 2017, net assets with donor restrictions relate to the following (in thousands):

	<u>2018</u>	<u>2017</u>
Net assets with donor restrictions:		
Hospital operations support	\$ 94,266	\$ 103,903
Hospital capital support	18,890	17,615
Research	8,844	8,722
Health care and other services	<u>6,407</u>	<u>4,770</u>
Total	<u>\$ 128,407</u>	<u>\$ 135,010</u>

Donor restricted net assets include those net assets that can later be reclassified into net assets without donor restriction due to time and purpose restriction being fulfilled and those held in perpetuity, the income from which is expendable to support healthcare services. All endowed assets are included within the net assets with donor restriction class; therefore, no distributions from them are permitted in order to maintain the endowed corpus. Certain restricted net asset investments are included with the System's pooled investments, following the same investment policies and objectives.

System Endowment Funds

The System's endowments consist of funds established for a variety of purposes. Its endowments include both donor restricted endowment funds and funds designated by the board of trustees to function as endowments. The System considers various factors in making a determination to appropriate or accumulate donor restricted endowment funds. The System employs a diversified investment approach in order to minimize risk and maximize returns, utilizing both intermediate and long-term portfolios. The System's asset allocation objective for the long-term portfolio is to maximize total return while preserving capital values. The short-term portfolio is intended to preserve the principal of the fund and to meet current liquidity requirements.

The System can appropriate each year all available earnings in accordance with donor restrictions. The endowment corpus is to be maintained in perpetuity. Certain donor-restricted endowments require a portion of annual earnings to be maintained in perpetuity along with the corpus. Only amounts exceeding the amounts required to be maintained in perpetuity are expended.

Net assets without donor restriction include board designated quasi-endowment funds as of December 31, 2018 and 2017 are \$15,776,000 and \$16,582,000, respectively.

ProMedica Health System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 15 - Net Assets with Donor Restrictions (Continued)

Changes in endowment net assets for the fiscal years ended December 31, 2018 and 2017 are as follows (in thousands):

	Net Assets without Donor Restriction	Net Assets with Donor Restriction	Total
Endowment net assets - December 31, 2016	\$ 14,632	\$ 36,237	\$ 50,869
Investment income	1,975	3,214	5,189
Contributions and transfers - Net	-	209	209
Termination of board-designated endowments	(25)	-	(25)
	<u>16,582</u>	<u>39,660</u>	<u>56,242</u>
Endowment net assets - December 31, 2017	16,582	39,660	56,242
Investment income	569	1	570
Contributions and transfers - Net	-	8	8
Change in net realized and unrealized losses	(1,375)	(3,936)	(5,311)
Other	-	(540)	(540)
	<u>-</u>	<u>(540)</u>	<u>(540)</u>
Endowment net assets - December 31, 2018	<u>\$ 15,776</u>	<u>\$ 35,193</u>	<u>\$ 50,969</u>

Funds with Deficiencies

Periodically, the fair value of assets associated with the individual donor restricted endowment funds may fall below the level that the donor requires the System retain for a perpetual duration. Deficiencies of this nature would be reported in unrestricted net assets. These deficiencies could result from unfavorable market fluctuations and/or continued appropriation for certain programs that were deemed prudent by the System. As of December 31, 2018 and 2017, the System did not have funds with deficiencies.

Pledges Receivable

The System occasionally receives unconditional promises to give with payments due in future periods. Pledges receivable are recorded in assets limited as to use or restricted. As of December 31, 2018 and 2017, the System had pledges receivable of \$16,720,000 and \$22,088,000, respectively, net of an allowance of \$33,000 and \$406,000, respectively, for uncollectibility and discounted at 3.98 percent, with amounts due as follows (in thousands):

Years Receivable	Amount
2019	\$ 8,905
2020-2021	4,059
2022-2023	1,143
2023 and thereafter	2,613
	<u>2,613</u>
Total	<u>\$ 16,720</u>

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 16 - Income Taxes

PIC is an entity of the System that is for-profit and is subject to federal income taxes. PIC's provision for income taxes on income for the years ended December 31, 2018 and 2017 consists of the following (in thousands):

	<u>2018</u>	<u>2017</u>
Current income tax expense (benefit)	\$ 16,213	\$ (3,918)
Deferred income tax (benefit) expense	<u>(8,694)</u>	<u>8,376</u>
Income tax expense	<u>\$ 7,519</u>	<u>\$ 4,458</u>

The income tax expense differed from the amounts computed by applying the statutory U.S. federal income tax rate of 21 percent to pretax income as a result of the following (in thousands):

	<u>2018</u>	<u>2017</u>
Income before income taxes	\$ 6,272	\$ 61,674
Statutory U.S. federal income tax rate	\$ 1,317	\$ 21,570
State income taxes - Net of federal benefit	6	72
Exempt income adjustments	6,380	(12,410)
Impact of rate change	63	(4,831)
Other	<u>(247)</u>	<u>57</u>
Income tax expense	<u>\$ 7,519</u>	<u>\$ 4,458</u>
Effective tax rate	119.90 %	7.30 %

In 2018, PIC recorded a \$6,380,205 unfavorable adjustment due to exempt earnings related to the Paramount Advantage subsidiary. Paramount Advantage is tax exempt under IRC Section 501(c)(4). It obtained its exemption on October 1, 2015.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below (in thousands):

	<u>2018</u>	<u>2017</u>
Deferred tax assets:		
Unpaid losses and LAE	\$ 110	\$ 89
Unearned premium reserves	229	139
Accrued compensation	658	618
General accruals	424	407
Other	<u>243</u>	<u>39</u>
Total deferred tax assets - Net of any applicable allowances	1,664	1,292
Deferred tax liabilities:		
Goodwill and intangibles	(12)	(7,344)
Prepaid expense	(12,705)	(13,386)
Unrealized gains	144	(348)
Basis in fixed assets	(923)	(762)
Other liabilities	<u>(68)</u>	<u>(45)</u>
Deferred tax liabilities	<u>(13,564)</u>	<u>(21,885)</u>
Net deferred tax liability	<u>\$ (11,900)</u>	<u>\$ (20,593)</u>

