

Self Regional Healthcare and Affiliates

Combined Financial Statements

September 30, 2017 and 2016

Table of Contents

Independent Auditors' Report	1
Management's Discussion and Analysis	3
Combined Financial Statements:	
Combined Statements of Net Position	9
Combined Statements of Revenues, Expenses, and Changes in Net Position.....	11
Combined Statements of Cash Flows	12
Notes to Combined Financial Statements	14
Required Supplementary Information:	
Schedules of Changes in Net Pension Liability and Related Ratios.....	36
Schedules of Contributions	37

Independent Auditors' Report

Board of Trustees of
Self Regional Healthcare and Affiliates
Greenwood, South Carolina

Report on the Combined Financial Statements

We have audited the accompanying combined financial statements of Self Regional Healthcare and Affiliates (the "Hospital") comprised of the combined statements of net position as of September 30, 2017 and 2016 and the related combined statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of these combined 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 combined financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these combined financial statements based on our audits. We did not audit the consolidated financial statements of the Self Regional Healthcare Foundation and Subsidiary (the "Foundation"), a blended component unit of the Hospital, which statements reflect total assets of approximately \$7,851,000 and \$8,448,000 as of September 30, 2017 and 2016, respectively, and total revenues of approximately \$2,016,000 and \$2,194,000, respectively, for the years then ended. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Foundation, is based solely on the report of the other auditors. 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 combined financial statements are free of material misstatement.

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

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

Opinion

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of Self Regional Healthcare and Affiliates as of September 30, 2017 and 2016, and its changes in financial position and cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the Schedules of Changes in Net Pension Liability and Related Ratios, and the Schedules of Contributions be presented to supplement the basic combined financial statements. Such information, although not a part of the combined financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic combined financial statements in an appropriate operational, economic, or historical context.

We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the combined financial statements, and other knowledge we obtained during our audit of the combined financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Dixon Hughes Goodman LLP

**Greenville, South Carolina
December 18, 2017**

Management's Discussion and Analysis

Overview of the Combined Financial Statements

This discussion and analysis are intended to serve as an introduction to Self Regional Healthcare and Affiliates' (the "Hospital's") audited combined financial statements. The Hospital's combined financial statements are comprised of two components: 1) combined financial statements and 2) notes to the combined financial statements.

The combined financial statements include the Combined Statements of Net Position, Combined Statements of Revenues, Expenses, and Changes in Net Position, and Combined Statements of Cash Flows for the fiscal years ended September 30, 2017 and 2016. The Hospital operates similar to a private business and therefore utilizes the enterprise fund method of accounting. This method provides both long-term and short-term financial information and requires that revenue and expenses are recognized on the full accrual basis.

The Combined Statements of Net Position present information on all of the Hospital's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Hospital is improving or deteriorating.

The Combined Statements of Revenues, Expenses, and Changes in Net Position present information demonstrating how the Hospital's net position has changed during the most recent two fiscal years. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows.

The Combined Statements of Cash Flows presents information about the Hospital's cash flows resulting from operating, investing, noncapital financing, and capital financing activities. It reports cash receipts, cash payments, and changes in the cash balance during the most recent two fiscal years.

FINANCIAL HIGHLIGHTS

The assets and deferred outflows of Self Regional Healthcare and Affiliates exceeded its liabilities and deferred inflows at September 30, 2017 by \$532.4 million, which represents the amount of Hospital's net position. This amount may be used to meet the Hospital's ongoing financial obligations and to finance capital improvement and expansion of services in the future.

The Hospital's total net position increased \$11.1 million in the twelve-month period ended September 30, 2017. This increase primarily represents the amount of excess revenues over expenses for the fiscal year along with the change in restricted net position. The following is an analysis of Self Regional Healthcare and Affiliates' financial performance in fiscal year 2017.

**Self Regional Healthcare And Affiliates
Management's Discussion and Analysis
September 30, 2017 and 2016**

FINANCIAL ANALYSIS

Total Assets and Deferred Outflows

Table 1 illustrates the changes in total assets and deferred outflows of the hospital in fiscal year 2017.

Table 1
Self Regional Healthcare and Affiliates
Summary of Assets and Deferred Outflows
(in millions of dollars)

	<u>2017</u>	<u>2016</u>
Current assets	\$ 81.1	\$ 86.1
Capital assets, net of accumulated depreciation	225.4	220.4
Investments and assets whose use is limited	449.8	473.1
Other assets	1.9	1.4
Deferred outflows	<u>2.4</u>	<u>2.9</u>
Total assets and deferred outflows	<u>\$ 760.6</u>	<u>\$ 783.9</u>

Current assets decreased \$5.0 million due primarily to a decrease in net accounts receivable of \$4.6 million. Investments and assets whose use is limited decreased \$23.3. This decrease is the result of the cash defeasance of the Series 2004B variable rate bonds whose principal balance at the time of the defeasance was \$25.0 million. Capital assets, net increased \$5.0 million. Table 2 demonstrates the increases in capital assets.

Table 2
Self Regional Healthcare and Affiliates
Capital Assets
(in millions of dollars)

	<u>2017</u>	<u>2016</u>
Land and land improvements	\$ 10.9	\$ 10.2
Buildings	298.2	290.1
Fixed equipment	27.6	26.4
Movable and other equipment	<u>184.6</u>	<u>173.7</u>
Gross capital assets	521.3	500.4
Less accumulated depreciation	(312.1)	(293.4)
Construction in progress	<u>16.2</u>	<u>13.4</u>
Capital assets	<u>\$ 225.4</u>	<u>\$ 220.4</u>

This year's major capital asset additions include:

- Acquisition or construction of four medical office buildings.
- Healthcare software system and hardware costs for Self Medical Group.
- Healthcare software system and hardware costs for Self Regional Hospital.

**Self Regional Healthcare And Affiliates
Management's Discussion and Analysis
September 30, 2017 and 2016**

Total Liabilities, Deferred Inflows, and Net Position

Table 3 illustrates the changes in liabilities and the change in net position.

Table 3
Self Regional Healthcare and Affiliates
Summary of Liabilities, Deferred Inflows, and Net Position
(in millions of dollars)

	<u>2017</u>	<u>2016</u>
Current liabilities	\$ 57.2	\$ 61.2
Long-term liabilities	<u>163.8</u>	<u>197.1</u>
Total liabilities	221.0	258.3
Deferred inflows	<u>7.2</u>	<u>4.4</u>
Unrestricted net position	440.3	461.2
Invested in capital assets, net of related debt	79.3	47.5
Restricted for debt service	8.4	8.3
Nonexpendable	1.0	1.0
Restricted for specific purposes	<u>3.4</u>	<u>3.2</u>
Total net position	<u>532.4</u>	<u>521.2</u>
Total liabilities, deferred inflows, and net position	<u>\$ 760.6</u>	<u>\$ 783.9</u>

The decrease in current liabilities is the result of a reduction in accrued salaries, wages and benefits as well as a reduction in estimated third-party payor settlements. The cash defeasance of the Series 2004B variable rate bonds in conjunction with a \$6.1 million decrease in in the defined benefit plan liability resulted in the decrease in long-term liabilities. Please see the notes to the financial statements for a more complete explanation of long-term liabilities as well as the deferred inflows. Invested in capital assets, net of related debt increased \$31.8 million due to the reduction in debt as well as the net increase in capital assets. The total net position increased \$11.2 million which represents the change in net position for fiscal year 2017.

**Self Regional Healthcare And Affiliates
Management's Discussion and Analysis
September 30, 2017 and 2016**

Total Operating Revenues

Table 4 illustrates the changes in operating revenues for fiscal year 2017 and 2016.

Table 4
Self Regional Healthcare and Affiliates
Summary of Total Operating Revenues
(in millions of dollars)

	<u>2017</u>	<u>2016</u>
Inpatient revenue	\$ 436.9	\$ 429.0
Outpatient revenue	<u>698.2</u>	<u>655.4</u>
Gross patient service charges	1,135.1	1,084.4
Contractual allowances	697.9	670.1
Provision for bad debts	<u>39.7</u>	<u>48.1</u>
Total revenue deductions	737.6	718.2
Net patient service revenue	397.5	366.2
Other operating revenue	<u>8.3</u>	<u>7.6</u>
Total operating revenues	<u>\$ 405.8</u>	<u>\$ 373.8</u>

In fiscal year 2017, gross patient service charges increased 4.7% due to increases in outpatient services revenue. Revenue deductions increased 2.7% in fiscal 2017 due to volume increases. Net patient service revenue increased 8.5% in fiscal year 2017. Excluded from gross patient service revenue for 2017 is \$36.2 million of charity care charges provided by Self Regional Healthcare and Affiliates.

Table 5 presents gross patient service charges by payor type in fiscal year 2017 and 2016 for Self Regional Healthcare and Affiliates.

Table 5
Self Regional Healthcare and Affiliates
Gross Patient Services Charges by Payor Type

	<u>2017</u>	<u>2016</u>
Medicare	54.3%	53.8%
Medicaid	12.2%	12.3%
Commercial	26.7%	26.6%
Uninsured	<u>6.8%</u>	<u>7.3%</u>
Total	<u>100.0%</u>	<u>100.0%</u>

**Self Regional Healthcare And Affiliates
Management's Discussion and Analysis
September 30, 2017 and 2016**

Table 6 presents revenue deductions as a percentage of gross patient service charges in fiscal year 2017 and 2016 for Self Regional Healthcare and Affiliates.

**Table 6
Self Regional Healthcare and Affiliates
Revenue Deductions as a Percentage of Gross Patient Services Revenue**

	<u>2017</u>	<u>2016</u>
Medicare & Medicaid	46.6%	49.1%
Provision for bad debts	3.4%	4.4%
Charity write-offs	3.1%	3.0%
Other	<u>11.9%</u>	<u>9.7%</u>
Total	<u>65.0%</u>	<u>68.2%</u>

Deductions from gross patient service charges represents the difference between charges and the amount of payment received for services provided. Medicare and Medicaid deductions are the largest category and represent a significant portion of the total deductions. The next largest category, Other, is mostly deductions resulting from contracts with managed care companies along with deductions from other governmental payors such as Champus. Bad debt results from patients who choose not to pay for their services without providing evidence of the lack of financial means to do so. Charity write-offs are provided primarily to uninsured patients who do not have the financial means to pay for their healthcare services.

Operating Expenses

Table 7 presents a percentage of operating expense by major category for fiscal year 2017 and 2016 for Self Regional Healthcare and Affiliates.

**Table 7
Self Regional Healthcare and Affiliates
Composition of Operating Expenses**

	<u>2017</u>	<u>2016</u>
Salaries, wages, and benefits	55.1%	55.7%
Supplies	17.7%	18.0%
Professional fees and other	20.8%	18.9%
Depreciation and amortization	<u>6.4%</u>	<u>7.4%</u>
Total	<u>100.0%</u>	<u>100.0%</u>

**Self Regional Healthcare And Affiliates
Management’s Discussion and Analysis
September 30, 2017 and 2016**

DEBT

Outstanding Debt

Table 8 details the composition of long-term debt at September 30, 2017 and 2016. The Hospital had \$146.1 million in outstanding debt, a decrease of \$26.8 million or 15.5% from fiscal year 2016.

Table 8
Self Regional Healthcare and Affiliates
Outstanding Debt
(in millions of dollars)

	<u>2017</u>	<u>2016</u>
Revenue bonds and notes payable	\$ 146.0	\$ 172.6
Capital leases	<u>0.1</u>	<u>0.3</u>
Total	<u>\$ 146.1</u>	<u>\$ 172.9</u>

As previously mentioned the Hospital cash defeased the series 2004B variable rate bonds whose principal outstanding at the time of the defeasance was \$25.0 million. Please refer to the Note 7 in the Footnotes for a detailed explanation of the hospitals debt position.

SUBSEQUENT EVENTS

Series 2017 Bond Issuance

Hospital Facility Refunding Revenue Bonds – Series 2017, were issued in October 2017. The proceeds from the issue were used to refund the outstanding principal of the Series 2009 bonds and to pay the cost of issuance.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of Self Regional Healthcare and Affiliates’ finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Self Regional Healthcare
Chief Financial Officer
1325 Spring Street
Greenwood, SC 29646

Self Regional Healthcare and Affiliates
Combined Statements of Net Position
September 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
ASSETS AND DEFERRED OUTFLOWS		
Current assets:		
Cash and cash equivalents	\$ 15,821,412	\$ 13,222,268
Assets whose use is limited	3,372,538	3,360,703
Patient accounts receivable, less allowance for uncollectible accounts of approximately \$25,733,000 in 2017 and \$25,075,000 in 2016	54,218,331	58,857,462
Inventories of drugs and supplies	2,601,847	2,692,960
Unconditional promises to give, net	400,246	446,086
Deposits, other receivables, and prepaid expenses	4,730,541	7,564,647
	<u>81,144,915</u>	<u>86,144,126</u>
Total current assets		
Assets whose use is limited, net of current portion	446,655,663	470,462,478
Investments	3,156,028	2,677,391
Physician receivables, net	354,557	52,404
Capital assets, net	225,386,408	220,445,181
Unconditional promises to give, net of current portion	1,015,906	727,864
Other assets	505,695	615,603
	<u>758,219,172</u>	<u>781,125,047</u>
Total assets		
Deferred outflows:		
Pension deferrals	2,431,614	2,848,152
	<u>2,431,614</u>	<u>2,848,152</u>
Total deferred outflows		
	<u>760,650,786</u>	<u>783,973,199</u>
Total assets and deferred outflows		

**Self Regional Healthcare and Affiliates
 Combined Statements of Net Position
 September 30, 2017 and 2016**

(Continued)

	<u>2017</u>	<u>2016</u>
LIABILITIES, DEFERRED INFLOWS, AND NET POSITON		
Current liabilities:		
Current installments of long-term debt	\$ 1,403,959	\$ 1,046,232
Accounts payable	20,392,810	19,149,640
Accrued salaries, wages and benefits	15,345,419	16,361,737
Other accrued expenses	6,379,818	6,812,033
Pledge payable	-	1,200,000
Estimated third-party payor settlements	13,657,864	16,582,735
Total current liabilities	<u>57,179,870</u>	61,152,377
Net pension liability	16,210,061	22,284,948
Annuity obligations	44,367	54,637
Other postemployment benefit obligation	2,912,194	2,912,194
Long-term debt, excluding current installments	144,709,144	171,869,585
Total liabilities	<u>221,055,636</u>	258,273,741
Deferred inflows:		
Pension deferrals	7,219,981	4,427,228
Total deferred inflows	<u>7,219,981</u>	4,427,228
Net position:		
Net investment in capital assets	79,273,305	47,529,364
Restricted:		
Held by trustee under indenture agreement	8,328,931	8,306,179
Held under employee benefit plan agreement	58,331	33,678
By donor for specific activities or capital acquisitions	3,468,380	3,191,950
Nonexpendable	970,393	1,034,419
Unrestricted	440,275,829	461,176,640
Total net position	<u>532,375,169</u>	521,272,230
Total liabilities, deferred inflows, and net position	<u>\$ 760,650,786</u>	<u>\$ 783,973,199</u>

See accompanying notes.