ProMedica Health System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 17 - Functional Expenses

The System provides general healthcare services and insurance to residents within its geographic locations, including medical/surgical, pediatric, crucial emergency, skilled nursing, home health, and hospice care. Total expenses, including depreciation, amortization, and interest, related to providing these services for the years ended December 31, 2018 and 2017 are as follows (in thousands):

	Program Services				Support Services		Total
	Provider	Post Acute	Insurance	Other	Management and General	Fundraising	
Salaries, wages, and employee benefits	\$ 782,971	\$ 807,719	\$ 50,490	\$ 5,310	\$ 298,601	\$ 4,696	\$ 1,949,787
Food and drugs	143,255	104,926	-	423	3,347	7	251,958
Medical expenses	-	-	1,317,510	1	-	-	1,317,511
Contracted fees	114,466	102,383	8,825	554	200,963	2,276	429,467
Supplies	192,011	44,919	-	41	3,993	263	241,227
Insurance	6,143	23,749	-	-	7,027	-	36,919
Utilities	1,671	28,609	-	61	27,217	3	57,561
Other	67,635	224,377	1,018	4,898	158,672	(985)	455,615
Depreciation and amortization	84,418	11,226	-	-	52,078	10	147,732
Interest expense	20,077	13,620	-	-	14,617	10	48,324
Total	\$ 1,412,647	\$ 1,361,528	\$ 1,377,843	\$ 11,288	\$ 766,515	\$ 6,280	\$ 4,936,101

	Program Services				Support Services		Total
	Provider	Post Acute	Insurance	Other	Management and General	Fundraising	
Salaries, wages, and employee benefits	\$ 722,888	\$ 47,479	\$ 34,866	\$ 3,957	\$ 254,665	\$ 4,167	\$ 1,068,022
Food and drugs	137,407	48,939	-	428	3,950	-	190,724
Medical expenses	-	-	1,004,050	-	9	-	1,004,059
Contracted fees	97,371	7,741	7,778	588	188,567	1,703	303,748
Supplies	182,949	10,449	-	18	4,682	40	198,138
Insurance	6,434	-	-	-	9,409	-	15,843
Utilities	1,183	361	-	48	24,420	4	26,016
Other	67,055	4,513	4,481	4,143	125,686	(474)	205,404
Depreciation and amortization	83,329	1,892	-	-	45,666	10	130,897
Interest expense	28,440	261	-	-	5,706	16	34,423
Total	\$ 1,327,056	\$ 121,635	\$ 1,051,175	\$ 9,182	\$ 662,760	\$ 5,466	\$ 3,177,274

Note 18 - Fair Value Measurements

The following methods and assumptions were used to estimate fair value of each class of financial instruments in accordance with FASB ASC Topic 820, *Fair Value Measurement*:

Cash Equivalents

The carrying value of cash equivalents approximates fair value as maturities are less than three months. Fair values of cash equivalent instruments that do not trade on a regular basis in active markets are classified as Level 2.

Equity and Fixed-income Securities

The estimated fair values of debt securities are based on quoted market prices and/or other market data for the same or comparable instruments and transactions in the establishing the prices. Fair values of debt securities that do not trade on a regular basis in active markets are classified as Level 2. Fair value estimates for publicly traded equity securities are based on quoted market prices and/or other market data for the same or comparable instruments and transactions in establishing the prices.

Note 18 - Fair Value Measurements (Continued)

Exchange Traded/Mutual Funds

Exchange-traded funds are valued at the closing price reported on the applicable exchange on which the fund is traded, or estimated using quoted market prices for similar securities. Mutual funds are valued using NAV based on the value of the underlying assets owned by the funds, minus liabilities, divided by the number of shares outstanding, and multiplied by the number of shares owned.

Commingled Funds

Commingled funds are for investment by institutional investors only and, therefore, do not require registration with the Securities and Exchange Commission. Commingled funds are recorded at fair value, based on the underlying investments having a readily determinable market value, or, based on NAV, which is calculated using the most recent fund financial statements.

Hedge Funds

Hedge fund utilizes a "fund-of-funds" approach resulting in diversified multistrategy, multimanager investment. Underlying investments in these funds are equity securities. These funds are valued at net asset value, which is calculated using the most recent financial statements.

Real Estate Held for Investment

The estimated fair market value of real estate held for investment is obtained using fair market appraisals.

Derivatives

Fair values of the System's interest rate swaps are estimated utilizing the terms of the swaps and publicly available market yield curves. Because the swaps are unique and are not actively traded, the fair values are classified as Level 2.

Private Capital

Private capital is invested in discounted loans and structured credit tied to residential and commercial real estate markets in the United States and Europe. Management's estimates of the fair value of this investment are provided by the third-party administrator and the fund manager/general partner. Management obtains and considers the audited financial statements of this investment when evaluating the overall reasonableness of the fair value. In addition to a review of external information provided, management's internal procedures include reviews of returns against benchmarks and discussions with fund managers of performance, change in personnel or process, and evaluations of current market conditions for these investments. Investment managers also meet with System management on a periodic basis. Because of the inherent uncertainty, valuations may differ materially from those obtained had an active market existed. The investment is a closed-end fund and has significant redemption restrictions that prohibit redemptions during the fund's life, which has an initial term of five years with two optional one and one-half year extension options exercisable at the sole discretion of the general partner. As of December 31, 2018 and 2017, unfunded capital commitments totaled \$2,500,000 and \$2,500,000, respectively.

Beneficial Interests in Perpetual Trusts

Beneficial interests in perpetual trusts are valued using the net asset value of the underlying assets multiplied by the System's percentage share in the applicable trust.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 18 - Fair Value Measurements (Continued)

The following tables present information about the fair value of the System's financial instruments as of December 31, 2018 and 2017, according to the valuation techniques used by the System. The assets are included in marketable securities and assets limited as to use current and noncurrent (in thousands).

	Assets Measured at Fair Value on a Recurring Basis at December 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2018
Assets				
Cash and cash equivalents	\$ 117,630	\$ 8,594	\$ -	\$ 126,224
U.S. equity securities:				
U.S. equity mutual funds	92,072	-	-	92,072
Marketable equity securities	121,031	-	-	121,031
International equity securities:				
International equity mutual funds	22,760	-	-	22,760
Marketable international equity securities	50,744	-	-	50,744
Fixed-income securities:				
U.S. Treasuries and agencies	-	232,606	-	232,606
Corporate, municipal, and other governmental bonds	-	272,570	-	272,570
Domestic fixed-income mutual funds	188,920	-	-	188,920
International fixed-income mutual funds	17,272	-	-	17,272
Real return strategy funds:				
All asset mutual funds	34,468	-	-	34,468
Private capital	-	-	13,323	13,323
Other	26,870	-	-	26,870
Beneficial interests in perpetual trusts	-	-	29,788	29,788
Domestic real estate	-	-	13,581	13,581
Total	\$ 671,767	\$ 513,770	\$ 56,692	1,242,229
Investments measured at net asset value:				
U.S. equity commingled funds				52,842
International equity commingled funds				106,225
Long-short equity hedge funds				56,133
Total assets limited as to use and marketable securities				\$ 1,457,429

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 18 - Fair Value Measurements (Continued)

	Assets and Liabilities Measured at Fair Value on a Recurring Basis at December 31, 2017			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2017
Assets				
Cash and cash equivalents	\$ 17,462	\$ 19,902	\$ -	\$ 37,364
U.S. equity securities:				
U.S. equity mutual funds	25,473	-	-	25,473
Marketable equity securities	332,913	-	-	332,913
International equity securities:				
International equity mutual funds	44,025	-	-	44,025
Marketable international equity securities	109,439	-	-	109,439
Fixed-income securities:				
U.S. Treasuries and agencies	-	298,281	-	298,281
Corporate, municipal, and other governmental bonds	-	376,364	-	376,364
Domestic fixed-income mutual funds	78,122	-	-	78,122
International fixed-income mutual funds	35,299	-	-	35,299
Real return funds:				
All asset mutual funds	59,130	-	-	59,130
Private capital	-	-	20,225	20,225
Other	32,956	-	-	32,956
Beneficial interests in perpetual trusts	-	-	32,096	32,096
Domestic real estate	-	-	8,428	8,428
Total	\$ 734,819	\$ 694,547	\$ 60,749	1,490,115
Investments measured at net asset value:				
U.S. equity commingled funds				78,086
International equity commingled funds				224,764
Long-short equity hedge funds				72,920
Total assets limited as to use and marketable securities				\$ 1,865,885
Liabilities				
Derivatives	\$ -	\$ 17,332	\$ -	\$ 17,332

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 18 - Fair Value Measurements (Continued)

The following is a summary of the fair value of System investments with a reported NAV per share as of December 31, 2018 and 2017 (in thousands):

	Investments Held at December 31, 2018		
	Fair Value	Redemption Frequency, if Eligible	Redemption Notice Period
U.S. equity commingled funds	\$ 52,842	Monthly	0-5 days
International equity commingled funds	106,225	Daily/Monthly	0-6 days
Long-short equity hedge funds	56,133	Monthly/Quarterly	60-90 days
Total	\$ 215,200		

	Investments Held at December 31, 2017		
	Fair Value	Redemption Frequency, if Eligible	Redemption Notice Period
U.S. equity commingled funds	\$ 78,086	Monthly	0-5 days
International equity commingled funds	224,764	Daily/Monthly	0-6 days
Long-short equity hedge funds	72,920	Monthly/Quarterly	60-90 days
Total	\$ 375,770		

U.S. Equity Commingled Funds - Composed of shares or units in commingled funds that are not publicly traded. Underlying assets in these funds include publicly traded options that are valued at their NAV calculated by the fund manager.

International Equity Commingled Funds - Composed of shares or units in commingled funds that are not publicly traded. Underlying assets in these funds primarily include publicly traded equity securities that are valued at their NAV calculated by the fund manager and have daily liquidity.

Long-short Equity Hedge Funds - Composed of investments in a hedge fund that invest both in long and short U.S. and international equities. Management of the hedge fund has the ability to shift investments from value-to-growth strategies, from small-to-large capitalization stocks, and from a net long position to a net short position. The fair value of investments in this class has been estimated using the NAV per share of the investments.

There are no unfunded commitments of System investments with a reported NAV per share.

Note 19 - Liquidity

The System has \$1,534,795,000 and \$1,062,882,000 of financial assets available within one year of the consolidated balance sheet date to meet cash needs for general expenditure consisting of cash of \$325,496,000 and \$294,030,000, short-term investments of \$566,992,000 and \$513,380,000, and accounts receivable of \$642,307,000 and \$255,472,000 at December 31, 2018 and 2017, respectively. Of the short-term investments \$307,237,000 and \$295,433,000 are included as current assets and the remaining \$259,755,000 and \$217,947,000 are included in noncurrent assets whose use is limited on the consolidated balance sheet. None of the financial assets are subject to donor or other contractual restrictions that make them unavailable for general expenditure within one year of the balance sheet date. The contributions receivable is subject to implied time restrictions but are expected to be collected within one year. The System has certain board designated assets, which are not included in amounts available for expenditure in the next year. However, the board-designated amounts could be made available, if necessary.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 19 - Liquidity (Continued)

The System has a goal to maintain financial assets, which consist of cash and marketable securities and certain designated fixed-income investments included in internally designated funds, on hand at a minimum 60 days of normal operating expenses, which are, on average, approximately \$779,185,000 and \$495,116,000 at December 31, 2018 and 2017, respectively. The System has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, as part of its liquidity management, the System invests cash in excess of daily requirements in various short-term investments, including certificates of deposit and short-term treasury instruments.