Self Regional Healthcare and Affiliates
Combined Statements of Revenues, Expenses, and Changes in Net Position
Years Ended September 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Operating revenues:		
Net patient service revenue, net of provision for bad debts of approximately \$39,727,000 in 2017 and \$48,099,000 in 2016	\$ 397,515,391	\$ 366,195,859
Other operating revenue	8,347,929	7,583,064
Total operating revenues	<u>405,863,320</u>	<u>373,778,923</u>
Operating expenses:		
Salaries and wages	173,720,391	158,289,071
Employee benefits	43,054,196	38,083,667
Supplies	69,684,933	63,462,361
Professional fees	14,977,565	13,656,241
Other expense	66,954,817	52,759,934
Depreciation and amortization	25,098,660	26,123,376
Total operating expenses	<u>393,490,562</u>	<u>352,374,650</u>
Operating income	<u>12,372,758</u>	<u>21,404,273</u>
Nonoperating revenues (expenses):		
Interest expense	(6,611,448)	(6,262,204)
Investment income, net	6,600,010	14,690,690
Rental income, net	139,988	(25,436)
Noncapital grants and contributions	1,493,338	2,394,980
Contribution expense	(19,620)	(385,157)
Fundraising expense	(495,374)	(112,085)
Depreciation for Foundation	(75,500)	(106,276)
Other	(1,770,048)	(772,685)
Total nonoperating revenues (expenses)	<u>(738,654)</u>	<u>9,421,827</u>
Excess of revenues over expenses	11,634,104	30,826,100
Contributions	32,335	-
Distributions to owners	<u>(563,500)</u>	<u>(595,350)</u>
Increase in net position	11,102,939	30,230,750
Net position, beginning of year	<u>521,272,230</u>	<u>491,041,480</u>
Net position, end of year	<u>\$ 532,375,169</u>	<u>\$ 521,272,230</u>

See accompanying notes.

Self Regional Healthcare and Affiliates
Combined Statements of Cash Flows
Years Ended September 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Receipts from and on behalf of patients	\$ 399,229,651	\$ 355,264,188
Other receipts and payments, net	8,543,389	10,697,243
Payments to suppliers and contractors	(154,923,738)	(131,175,819)
Payments to employees	(217,790,905)	(192,686,054)
Net cash provided by operating activities	<u>35,058,397</u>	<u>42,099,558</u>
Cash flows from noncapital financing activities:		
Net change in unconditional promises to give	(242,202)	(244,308)
Net change in annuity obligations	(10,270)	(12,472)
Receipts from noncapital grants and contributions	1,493,338	2,394,980
Net cash provided by noncapital financing activities	<u>1,240,866</u>	<u>2,138,200</u>
Cash flows from capital and related financing activities:		
Purchase of capital assets	(29,264,801)	(29,942,050)
Proceeds from sale of capital assets	1,280,051	47,098
Proceeds from long-term debt	2,187	-
Principal paid on long-term debt	(26,012,775)	(1,546,926)
Interest paid on long-term debt	(6,944,915)	(6,272,431)
Net cash used in capital and related financing activities	<u>(60,940,253)</u>	<u>(37,714,309)</u>
Cash flows from investing activities:		
Proceeds from sale of investments	155,456,304	171,717,166
Purchases of investments	(139,977,273)	(198,601,736)
Gain from investment	6,524,510	14,584,682
Contributions	32,335	-
Distributions paid	(563,500)	(595,350)
Other	(2,069,554)	(1,369,384)
Net cash provided by (used in) investing activities	<u>19,402,822</u>	<u>(14,264,622)</u>
Net decrease in cash and cash equivalents	(5,238,168)	(7,560,876)
Cash and cash equivalents, beginning of year	<u>40,728,345</u>	<u>48,289,221</u>
Cash and cash equivalents, end of year	<u>\$ 35,490,177</u>	<u>\$ 40,728,345</u>

Self Regional Healthcare and Affiliates
Combined Statements of Cash Flows
Years Ended September 30, 2017 and 2016

(Continued)

	<u>2017</u>	<u>2016</u>
Reconciliation of cash and cash equivalents to the combined statements of net position:		
Cash and cash equivalents in current assets	\$ 15,821,412	\$ 13,222,268
Cash and cash equivalents in investments	85,108	34,918
Cash and cash equivalents in assets whose use is limited:		
Internally designated	11,048,227	18,773,933
Held by trustee under debt indenture	8,328,931	8,306,179
Under employee benefit plan agreement	58,331	33,678
Donor restricted for specific activities or capital acquisitions	148,168	357,369
	<u>35,490,177</u>	<u>40,728,345</u>
Total cash and cash equivalents	<u>\$ 35,490,177</u>	<u>\$ 40,728,345</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 12,372,758	\$ 21,404,273
Adjustments to reconcile operating income to net cash provided by operating activities:		
Provision for bad debts	39,727,322	48,098,799
Depreciation and amortization	25,098,660	26,123,376
Loss on disposal of capital assets	1,281,075	2,963,750
Change in net operating assets and liabilities:		
Patient accounts receivable, net	(35,088,191)	(59,125,375)
Deposits, other receivables and prepaid expenses	2,834,106	(2,277,149)
Inventories of drugs and supplies	91,113	(190,134)
Physician receivables, net	(302,153)	63,854
Other assets and deferred outflows	416,538	1,286,575
Accounts payable, accrued salaries, wages and benefits and other accrued expenses	(3,965,826)	7,131,856
Other liabilities and deferred inflows	(3,282,134)	(2,275,172)
Pledge payable	(1,200,000)	(1,200,000)
Estimated third-party payor settlements	(2,924,871)	94,905
	<u>35,058,397</u>	<u>42,099,558</u>
Net cash provided by operating activities	<u>\$ 35,058,397</u>	<u>\$ 42,099,558</u>
Noncash investing and financing activities:		
Acquisition of equipment through accounts payable	<u>\$ 4,093,930</u>	<u>\$ 3,286,783</u>

See accompanying notes.

Notes to Combined Financial Statements

1. Description of Reporting Entity and Summary of Significant Accounting Policies

Reporting entity

The Greenwood County Hospital Board (the "Board") is a public body corporate of South Carolina and was established by Act No. 1554 enacted by the General Assembly of the State of South Carolina on May 30, 1968. The members of the Board are appointed by the Governor of the State of South Carolina upon recommendation of the Board and the Greenwood County legislative delegation. The Board is empowered to operate Self Regional Healthcare ("SRH"), an acute care facility located in Greenwood, South Carolina, and other health care facilities as are necessary and convenient to benefit the residents of Greenwood County. The Board leases the original main hospital building and the land on which it stands from Greenwood County. The lease expires in 2047 and provides for annual rent of \$1. Although legal title to the property is held by Greenwood County, such assets are recorded on the books of Self Regional Healthcare and reflected in the accompanying combined financial statements at the original cost to Greenwood County.

Self Memorial Regional Health Services, Inc. ("SMRHS") is a not-for-profit corporation established by the Board to provide health related services to the residents of Greenwood County and the surrounding area. The Board is the sole member and appoints the Board of Trustees of SMRHS. Further, SMRHS operates for the benefit of the Board and Self Regional Healthcare. Accordingly, SMRHS is reported as a blended component unit of SRH, the primary government.