Note 20 - Commitments and Contingencies

Operating Leases

The System leases various equipment and facilities under operating leases. Total rental expense in 2018 and 2017 for all operating leases was approximately \$130,929,000 and \$20,409,000, respectively.

The following is a schedule by year of future minimum lease payments under operating leases as of December 31, 2018 that have initial or remaining lease terms in excess of one year (in thousands):

Years Ending December 31	Amount
2019	\$ 202,920
2020	200,627
2021	199,332
2022	200,482
2023	203,103
Thereafter	<u>2,217,112</u>
Total	<u>\$ 3,223,576</u>

Master Lease

On July 27, 2018, HCR entered into an Amended and Restated Master Lease with a subsidiary of Welltower (NYSE: WELL), which is a triple-net master lease with an initial term of 15 years. The lease may be renewed at the option of the tenant for two five-year terms and a four-year, 11-month term. The lease applies to 216 of the 222 skilled nursing and assisted living facilities operated by HCR. The System has guaranteed the payment obligations under the lease. The base rent payable under the lease is \$179,000,000 for the first year of its term, with an escalator of 1.375 percent for the second year of its term and of 2.75 percent annually thereafter. Base rent for the renewal periods is to be reset to the then-current market value taking into consideration specific factors set forth in the lease. The lease is accounted for as an operating lease, with rent expense recognized on a straight-line basis over each year of the initial lease term. Rent related to the lease was \$92,531,000 in 2018.

Litigation

The System is involved in litigation and regulatory investigations arising in the course of business. Based in part on consultation with legal counsel, management believes that these matters will be resolved without material adverse effect on the System's consolidated financial position or results of operations.

ProMedica Health System and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 21 - Asset Retirement Obligations

FASB ASC Topic 410, *Asset Retirement and Environmental Obligations*, requires that the fair value of the liability for an asset retirement obligation be recognized in the period in which it is incurred and the settlement date is estimable and capitalized as part of the carrying amount of the related tangible long-lived asset. The liability is recorded at fair value, and the capitalized cost is depreciated over the remaining useful life of the related asset.

The System has determined it has legal obligations to perform certain asset retirement activities associated with planned and estimated demolition and remediation at various hospitals, long-term care facilities, medical office buildings, and other facilities. During 2018 and 2017, changes to the asset retirement obligation are as follows (in thousands):

	2018	2017
Balance - January 1	\$ 24,306	\$ 24,081
Additions	3,648	400
Accretion expense	602	521
Settlements	(197)	(696)
Balance - December 31	<u>\$ 28,359</u>	<u>\$ 24,306</u>

Note 22 - Leasing Revenue Activity

The System leases space to tenants under various operating lease agreements. These agreements, without giving effect to renewal options, have expiration dates ranging from 2018 to 2038. The rental revenue for the years ended December 31, 2018 and 2017 was \$7,212,000 and \$6,843,000, respectively. As of December 31, 2018, the aggregate future minimum base rental payments to the System under noncancelable operating leases by year are as follows (in thousands):

Years Ending	Amount
2019	\$ 5,678
2020	4,474
2021	3,812
2022	2,184
2023	2,536
Thereafter	6,703
Total	<u>\$ 25,387</u>

Note 23 - Investments in Affiliated Companies

The summarized financial position and results of operations for the entities accounted for under the equity method, excluding the System's investment in Welltower, as of and for the years ended December 31 are as follows (in thousands):

	2018	2017
Total assets	\$ 352,870	\$ 303,905
Total liabilities	134,220	105,941
Net assets	218,650	197,964
Revenue - Net	351,920	258,294
Net income	14,286	6,153

Included in the table above is the System's investment in Lima Memorial Hospital that represents approximately 8 and 59 percent of the total equity method investments as of December 31, 2018 and 2017, respectively. Lima Memorial Hospital operates as a not-for-profit hospital.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 23 - Investments in Affiliated Companies (Continued)

HCR purchases various pharmaceutical supplies from an affiliate accounted for as an equity investment. Total purchases for 2018 is approximately \$29.5 million.

The summarized financial position and results of operations for the System's joint venture with in Welltower (see Note 24), as of and for the years ended December 31, 2018 are as follows (in thousands):

Total assets	\$	2,558,148
Total liabilities		(54)
Net assets		2,558,202
Revenue - Net		92,059
Net income		65,516

Note 24 - Business Combinations

Acquisition of Health Resources, Inc. (HRI)

On December 29, 2017, ProMedica Insurance Corporation acquired HRI through a stock acquisition. HRI, headquartered in Evansville, Indiana, offers dental benefit programs to employer groups located in Indiana and Kentucky. PIC recorded the purchase as an acquisition and paid total consideration of \$86,200,000. PIC recorded amortizable intangible assets of \$38,300,000 and an indefinite-lived intangible asset of \$12,400,000 in its consolidated balance sheet. PIC also recorded goodwill of \$28,000,000 for the excess of total consideration paid over the fair value of the identifiable acquisition-date net assets. HRI is included in PIC's consolidated balance sheet at December 31, 2018.

Acquisition of ProMedica Coldwater Regional Hospital (Coldwater)

On January 1, 2018, the System became the sole member of ProMedica Coldwater Regional Hospital, formerly Community Health Center of Branch County and Community Health Center Foundation, which was accounted for as an acquisition. The hospital, headquartered in Coldwater Michigan, operates an acute care facility with 87 beds. The fair value of the assets acquired exceeded the liabilities assumed resulting in an inherent contribution of \$14,639,000 which was recorded during the year ended December 31, 2018.

Acquisition of HCR ManorCare, Inc. and Subsidiaries (HCR)

On July 26, 2018, the System acquired HCR through a Chapter 11 Reorganization and stock acquisition. The System made a capital contribution and loans to HCR to enable HCR to discharge certain liabilities in exchange for 100 percent of its equity shares. The reorganized HCR then became a wholly owned subsidiary of the System. HCR, headquartered in Toledo, Ohio, operates 168 skilled nursing facilities, 54 assisted living facilities, 108 hospice and home health offices, and 51 rehabilitation clinics in 27 states.

The System recorded the transaction as an acquisition and paid a total consideration of \$1,116,400,000. Provisional goodwill of \$1,184,364,000 was recognized by the System as part of the acquisition. The goodwill amount is provisional pending the finalization of the fair value of certain acquired intangible assets. HCR is included in the System's consolidated balance sheet at December 31, 2018.

Notes to Consolidated Financial Statements

December 31, 2018 and 2017

Note 24 - Business Combinations (Continued)

The fair values of the net assets acquired and liabilities assumed as of July 26, 2018 were as follows (in thousands):

Current assets	\$ 633,300
Goodwill	1,184,364
Intangible assets	18,036
Investment in CVS Pharmacy joint venture	37,000
Property and equipment - Net	103,100
Other assets	<u>29,400</u>
Total assets acquired	2,005,200
Trade payable and accrued expenses	577,600
Capital lease obligation	17,400
Other liabilities	<u>293,800</u>
Total liabilities assumed	<u>888,800</u>
Aggregate purchase price	<u>\$ 1,116,400</u>

HCR revenue and excess of revenue (under) over expenses for the five-month period ended December 31, 2018 that is included in the System's consolidated financial statements is \$1,320,516,000 and \$36,776,000, respectively. The revenue and excess revenue (under) over expenses for year ended December 31, 2017 for the System would have increased by \$3,014,000,000 and \$183,246,000, respectively, if HCR was included in the 2017 consolidated financial statements of the System. The revenue and excess revenue (under) over expenses for the System would have increased by \$3,013,000,000 and \$81,552,000 if HCR was included in the 2018 consolidated financial statements of the System for the entire year.

Joint Venture with Welltower

In connection with the HCR acquisition, the System also paid \$512,700,000 to Welltower (NYSE: WELL) in exchange for a 20 percent share of a new joint venture with Welltower, which it subsequently contributed to HCR. The System accounts for this joint venture using the equity method. The joint venture was formed to hold the 216 skilled nursing and assisted living facilities formerly owned by Quality Care Properties (NYSE: QCP) and leased to HCR. Those properties will continue to be operated by HCR under an amended and restated master lease agreement with the Welltower joint venture. See Note 20 for a discussion of the master lease and Note 23 for discussion of the Welltower joint venture.

Note 25 - Discontinued Operations

As described in Note 24, the System's acquisition of HCR ManorCare included assets that were planned for divestiture. All of these assets were divested in 2018 subsequent to the acquisition. The postacquisition results of operations and loss on sale have been classified as discontinued operations.

Following is a summary of discontinued operations from the acquisition date through December 31, 2018 (in thousands):

Net patient service revenue	\$ 121,252
Operating expenses	<u>(142,145)</u>
Loss from operations	(20,893)
Loss on sale of assets	<u>(1,042)</u>
Loss on discontinued operations	<u>\$ (21,935)</u>

December 31, 2018 and 2017

Note 25 - Discontinued Operations (Continued)

The System retains risk for loss contingencies related to the discontinued operations. Such liabilities are estimated based on the best available evidence. The System's future estimate of loss settlements may change and actual losses may be more or less than the current estimate. Subsequent changes to the estimates will be recorded in discontinued operations.

Note 26 - University of Toledo College of Medicine and Life Sciences Affiliation

ProMedica and the University of Toledo are partners in a 50-year Academic Affiliation Agreement (the "Agreement") to support the academic programs of the College of Medicine and Life Sciences (including research, education of medical students, and residency programs) which is anticipated to develop Toledo Hospital and Toledo Children's Hospital into a premier academic medical center and preeminent quaternary center.

The Agreement includes a financial commitment by ProMedica to provide academic support to The University of Toledo through payments for certain defined services, research, branding rights, and other related services for value and benefits to ProMedica. ProMedica made initial payments totaling \$40 million over the three-year period ending in 2017, which have been deferred and are being expensed over 30 years to match the estimated years of benefit realization. In addition, ProMedica incurred transitional payments expense of \$16,232,000 in 2017 and \$26,002,000 in 2018 and is obligated to make payments of \$38,502,000 in 2019; and \$47,500,000 in 2020. Beginning in 2021 through 2065, annual support payments will be at least \$50,000,000 and calculated based on the aggregate of: (i) 3 percent of base year 2015 net patient service revenue; plus, (ii) 2 percent of the difference in the current year net patient service revenue, excluding net patient service revenue generated from facilities acquired by ProMedica after 2015, and the base year of 2015; plus, (iii) one quarter of 1 percent of net patient service revenue generated in the then-current year from facilities acquired by ProMedica after 2015. The amount of annual support payments will be reassessed every five years, starting in the academic year 2030.

In addition, ProMedica also committed \$250,000,000 to construct and renovate certain lab and teaching space on The University of Toledo and Toledo Hospital campuses, with \$100,000,000 expended by 2027, and the remaining \$150,000,000 expended by 2040.

As of December 31, 2018 and 2017, the carrying amount of the deferred payments is \$36,888,000 and \$38,229,000, respectively, and is included in intangible assets and other.

Management has evaluated the expected future benefits to be received under the Agreement in relation to future payments. It is expected that future payments beyond 2018 will be expensed as incurred and will approximate the annual benefits received.

Note 27 - Subsequent Events

Management has evaluated all events subsequent to the consolidated balance sheet date of December 31, 2018 through the date the consolidated financial statements were issued and has determined that there are no subsequent events that require disclosure under FASB ASC Topic 855, *Subsequent Events*.