SMRHS formed The Surgery Center at Self Memorial Hospital L.L.C. d/b/a Surgery Center of the Lakelands (the "Surgery Center"). The Surgery Center, a joint venture with qualified physician investors, commenced operations during 2001. Under the terms of the operating agreement, SMRHS retains at least a 51% ownership in the Surgery Center. The remaining ownership percentage has been designated as restricted nonexpendable net position on the combined statements of net position.

Self Regional Physician Services L.L.C. ("SRPS") is a wholly-owned subsidiary of Self Regional Healthcare. When formed, SRPS purchased substantially all of the assets of a physician group practice for the purpose of operating one or more physician group practices in the region. SRPS is controlled by the Board. Accordingly, SRPS is reported as a blended component unit of the SRH, the primary government.

Self Regional Healthcare Foundation and Subsidiary (the "Foundation") was organized as an eleemosynary corporation on January 9, 1985. The purpose of the Foundation is to receive, hold, manage, invest, or arrange for investing and to acquire by gift, devise, bequest, purchase or otherwise use of property of any kind and funds exclusively for the benefit of Self Regional Healthcare and any other publicly supported hospitals in the State of South Carolina. Members of the Board of Trustees of the Foundation are approved by the Board. Accordingly, the Foundation is reported as a blended component unit of the SRH, the primary government.

The Foundation is the sole shareholder of Greenwood Medical Company, Inc. (the "Subsidiary"), a for profit corporation. The Subsidiary was formed to own several medical buildings in Greenwood, South Carolina, and leases space to a variety of physician practices, laboratories, and durable medical equipment suppliers for medical practice sites. Accordingly, the accounts of the Subsidiary have been consolidated with the Foundation.

Self Memorial Hospital Auxiliary, Inc. (the "Auxiliary") was organized as a not-for-profit entity on July 12, 1971. This corporation was established to engage in activities that are devoted to charitable purposes, and shall promote, enhance, and support SRH. Members of the Board of Trustees of the Auxiliary are approved by the Board. Accordingly, the Auxiliary is reported as a blended component unit of SRH, the primary government.

Self Regional Healthcare and Affiliates Notes to Combined Financial Statements

Self Medical Group, Inc. (“SMG”) was organized as a not-for-profit entity on July 27, 2009. This corporation was established to employ and manage physician practices. Members of the Board of Trustees of SMG are appointed by the Board. Accordingly, SMG is reported as a blended component unit of the SRH, the primary government.

Affiliation with Edgefield County Hospital

In September 2017, the Hospital and Edgefield County Hospital (“ECH”) signed a letter of intent to execute a Facility and Equipment Lease Agreement and Hospital Operating Agreement where the Hospital will be operating ECH’s hospital facilities as part of the Hospital. The proposed initial term of the affiliation is 10 years with succeeding automatic renewal periods of 5 years each.

Combined financial statements

The accompanying combined financial statements include the accounts of SRH, SMRHS, the Surgery Center, SRPS, the Foundation, the Auxiliary, and SMG, jointly referred to as Self Regional Healthcare and Affiliates (the “Hospital”). All intercompany balances between these entities have been eliminated in the combination.

Enterprise fund accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Pursuant to Governmental Accounting Standards Board (“GASB”) Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements, the Hospital will only recognize GASB statements as authoritative guidance. Financial Accounting Standards Board (“FASB”) statements, including those issued after November 30, 1989 and AICPA pronouncements will no longer be authoritative and may be used as non-authoritative guidance.

Use of estimates

The preparation of the Hospital’s combined financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the combined financial statements and accompanying notes. Actual results could differ from those estimates and assumptions.

Cash and cash equivalents

The Hospital considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

The Hospital maintains bank accounts at various financial institutions covered by the Federal Deposit Insurance Corporation (“FDIC”). At various times throughout the year, the Hospital may maintain bank account balances in excess of FDIC insured limits. At September 30, 2017 and 2016, the Hospital’s deposits had a carrying amount of approximately \$15,821,000 and \$13,222,000, respectively, and a bank balance of approximately \$18,624,000 and \$17,358,000, respectively. The Hospital had cash on hand of approximately \$14,000 and \$13,000 at September 30, 2017 and 2016, respectively.

Patient accounts receivable

Patient accounts receivable are carried at the original charge less an estimate made for doubtful or uncollectible accounts. The estimate for doubtful or uncollectible accounts is based upon a review of the outstanding balances aged by financial class. Management uses historical collection percentages to determine collectability. Management also reviews troubled, aged accounts to determine collection potential. Patient accounts receivable are written off when deemed uncollectible. Recoveries of accounts previously written off are recorded as a reduction to provision for bad debts when received. Interest is not charged on patient accounts receivable.

Inventories of drugs and supplies

Inventories of drugs and supplies are stated at the lower of cost, determined using the first-in, first-out method, or market.

**Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements**

Unconditional promises to give, net

Unconditional promises to give cash and other assets to the Foundation 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. An allowance for uncollectible unconditional promises to give is estimated based on past experience and on analysis of collectability.

Investments in debt and equity securities

Investments in debt and equity securities are reported at fair value. Interest, dividends, and gains and losses, both realized and unrealized, on investments in debt and equity securities are included in nonoperating revenues (expenses) when earned.

Assets whose use is limited

Assets whose use is limited include cash and cash equivalents and investments that are internally designated for operations and capital improvement, held by trustee under indenture agreement, for employee benefit plan agreement, and restricted by donor. The current portion of assets whose use is limited is assets held by trustee under indenture agreement that will be paid in the following year.

Capital assets

The Hospital's policy is to capitalize any capital asset with a unit cost of \$1,500 or more. Capital assets are reported at historical cost. Contributed capital assets are reported at their estimated fair value at the time of their donation. All capital assets other than land are depreciated or amortized (in the case of capital leases) using the straight-line method of depreciation using these asset lives or lease periods:

Land improvements	3 to 25 years
Buildings and building fixtures	5 to 30 years
Fixed equipment	5 to 20 years
Major movable equipment	3 to 20 years

When properties are retired or otherwise disposed of, the cost of the assets and related allowances for depreciation are removed from the accounts, and any resulting gain or loss is recognized in operating income on the combined statement of revenues, expenses, and changes in net position.

Costs of borrowing

Except for capital assets acquired through gifts, contributions or capital grants, interest cost on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquisition of those assets.

Annuity obligations

The Foundation has received charitable gift annuities as contributions. The donors contributed assets to the Foundation or placed the assets under an irrevocable trust agreement in exchange for a promise by the Foundation to pay fixed amounts to the donors for the remainder of their lives. The Foundation has recognized the asset or beneficial interests received and the related liability for the annuity payments.

Net position

Net position of the Hospital is classified in three components. Net investment in capital assets consists of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted net position are noncapital and capital net position that must be used for a particular purpose, as specified by creditors, grantors, trustees, or donors external to the Hospital. Nonexpendable restricted net position represents the portion of net position attributable to non-controlling interests. Unrestricted net position are remaining net position that do not meet the definition of net

Self Regional Healthcare and Affiliates Notes to Combined Financial Statements

investment in capital assets or restricted. The Hospital first applies restricted net position when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

Net patient service revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Third-party contractual revenue adjustments are accrued on an estimated basis in the period the related services are rendered. Such amounts are subject to audit by governmental agencies. Adjustments, if any, are included in contractual revenue adjustments in the year of determination. In compliance with GASB pronouncements, net patient service revenues have been reduced by the amount of provision for bad debts incurred by the Hospital.

The Hospital's policy does not require collateral or other security for patient accounts receivable. The Hospital routinely accepts assignment of, or is otherwise entitled to receive, patient benefits payable under health insurance programs, plans or policies such as those related to Medicare, Medicaid, Blue Cross, health maintenance organizations and commercial insurance carriers.