Supplemental Information

Independent Auditor's Report on Supplemental Information

To the Board of Trustees
ProMedica Health System and Subsidiaries

We have audited the consolidated financial statements of ProMedica Health System and Subsidiaries as of and for the years ended December 31, 2018 and 2017 and have issued our report thereon dated April 23, 2019, which contained an unmodified opinion on those consolidated financial statements. Our audit was performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information is presented for the purpose of additional analysis rather than to present the financial position, results of operations, and cash flows of the individual companies 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 audit 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.

Plante & Moran, PLLC

April 23, 2019

ProMedica Health System and Subsidiaries

Consolidating Balance Sheet

December 31, 2018

(In Thousands)

	The Toledo Hospital	Defiance Hospital, Inc.	Bay Park Community Hospital	Emma L. Bixby Medical Center	Herrick Memorial Hospital, Inc.	Lenawee Long Term Care	Fostoria Hospital Association	Memorial Hospital	Mercy Memorial Hospital Corporation	ProMedica Continuing Care Services Corp.	Eliminations	Total Obligated Group	Nonobligated Group	Consolidating Adjustments and Eliminations	Consolidated ProMedica Health System and Subsidiaries Total
Assets															
Current Assets															
Cash and cash equivalents	\$ 10,813	\$ 12,569	\$ 12,133	\$ 13,078	\$ 1,095	\$ 4,060	\$ 6,919	\$ 557	\$ 3,885	\$ (398)	\$ -	\$ 64,711	\$ 260,785	\$ -	\$ 325,496
Marketable securities	6,201	193	-	-	-	-	-	-	-	-	-	6,394	300,843	-	307,237
Assets limited as to use or restricted	-	-	-	-	-	-	-	-	-	-	-	-	12,887	-	12,887
Accounts receivable - Net	162,440	7,620	9,417	9,901	3,546	969	4,914	8,653	15,807	5,479	-	228,746	442,414	(28,853)	642,307
Intercompany accounts receivable	66,998	2,479	1,712	3,579	1,119	7	750	430	11,972	27,841	(33,711)	83,176	58,346	(141,522)	-
Estimated third-party payor receivable	6,489	1,237	815	1,038	15	-	932	1,327	3,450	-	-	15,303	21,405	-	36,708
Supplies	12,969	878	1,290	1,510	422	-	910	1,104	1,933	-	-	21,016	10,796	-	31,812
Other current assets	7,415	172	152	302	94	42	386	340	654	119	-	9,676	146,107	(9,335)	146,448
Total current assets	273,325	25,148	25,519	29,408	6,291	5,078	14,811	12,411	37,701	33,041	(33,711)	429,022	1,253,583	(179,710)	1,502,895
Noncurrent Assets Limited as to Use or Restricted - Net of amounts required to meet current obligations															
Restricted funds	2,326	11	-	147	-	-	14	-	43	1	-	2,542	150,309	(24,444)	128,407
Bond indenture agreement funds	62,271	3	4	-	-	-	-	-	-	-	-	62,278	-	-	62,278
Professional liability and workers' compensation insurance funds	-	-	-	-	-	-	-	-	-	-	-	-	61,688	-	61,688
Internally designated for capital acquisition	188,558	84,850	14,030	101,098	43,061	12,051	36,521	37,435	64,779	3,047	-	585,430	48,296	-	633,726
Other segregated investments	38,259	(10)	-	(147)	-	-	(14)	2,217	44	-	-	40,349	209,522	1,335	251,206
Total noncurrent assets limited as to use or restricted	291,414	84,854	14,034	101,098	43,061	12,051	36,521	39,652	64,866	3,048	-	690,599	469,815	(23,109)	1,137,305
Property and Equipment - Net	876,803	35,987	42,713	45,715	11,384	1,247	18,109	44,259	70,515	2,684	-	1,149,416	462,044	(2,565)	1,608,895
Other Assets															
Goodwill	17,958	-	-	-	-	-	-	282	-	-	-	18,240	1,265,540	-	1,283,780
Intangible assets	66	-	-	-	-	-	-	380	1,100	-	-	1,546	68,239	-	69,785
Investments in affiliated companies	3,453	-	159	124	-	-	-	291	879	728	-	5,634	310,380	319,427	635,441
Other	-	-	-	-	-	-	100	482	-	-	-	582	93,444	-	94,026
Total other assets	21,477	-	159	124	-	-	100	1,435	1,979	728	-	26,002	1,737,603	319,427	2,083,032
Total assets	\$ 1,463,019	\$ 145,989	\$ 82,425	\$ 176,345	\$ 60,736	\$ 18,376	\$ 69,541	\$ 97,757	\$ 175,061	\$ 39,501	\$ (33,711)	\$ 2,295,039	\$ 3,923,045	\$ 114,043	\$ 6,332,127

ProMedica Health System and Subsidiaries

Consolidating Balance Sheet (Continued)

December 31, 2018

(In Thousands)

	The Toledo Hospital	Defiance Hospital, Inc.	Bay Park Community Hospital	Emma L. Bixby Medical Center	Herrick Memorial Hospital, Inc.	Lenawee Long Term Care	Fostoria Hospital Association	Memorial Hospital	Mercy Memorial Hospital Corporation	ProMedica Continuing Care Services Corp.	Eliminations	Total Obligated Group	Nonobligated Group	Consolidating Adjustments and Eliminations	Consolidated ProMedica Health System and Subsidiaries Total
Liabilities and Net Assets															
Current Liabilities															
Accounts payable and accrued expenses	\$ 66,479	\$ 2,403	\$ 3,163	\$ 5,557	\$ 333	\$ 310	\$ 1,238	\$ 5,132	\$ 5,709	\$ 2,280	\$ -	\$ 92,604	\$ 343,481	\$ (240)	\$ 435,845
Intercompany accounts payable	81,380	1,875	2,791	7,459	2,035	637	1,331	2,255	25,168	2,561	(33,711)	93,781	47,744	(141,525)	-
Contractual current installments of long-term debt	16,385	319	334	488	141	11	101	553	1,945	4	-	20,281	2,922	-	23,203
Contingent current installments of long-term debt	323,429	15,018	24,855	9,421	13,070	2,345	10,664	-	31,033	2,230	-	432,065	14,379	-	446,444
Estimated third-party payor settlements	8,788	2,616	600	4,698	2,423	569	2,296	683	4,909	41	-	27,623	6,811	-	34,434
Accrued liabilities and other:															
Compensation and benefits	34,860	1,899	2,355	3,950	621	435	986	1,612	4,764	2,877	-	54,359	262,518	-	316,877
Professional liability and workers' compensation	-	-	-	-	-	-	-	-	-	-	-	-	111,535	-	111,535
Claims expense	-	-	-	-	(1)	-	-	-	-	-	-	(1)	137,416	(28,853)	108,562
Other current liabilities	128	-	-	13	44	-	-	-	-	-	-	185	17,292	(9,092)	8,385
Total current liabilities	531,449	24,130	34,098	31,586	18,666	4,307	16,616	10,235	73,528	9,993	(33,711)	720,897	944,098	(179,710)	1,485,285
Long-term Debt - Less current installments	1,753,519	19,182	25,337	50,224	173	-	181	24,652	-	18	-	1,873,286	28,872	-	1,902,158
Other Liabilities															
Accrued professional liability and workers' compensation - Less current portion	-	-	-	-	-	-	-	-	-	-	-	-	312,822	-	312,822
Deferred compensation	4,034	-	-	-	-	-	-	-	-	-	-	4,034	34,586	-	38,620
Pension	292	-	-	-	-	-	-	-	-	-	-	292	24,170	-	24,462
Other	10,742	(68)	(11)	1,542	1,183	201	1,267	2,224	1,673	811	-	19,564	51,222	-	70,786
Total other liabilities	15,068	(68)	(11)	1,542	1,183	201	1,267	2,224	1,673	811	-	23,890	422,800	-	446,690
Total liabilities	2,300,036	43,244	59,424	83,352	20,022	4,508	18,064	37,111	75,201	10,822	(33,711)	2,618,073	1,395,770	(179,710)	3,834,133

ProMedica Health System and Subsidiaries

Consolidating Balance Sheet (Continued)

December 31, 2018

(In Thousands)

	The Toledo Hospital	Defiance Hospital, Inc.	Bay Park Community Hospital	Emma L. Bixby Medical Center	Herrick Memorial Hospital, Inc.	Lenawee Long Term Care	Fostoria Hospital Association	Memorial Hospital	Mercy Memorial Hospital Corporation	ProMedica Continuing Care Services Corp.	Eliminations	Total Obligated Group	Nonobligated Group	Consolidating Adjustments and Eliminations	Consolidated ProMedica Health System and Subsidiaries Total
Net Assets															
Net assets without donor restrictions:															
Controlling interest	\$ (839,343)	\$ 102,734	\$ 23,001	\$ 92,846	\$ 40,714	\$ 13,868	\$ 51,463	\$ 60,646	\$ 99,817	\$ 28,678	\$ -	\$ (325,576)	\$ 2,327,776	\$ 316,862	\$ 2,319,062
Noncontrolling interest	-	-	-	-	-	-	-	-	-	-	-	-	50,525	-	50,525
Total net assets without donor restrictions	(839,343)	102,734	23,001	92,846	40,714	13,868	51,463	60,646	99,817	28,678	-	(325,576)	2,378,301	316,862	2,369,587
Net assets with donor restrictions	2,326	11	-	147	-	-	14	-	43	1	-	2,542	148,974	(23,109)	128,407
Total net assets	(837,017)	102,745	23,001	92,993	40,714	13,868	51,477	60,646	99,860	28,679	-	(323,034)	2,527,275	293,753	2,497,994
Total liabilities and net assets	<u>\$ 1,463,019</u>	<u>\$ 145,989</u>	<u>\$ 82,425</u>	<u>\$ 176,345</u>	<u>\$ 60,736</u>	<u>\$ 18,376</u>	<u>\$ 69,541</u>	<u>\$ 97,757</u>	<u>\$ 175,061</u>	<u>\$ 39,501</u>	<u>\$ (33,711)</u>	<u>\$ 2,295,039</u>	<u>\$ 3,923,045</u>	<u>\$ 114,043</u>	<u>\$ 6,332,127</u>

ProMedica Health System and Subsidiaries

Consolidating Statement of Operations and Changes in Unrestricted Net Assets

Year Ended December 31, 2018

(In Thousands)