Charity care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as net patient service revenue. The amounts of direct and indirect costs foregone for services and supplies furnished under the Hospital's charity care policy totaled approximately \$11,135,000 and \$9,647,000 for the years ended September 30, 2017 and 2016, respectively, and is based on a ratio of the Hospital's operating expenses to its gross patient service charges.

Operating revenues and expenses

The Hospital's combined statement of revenues, expenses, and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, the Hospital's principal activity. Nonexchange revenues including grants and contributions received for purposes other than capital asset acquisition are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide healthcare services, other than financing costs.

Grants and contributions

From time to time, the Hospital receives grants from Federal and state agencies as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

Fundraising

The Foundation incurs expenses related to obtaining contributions and grants which are included in other nonoperating expenses.

Amortization

Bond discounts and premiums are amortized over the respective lives of the bonds.

Income taxes

SRH, SMRHS, the Foundation, the Auxiliary, and SMG have been recognized by the Internal Revenue Service as not-for-profit organizations as described in section 501(c)(3) of the Internal Revenue Code ("IRC") and are exempt from federal income taxes pursuant to section 501(a) of the IRC. SRPS, as a wholly-owned limited liability

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

partnership of SMRHS, is not subject to federal income taxes. The Surgery Center is a limited liability company and, therefore, is not subject to income taxes. Greenwood Medical Company, Inc., as a wholly-owned subsidiary of the Foundation, is a for-profit entity, and as such, is subject to federal and state income taxes. The Hospital has determined that it does not have any material unrecognized tax benefits or obligations as of September 30, 2017.

Compensated absences

The majority of the Hospital’s employees earn paid time off (“PTO”) at varying rates depending on years of service. Accumulated PTO time may be carried over each year up to a maximum amount, depending on years of service.

Risk management

The Hospital is exposed to various risks of loss including torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice; and, employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years. The Hospital is self-insured for amounts up to a specified level for health and medical coverage for its employees. The estimated liability is the total estimated amount to be paid for all known claims or incidents and a reserve for incurred but not reported claims.

Reclassifications

Certain reclassifications to net patient service revenue, other operating revenue, and operating expenses have been made to the 2016 amounts to conform to the 2017 combined financial statement presentation.

2. Assets Whose Use Is Limited

The Hospital’s investments generally are reported at fair value, as discussed in Note 1, and included in the assets whose use is limited on the combined statements of net position. At September 30, 2017 and 2016, the Hospital had the following investments with set maturities, all of which were held in the Hospital’s name by a custodial bank that is the agent of the Hospital.

September 30, 2017	Carrying Amount	Investment Maturities (in Years)			
		Less Than 1	1-5	6-10	More Than 10
Investment Type:					
U.S. Treasury obligations	\$ 12,551,240	\$ 1,744,050	\$ 5,545,835	\$ 5,261,355	\$ -
U.S. Municipal bonds	3,362,401	-	3,362,401	-	-
U.S. Corporate bonds	138,754,890	11,895,427	93,715,450	31,147,653	1,996,360
U.S. Government bonds	185,602,723	13,146,532	86,176,989	15,111,929	71,167,273
Foreign bonds and notes	6,004,149	-	6,004,149	-	-
Total	\$346,275,403	\$ 26,786,009	\$194,804,824	\$ 51,520,937	\$ 73,163,633

September 30, 2016	Carrying Amount	Investment Maturities (in Years)			
		Less Than 1	1-5	6-10	More Than 10
Investment Type:					
U.S. Treasury obligations	\$ 25,220,850	\$ -	\$ 21,153,810	\$ 4,067,040	\$ -
U.S. Municipal bonds	4,502,977	-	4,502,977	-	-
U.S. Corporate bonds	151,609,092	-	121,603,274	25,947,398	4,058,420
U.S. Government bonds	179,660,064	76,780	84,488,243	21,930,603	73,164,438
Foreign bonds and notes	4,740,300	-	4,740,300	-	-
Total	\$365,733,283	\$ 76,780	\$236,488,604	\$ 51,945,041	\$ 77,222,858

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

The composition of assets whose use is limited at September 30, 2017 and 2016 is set forth in the following table. The Hospital's investments included in assets whose use is limited are categorized to give an indication of the level of risk assumed by the Hospital. Assets whose use is limited are comprised of the following:

	<u>2017</u>	<u>2016</u>
Internally designated for operations and capital improvements:		
Cash	\$ 1,603,654	\$ 1,597,873
Money market funds	9,444,573	17,176,060
U. S. Municipal bonds	3,362,401	4,502,977
U. S. Treasury obligations	12,551,240	25,220,850
U. S. Government bonds	185,602,723	179,660,064
U. S. Mutual funds	64,895,810	65,121,929
U. S. Corporate bonds	137,694,930	151,045,086
Foreign bonds and notes	6,004,149	4,740,300
Multi-manager structured product	14,843,000	11,028,000
Accrued interest	<u>2,067,077</u>	<u>2,222,618</u>
	<u>438,069,557</u>	<u>462,315,757</u>
Held by trustee under indenture agreement:		
Cash	<u>8,328,931</u>	<u>8,306,179</u>
Held under employee benefit plan agreement:		
Cash	<u>58,331</u>	<u>33,678</u>
Donor restricted for specific activities or capital acquisitions:		
Money market funds	148,168	357,369
U. S. Corporate bonds	1,059,960	564,006
U. S. Equities	1,918,168	1,913,500
Foreign equities	150,114	130,839
Exchange traded funds	<u>294,972</u>	<u>201,853</u>
	<u>3,571,382</u>	<u>3,167,567</u>
Total	450,028,201	473,823,181
Less current portion	<u>3,372,538</u>	<u>3,360,703</u>
Long term portion	<u>\$ 446,655,663</u>	<u>\$ 470,462,478</u>

Interest rate risk

This is the risk that changes in interest rates will adversely affect the fair value of an investment. The Hospital's Investment Policy authorizes a strategic asset allocation that is designed to provide an optimal return over the Hospital's investment horizon and within the Hospital's risk tolerance and cash requirements.

Investment income, net consists of the following:

	<u>2017</u>	<u>2016</u>
Interest and dividend income	\$ 6,971,853	\$ 7,106,097
Increase (decrease) in fair value of investments, net	<u>(371,843)</u>	<u>7,584,593</u>
Investment income, net	<u>\$ 6,600,010</u>	<u>\$ 14,690,690</u>

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

Custodial credit risk

The Hospital's deposits are exposed to custodial credit risk if they are not covered by depository insurance and deposits are uncollateralized or are collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name. The deposit risk is that, in the event of the failure of a depository financial institution, the Hospital will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

Credit risk

This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Hospital's investment policy provides guidelines for its fund managers and lists specific allowable investments so that no more than 15% of the portfolio's market value may be held in the lowest investment grade category ("BBB" or "BBB+"). As of September 30, 2017 and 2016, the credit ratings assigned to the Hospital's applicable securities by a nationally recognized credit rating agency were rated "A-" or better except for approximately \$24,110,000 and \$22,031,000, respectively, that were rated "BAA" or "BBB+."

Concentration of credit risk

The Hospital places no limit on the amount it may invest in any one issuer. The Hospital held less than 5% of the carrying amount of investments in any one issuer as of September 30, 2017 and 2016.

3. Fair Value of Financial Investments

The Fair Value Measurements and Application Standard addresses accounting and financial reporting issues related to fair value measurements. The standard describes fair value as an exit price. The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This statement provides guidance for determining a fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements.

The statement establishes a three-level hierarchy of inputs to valuation techniques used to measure fair value. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets or liabilities, inputs that are observable for the asset or liability, and market-corroborated inputs. Level 3 inputs are unobservable inputs and take into account all information about market participant assumptions that are reasonably available. The Hospital categorizes its fair value measurements within the fair value hierarchy established by this standard.

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

For assets carried at fair value, the following table provides fair value information as of September 30, 2017 and 2016:

Fair value measurements at September 30, 2017				
		Quoted prices In active markets for identical assets and liabilities (Level 1)	Quoted prices for similar assets and liabilities (Level 2)	Significant unobservable inputs (Level 3)
	<u>Fair value at Sept 30, 2017</u>			
<i>Investments by fair value level</i>				
Money market accounts	\$ 9,592,741	\$ 9,592,741	\$ -	\$ -
U.S. Municipal bonds	3,362,401	3,362,401	-	-
U.S. Treasury obligations	12,551,240	12,551,240	-	-
U.S. Government bonds	185,602,723	185,602,723	-	-
U.S. Mutual funds	67,966,730	67,966,730	-	-
U.S. Corporate bonds	138,754,890	138,754,890	-	-
U.S. equities	1,918,168	1,918,168	-	-
Foreign equities	150,114	150,114	-	-
Foreign bonds and notes	6,004,149	6,004,149	-	-
Exchange traded funds	294,972	294,972	-	-
Multi-manager structured product	<u>14,843,000</u>	<u>-</u>	<u>-</u>	<u>14,843,000</u>
Total investments by level	<u>\$ 441,041,128</u>	<u>\$ 426,198,128</u>	<u>\$ -</u>	<u>\$ 14,843,000</u>

At September 30, 2017, approximately \$10,076,000 in cash and \$2,067,000 in accrued interest are included in assets whose use is limited on the statements of net position.

Fair value measurements at September 30, 2016				
		Quoted prices In active markets for identical assets and liabilities (Level 1)	Quoted prices for similar assets and liabilities (Level 2)	Significant unobservable inputs (Level 3)
	<u>Fair value at Sept 30, 2016</u>			
<i>Investments by fair value level</i>				
Money market accounts	\$ 17,533,429	\$ 17,533,429	\$ -	\$ -
U.S. Municipal bonds	4,502,977	4,502,977	-	-
U.S. Treasury obligations	25,220,850	25,220,850	-	-
U.S. Government bonds	179,660,064	179,660,064	-	-
U.S. Mutual funds	67,764,402	67,764,402	-	-
U.S. Corporate bonds	151,609,092	151,609,092	-	-
U.S. equities	1,913,500	1,913,500	-	-
Foreign equities	130,839	130,839	-	-
Foreign bonds and notes	4,740,300	4,740,300	-	-
Exchange traded funds	201,853	201,853	-	-
Multi-manager structured product	<u>11,028,000</u>	<u>-</u>	<u>-</u>	<u>11,028,000</u>
Total investments by level	<u>\$ 464,305,306</u>	<u>\$ 453,277,306</u>	<u>\$ -</u>	<u>\$ 11,028,000</u>

Self Regional Healthcare and Affiliates Notes to Combined Financial Statements

At September 30, 2016, approximately \$9,973,000 in cash and \$2,223,000 in accrued interest are included in assets whose use is limited on the statements of net position.

Money markets accounts, common stocks, bond and stock mutual funds, structured notes, and exchange traded funds classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

Multi Manager Structured fund classified as Level 3 is valued using fundamental analysis of underlying securities.

4. Net Patient Service Revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare

Inpatient acute care 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. Outpatient services are reimbursed under a prospective payment system called the Ambulatory Payment Classification System ("APCs"). Inpatient nonacute services and defined capital and medical education costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items on a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through 2010.

Medicaid

Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Outpatient services are reimbursed at prospectively determined rates per procedure. The Hospital's Medicaid cost reports have been audited by the Medicaid fiscal intermediary through 2012.

Revenue from the Medicare and Medicaid programs accounted for approximately 50 percent and 9 percent, respectively, of the Hospital's net patient service revenue for the year ended September 30, 2017. Revenue from the Medicare and Medicaid programs accounted for approximately 45 percent and 9 percent, respectively, of the Hospital's net patient service revenue for the year ended September 30, 2016. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The 2017 and 2016 net patient service revenue increased approximately \$3,341,000 and decreased approximately \$66,000, respectively, due to prior year retroactive adjustments in excess of amounts previously estimated and to the addition of allowances estimated that are still subject to audits, reviews and investigations.

The Hospital has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The bases for payment to the Hospital under these agreements include prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

The Hospital qualified for disproportionate share payments from the South Carolina Medicaid Program (the "Program") through September 30, 2017. The Hospital recognized quarterly lump-sum payments totaling approximately \$4,302,000 and \$6,966,000 for the years ended September 30, 2017 and 2016, respectively. These amounts are reflected as a reduction of contractual adjustments. The Program contains a provision requiring the repayment of disproportionate funds received if the participating hospital is determined to be ineligible. The Hospital is also subject to audits performed by the Program and could have repayments due to Program as a result of the

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

audits. The disproportionate share payments are subject to audit by the South Carolina Medicaid Program. In fiscal year 2017 the Medicaid Program completed the audit of the fiscal year 2013 disproportionate share payments and as a result the Hospital received \$115,000 in payments, which was included in estimated third-party payor settlements at September 30, 2017. In fiscal year 2016 the Medicaid Program completed the audit of the fiscal year 2012 disproportionate share payments and as a result the Hospital returned \$285,000 in payments. The Hospital has set aside reserves for future repayments of approximately \$547,000 at September 30, 2017. As a result of the audits it is a reasonable possibility that recorded reserves will change by a material amount in the near term.

HITECH funding for meaningful use of Electronic Health Records (“EHR”)

The Hospital recognizes revenue for incentives earned under the EHR program in the period in which all contingencies related to the payments are complete. Incentive payments received under the EHR program include a discharge-related portion, which is calculated by Centers for Medicare & Medicaid Services (“CMS”) based on the Hospital's most recently filed cost report. Such amounts are subject to adjustment at the time of settling the 12-month cost report for the Hospital's fiscal year that begins after the beginning of the payment year. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The EHR funding received is subject to CMS audit. The results of that audit and settlement could result in a potential payback in future periods. The Hospital achieved compliance with Year 3 meaningful use requirements under the Medicare program during fiscal year 2015 and, accordingly received payments of approximately \$1,170,000 during fiscal year 2016 and \$581,000 during fiscal year 2017. The Hospital achieved compliance with Year 3 meaningful use requirements under the Medicaid program during fiscal year 2014 and, accordingly received payments of approximately \$219,000 during fiscal year 2016, and no payments were received during fiscal year 2017. Under the contingency model, payments received of \$581,000 and \$1,389,000 were recorded in the accompanying statements of net position in estimated third-party payor settlements for the years ended September 30, 2017 and 2016, respectively.