	The Toledo Hospital	Defiance Hospital, Inc.	Bay Park Community Hospital	Emma L. Bixby Medical Center	Herrick Memorial Hospital, Inc.	Lenawee Long Term Care	Fostoria Hospital Association	Memorial Hospital	Mercy Memorial Hospital Corporation	ProMedica Continuing Care Services Corp.	Eliminations	Total Obligated Group	Nonobligated Group	Consolidating Adjustments and Eliminations	Consolidated ProMedica Health System and Subsidiaries Total
Unrestricted Revenue, Gains, and Other Support															
Net patient service revenue	\$ 1,058,524	\$ 64,861	\$ 80,498	\$ 82,772	\$ 25,337	\$ 10,916	\$ 34,528	\$ 58,426	\$ 121,748	\$ 37,152	\$ (17,132)	\$ 1,557,630	\$ 1,708,767	\$ (274,492)	\$ 2,991,905
Premium revenue	-	-	-	-	-	-	-	-	-	-	-	-	1,808,140	(5,632)	1,802,508
Other	17,601	262	324	1,816	242	10	2,583	1,595	5,152	342	(341)	29,586	101,359	(7,997)	122,948
Net assets released for use in operations	8,177	55	75	540	110	-	111	72	204	74	-	9,418	15,150	(10,857)	13,711
Total unrestricted revenue, gains, and other support	1,084,302	65,178	80,897	85,128	25,689	10,926	37,222	60,093	127,104	37,568	(17,473)	1,596,634	3,633,416	(298,978)	4,931,072
Expenses															
Salaries, wages, and employee benefits	373,190	19,474	29,010	32,321	7,829	6,464	11,099	18,066	59,671	31,028	(17,473)	570,679	1,421,571	(42,463)	1,949,787
Food and drugs	92,894	3,799	3,424	4,322	766	699	4,630	4,359	11,168	1,932	-	127,993	123,994	(29)	251,958
Medical expenses	-	-	-	-	-	-	-	-	-	-	-	-	1,555,418	(237,907)	1,317,511
Contracted fees	93,352	5,884	6,839	8,805	4,223	493	3,383	11,023	15,705	1,184	-	150,891	278,576	-	429,467
Supplies	133,157	4,080	8,925	7,592	1,267	311	2,281	4,028	10,600	1,138	-	173,379	67,975	(127)	241,227
Insurance	5,030	314	430	600	305	-	189	311	1,335	371	-	8,885	35,608	(7,574)	36,919
Utilities	10,177	818	936	1,246	524	147	652	1,168	1,658	286	-	17,612	39,949	-	57,561
Other	243,348	14,066	18,573	19,775	7,044	3,016	8,409	14,753	33,318	841	-	363,143	92,492	(20)	455,615
Total expenses	951,148	48,435	68,137	74,661	21,958	11,130	30,643	53,708	133,455	36,780	(17,473)	1,412,582	3,615,583	(288,120)	4,740,045
Operating Income (Loss) before Depreciation and Amortization Expense	133,154	16,743	12,760	10,467	3,731	(204)	6,579	6,385	(6,351)	788	-	184,052	17,833	(10,858)	191,027
Depreciation and Amortization	60,936	3,792	4,594	2,800	1,678	180	2,084	4,957	8,008	322	-	89,351	58,471	(90)	147,732
Operating Income (Loss)	72,218	12,951	8,166	7,667	2,053	(384)	4,495	1,428	(14,359)	466	-	94,701	(40,638)	(10,768)	43,295
Other (Loss) Income															
Interest expense	(13,472)	(1,223)	(1,928)	(385)	(414)	(72)	(270)	(1,187)	(960)	(64)	-	(19,975)	(28,407)	58	(48,324)
Investment (loss) income	(2,534)	(3,808)	(1,171)	101	(888)	(451)	(1,753)	(2,326)	(3,257)	(91)	-	(16,178)	(14,601)	(1,261)	(32,040)
Income tax expense	-	-	-	-	-	-	-	-	-	-	-	-	(7,519)	-	(7,519)
Inherent contribution	-	-	-	-	-	-	-	-	-	-	-	-	14,639	-	14,639
Loss on extinguishment of debt	(60)	(12)	(15)	-	-	-	-	-	-	-	-	(87)	-	-	(87)
Other	(338)	-	165	(419)	(1,257)	-	1	(315)	(408)	(152)	-	(2,723)	(2,390,327)	2,386,852	(6,198)
Total other (loss) income - Net	(16,404)	(5,043)	(2,949)	(703)	(2,559)	(523)	(2,022)	(3,828)	(4,625)	(307)	-	(38,963)	(2,426,215)	2,385,649	(79,529)
Excess of Revenue Over (Under) Expenses before Unusual Items	55,814	7,908	5,217	6,964	(506)	(907)	2,473	(2,400)	(18,984)	159	-	55,738	(2,466,853)	2,374,881	(36,234)
Restructuring, Severance, and Acquisition Costs Expense	-	-	-	-	-	-	-	-	-	-	-	-	(30,237)	-	(30,237)

ProMedica Health System and Subsidiaries

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

Year Ended December 31, 2018

(In Thousands)

	The Toledo Hospital	Defiance Hospital, Inc.	Bay Park Community Hospital	Emma L. Bixby Medical Center	Herrick Memorial Hospital, Inc.	Lenawee Long Term Care	Fostoria Hospital Association	Memorial Hospital	Mercy Memorial Hospital Corporation	ProMedica Continuing Care Services Corp.	Eliminations	Total Obligated Group	Nonobligated Group	Consolidating Adjustments and Eliminations	Consolidated ProMedica Health System and Subsidiaries Total
Excess of Revenue Over (Under) Expense	\$ 55,814	\$ 7,908	\$ 5,217	\$ 6,964	\$ (506)	\$ (907)	\$ 2,473	\$ (2,400)	\$ (18,984)	\$ 159	\$ -	\$ 55,738	\$ (2,497,090)	\$ 2,374,881	\$ (66,471)
Transfer (to) from Affiliate	(1,510,962)	(148,562)	(55,254)	(21,019)	(11,471)	-	(52,060)	5,922	12,927	6,449	-	(1,774,030)	1,762,604	11,426	-
Capital Contributions by Noncontrolling Members	-	-	-	-	-	-	-	-	-	-	-	-	41,173	-	41,173
Distributions to Noncontrolling Interests	-	-	-	-	-	-	-	-	-	-	-	-	(1,002)	-	(1,002)
Net Assets Released from Restriction for Fixed Assets	2,973	38	24	68	-	-	84	271	326	-	-	3,784	743	(569)	3,958
Pension and Other Postretirement Adjustments	(84)	-	-	(14)	45	-	-	-	-	-	-	(53)	(39,517)	-	(39,570)
Loss on Discontinued Operations	-	-	-	-	-	-	-	-	-	-	-	-	(21,935)	-	(21,935)
(Decrease) Increase in Net Assets without Donor Restriction	<u>\$ (1,452,259)</u>	<u>\$ (140,616)</u>	<u>\$ (50,013)</u>	<u>\$ (14,001)</u>	<u>\$ (11,932)</u>	<u>\$ (907)</u>	<u>\$ (49,503)</u>	<u>\$ 3,793</u>	<u>\$ (5,731)</u>	<u>\$ 6,608</u>	<u>\$ -</u>	<u>\$ (1,714,561)</u>	<u>\$ (755,024)</u>	<u>\$ 2,385,738</u>	<u>\$ (83,847)</u>