Contractual adjustments related to Medicare and Medicaid programs and other adjustments were deducted from gross patient service charges to arrive at net patient service revenue as follows:

	<u>2017</u>	<u>2016</u>
Gross patient service charges, net of charity care	\$ 1,135,122,672	\$ 1,084,325,931
Deductions:		
Contractual adjustments	(697,879,959)	(670,031,273)
Provision for bad debts	<u>(39,727,322)</u>	<u>(48,098,799)</u>
Net patient service revenue	<u>\$ 397,515,391</u>	<u>\$ 366,195,859</u>

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

5. Accounts Receivable and Accounts Payable

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the Hospital consisted of these amounts at September 30:

Patient Accounts Receivable

	<u>2017</u>	<u>2016</u>
Receivable from patients and their insurance carriers	\$ 71,354,016	\$ 71,970,854
Receivable from Medicare	65,775,555	79,788,631
Receivable from Medicaid	<u>27,574,957</u>	<u>27,790,771</u>
Total patient accounts receivable	<u>164,704,528</u>	179,550,256
Less allowance for contractual adjustments	84,753,151	95,617,587
Less allowance for uncollectible amounts	<u>25,733,046</u>	<u>25,075,207</u>
	<u>110,486,197</u>	120,692,794
Patient accounts receivable, net	<u>\$ 54,218,331</u>	<u>\$ 58,857,462</u>

Accounts payable and accrued expenses

	<u>2017</u>	<u>2016</u>
Payable to suppliers and others	\$ 26,772,628	\$ 25,961,673
Payable to employees (including payroll taxes)	<u>15,345,419</u>	<u>16,361,737</u>
Total accounts payable and accrued expenses	<u>\$ 42,118,047</u>	<u>\$ 42,323,410</u>

6. Capital Assets

Capital asset additions, retirements, transfers, and balances for the years ended September 30 were as follows:

	<u>Balance September 30, 2016</u>	<u>Additions</u>	<u>Retirements</u>	<u>Transfers</u>	<u>Balance September 30, 2017</u>
Land	\$ 5,217,031	\$ 1,170,384	\$ (500,000)	\$ -	\$ 5,887,415
Construction in progress	<u>13,458,455</u>	<u>17,819,426</u>	<u>-</u>	<u>(15,058,871)</u>	<u>16,219,010</u>
	<u>18,675,486</u>	<u>18,989,810</u>	<u>(500,000)</u>	<u>(15,058,871)</u>	<u>22,106,425</u>
Land improvements	5,011,922	4,267	-	-	5,016,189
Buildings and building fixtures	290,062,956	3,765,139	(3,264,064)	7,637,558	298,201,589
Fixed equipment	26,377,295	1,441,855	(897,070)	672,020	27,594,100
Major movable equipment	<u>173,712,367</u>	<u>9,157,660</u>	<u>(5,099,965)</u>	<u>6,749,293</u>	<u>184,519,355</u>
	495,164,540	14,368,921	(9,261,099)	15,058,871	515,331,233
Accumulated depreciation	<u>(293,394,845)</u>	<u>(25,856,378)</u>	<u>7,199,973</u>	<u>-</u>	<u>(312,051,250)</u>
	<u>201,769,695</u>	<u>(11,487,457)</u>	<u>(2,061,126)</u>	<u>15,058,871</u>	<u>203,279,983</u>
Capital assets, net	<u>\$ 220,445,181</u>	<u>\$ 7,502,353</u>	<u>\$ (2,561,126)</u>	<u>\$ -</u>	<u>\$ 225,386,408</u>

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

	<u>Balance September 30, 2015</u>	<u>Additions</u>	<u>Retirements</u>	<u>Transfers</u>	<u>Balance September 30, 2016</u>
Land	\$ 4,695,565	\$ 521,466	\$ -	\$ -	\$ 5,217,031
Construction in progress	<u>2,963,781</u>	<u>13,512,809</u>	<u>-</u>	<u>(3,018,135)</u>	<u>13,458,455</u>
	<u>7,659,346</u>	<u>14,034,275</u>	<u>-</u>	<u>(3,018,135)</u>	<u>18,675,486</u>
Land improvements	5,012,560	20,136	(26,149)	5,375	5,011,922
Buildings and building fixtures	284,530,663	10,059,305	(6,992,021)	2,465,009	290,062,956
Fixed equipment	24,251,744	2,197,322	(129,808)	58,037	26,377,295
Major movable equipment	<u>168,687,807</u>	<u>6,917,795</u>	<u>(2,382,949)</u>	<u>489,714</u>	<u>173,712,367</u>
	482,482,774	19,194,558	(9,530,927)	3,018,135	495,164,540
Accumulated depreciation	<u>(273,376,685)</u>	<u>(26,538,239)</u>	<u>6,520,079</u>	<u>-</u>	<u>(293,394,845)</u>
	<u>209,106,089</u>	<u>(7,343,681)</u>	<u>(3,010,848)</u>	<u>3,018,135</u>	<u>201,769,695</u>
Capital assets, net	<u>\$ 216,765,435</u>	<u>\$ 6,690,594</u>	<u>\$ (3,010,848)</u>	<u>\$ -</u>	<u>\$ 220,445,181</u>

At September 30, 2017, construction in progress includes costs related to various construction projects and the implementation of an electronic medical records system. The Hospital has entered into various contracts related to these projects which amount to approximately \$41,529,000. As of September 30, 2017, approximately \$14,397,000 remains payable of these contracts.

7. Long-Term Debt

A schedule of changes in the Hospital's long-term debt for 2017 and 2016 follows:

	<u>Balance September 30, 2016</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2017</u>	<u>Amounts Due Within One Year</u>
Hospital Facilities Revenue Bonds – Series 2012 A1	\$ 25,000,000	\$ -	\$ -	\$ 25,000,000	\$ -
Hospital Facilities Revenue Bonds – Series 2012 A2	14,000,000	-	-	14,000,000	500,000
Hospital Facilities Revenue Bonds – Series 2012 B	53,595,000	-	(715,000)	52,880,000	745,000
Hospital Facilities Revenue Bonds – Series 2009	50,000,000	-	-	50,000,000	-
Hospital Facilities Revenue Bonds – Series 2004 B	<u>25,000,000</u>	<u>-</u>	<u>(25,000,000)</u>	<u>-</u>	<u>-</u>
	167,595,000	-	(25,715,000)	141,880,000	1,245,000
Plus/less discount/premium	<u>3,522,579</u>	<u>-</u>	<u>(792,126)</u>	<u>2,730,453</u>	<u>-</u>
	171,117,579	-	(26,507,126)	144,610,453	1,245,000
Notes payable to banks - The Surgery Center	1,505,016	-	(101,584)	1,403,432	122,774
Capital lease obligations	<u>293,222</u>	<u>2,187</u>	<u>(196,191)</u>	<u>99,218</u>	<u>36,185</u>
	<u>\$ 172,915,817</u>	<u>\$ 2,187</u>	<u>\$ (26,804,901)</u>	<u>\$ 146,113,103</u>	<u>\$ 1,403,959</u>

**Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements**

	<u>Balance September 30, 2015</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2016</u>	<u>Amounts Due Within One Year</u>
Hospital Facilities Revenue Bonds – Series 2012 A1	\$ 25,000,000	\$ -	\$ -	\$ 25,000,000	\$ -
Hospital Facilities Revenue Bonds – Series 2012 A2	14,500,000	-	(500,000)	14,000,000	-
Hospital Facilities Revenue Bonds – Series 2012 B	54,285,000	-	(690,000)	53,595,000	715,000
Hospital Facilities Revenue Bonds – Series 2009	50,000,000	-	-	50,000,000	-
Hospital Facilities Revenue Bonds – Series 2004 B	<u>25,000,000</u>	<u>-</u>	<u>-</u>	<u>25,000,000</u>	<u>-</u>
	168,785,000	-	(1,190,000)	167,595,000	715,000
Plus/less discount/premium	<u>3,894,196</u>	<u>-</u>	<u>(371,617)</u>	<u>3,522,579</u>	<u>-</u>
715,000	172,679,196	171,117,579	-	(1,561,617)	171,117,579
Notes payable to banks - The Surgery Center	1,598,665	-	(93,649)	1,505,016	89,000
Note payable – Foundation	71,725	-	(71,725)	-	-
Capital lease obligations	<u>484,774</u>	<u>-</u>	<u>(191,552)</u>	<u>293,222</u>	<u>242,232</u>
	<u>\$ 174,834,360</u>	<u>\$ -</u>	<u>\$ (1,918,543)</u>	<u>\$ 172,915,817</u>	<u>\$ 1,046,232</u>

Hospital Facilities Revenue Bonds - Series 2012A, were issued by Greenwood County, South Carolina, on May 11, 2012 to be used for the following projects (a) the acquisition, construction, renovation, improvement, and equipping of: support services building, data center, service center AHU, health education, west tower, east tower, old main demolition, old main 1st and 2nd floor, pharmacy, lab, and cafeteria (b) pay certain costs of issuance of the Series 2012A Bonds and (c) to fund interest during the construction of the project. The Series 2012 A include \$25,000,000 Series 2012A-1 variable rate and \$15,000,000 Series 2012A-2 fixed rate bonds. The Series 2012A-1 variable rate bonds bear interest at the monthly British Bankers Association LIBOR rate ("LIBOR"). The Series 2012A-2 fixed rate bonds bear interest at 2.578%. Interest is paid monthly. The Series 2012A-1 variable rate bonds have principal requirements ranging from \$750,000 to \$7,025,000 due October 1, 2032 through October 1, 2042. The Series 2012A-2 fixed rate bonds have principal requirements ranging from \$500,000 to \$2,000,000 due October 1, 2017 through October 1, 2032. A Trust Agreement names a bank as Trustee to receive, transfer and disburse all monies. The agreement contains certain restrictive covenants which, among other matters, require the Hospital to maintain its rates, fees and charges to the extent necessary in order for the Hospital to maintain certain earnings levels, as defined in the Trust Agreement. The Series 2012A bonds are limited obligations of Greenwood County payable solely from and secured by revenues of the Hospital, as defined in the Trust Agreement, and certain funds and accounts held under the Trust Agreement. Payment of the obligations is also secured by a mortgage on the land on which the Hospital's main and related support facilities stand.

A financial institution directly purchased the Series 2012A Bonds from Greenwood County. The financial institution advanced the principal amount of the 2012A Bonds to the Hospital, and the advances were used to pay for the project. The Hospital pays interest on the advanced principal amounts on the first day of each month, until the Series 2012A Bonds have been paid in full. The initial mandatory purchase date from the financial institution is May 1, 2022.

Hospital Facilities Revenue Bonds - Series 2012B, were issued by Greenwood County, South Carolina, on April 24, 2012 to be used to pay for (a) refunding the outstanding principal amount of the Series 1998A Bonds (b) refunding the outstanding principal amount of the Series 2001 bonds and (c) certain costs of issuance of the Series 2012B Bonds. The Series 2012B Bonds include term bonds with principal requirements ranging from \$745,000 to \$5,645,000 due October 1, 2017 through October 1, 2032. The Series 2012B bonds bear interest at varying rates from 2% to 5%. Interest is paid semi-annually. The 2012B Bonds are subject to mandatory sinking fund redemption

Self Regional Healthcare and Affiliates Notes to Combined Financial Statements

beginning October 1, 2028, through October 1, 2031, with principal requirements ranging from \$200,000 through \$5,645,000. A Trust Agreement names a bank as Trustee to receive, transfer and disburse all monies. The agreement contains certain restrictive covenants which, among other matters, require the Hospital to maintain its rates, fees and charges to the extent necessary in order for the Hospital to maintain certain earnings levels, as defined in the Trust Agreement. The Series 2012B bonds are limited obligations of Greenwood County payable solely from and secured by revenues of the Hospital, as defined in the Trust Agreement, and certain funds and accounts held under the Trust Agreement. Payment of the obligations is also secured by a mortgage on the land on which the Hospital's main and related support facilities stand.

Hospital Facilities Revenue Bonds - Series 2009, were issued by Greenwood County, South Carolina, on September 29, 2009 to be used for (a) construction of the Cancer Center and (b) reimbursement to the Hospital for routine capital items acquired during fiscal years 2008 and through September 2009. The Series 2009 Bonds include term bonds with principal requirements ranging from \$315,000 to \$10,360,000 due October 1, 2019 through October 1, 2040. The Series 2009 bonds bear interest at varying rates from 4.375% to 5.375%. Interest is paid annually. The 2009 Bonds are subject to mandatory sinking fund redemption beginning October 1, 2033, through October 1, 2040, with principal requirements ranging from \$190,000 through \$10,360,000. A Trust Agreement names a bank as Trustee to receive, transfer and disburse all monies. The agreement contains certain restrictive covenants which, among other matters, require the Hospital to maintain its rates, fees and charges to the extent necessary in order for the Hospital to maintain certain earnings levels, as defined in the Trust Agreement. The Series 2009 bonds are limited obligations of Greenwood County payable solely from and secured by revenues of the Hospital, as defined in the Trust Agreement, and certain funds and accounts held under the Trust Agreement. Payment of the obligations is also secured by a mortgage on the land on which the Hospital's main and related support facilities stand.

Hospital Facilities Revenue Bonds - Series 2004 B, were issued by Greenwood County, South Carolina, on February 4, 2004, to be used in connection with the advance refunding of the Series 1993 Bonds and to assist in the construction of a new patient tower facility. The 2004 B Bonds are Auction Rate Hospital Revenue Bonds subject to mandatory sinking fund redemption beginning October 1, 2018, through October 1, 2034, with principal requirements ranging from \$190,000 through \$7,565,000. The Series 2004 B bonds bear interest at varying rates from .399% to .620%. Interest on the Series 2004 Bonds are paid semi-annually. A Trust Agreement names a bank as Trustee to receive, transfer and disburse all monies. The agreement contains certain restrictive covenants which, among other matters, require the Hospital to maintain its rates, fees and charges to the extent necessary in order for the Hospital to maintain certain earnings levels, as defined in the Trust Agreement. The Series 2004 B bonds are limited obligations of Greenwood County payable solely from and secured by revenues of the Hospital, as defined in the Trust Agreement, and certain funds and accounts held under the Trust Agreement. Payment of the obligations is also secured by a mortgage on the land on which the Hospital's main and related support facilities stand. The Series 2004B bonds were issued as variable rate bonds secured by municipal bond insurance. The municipal bond insurance would be placed into effect if the Remarketing Agents are unable to resell, under a "best efforts" arrangement, bonds that are tendered. The municipal bond insurance would make payments under the terms of the Bonds. The Series 2004B bonds were paid off during 2017.

The notes payable to banks consist of two notes, the Building note and the Equipment note. The Building note for \$2,350,000 was executed to finance construction for the Surgery Center. The note is payable over 25 years, ending September 2026. Interest for the building note is payable monthly based on a rate equal to the monthly LIBOR Index, as defined in the credit agreement, plus 150 basis points.

The Foundation had an outstanding note payable collateralized by a deed of trust on certain real estate. The note is payable over 10 years ending August 2016 with an original principal amount of \$600,000. Principal and interest at a rate of 6.24% are payable at \$6,762 monthly. In August 2008, the Foundation obtained an additional note payable collateralized by a deed of trust on certain real estate. Principal and interest at a rate of 6.40% are payable at \$4,304 monthly. The note was paid off during fiscal year 2016.

The 2012B, 2009, and 2004B Series bonds are reported net of premium (discount) on bonds payable at September 30, 2017 and 2016 of approximately \$2,730,000 and \$3,523,000, respectively.

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

Future principal and interest payments, excluding unamortized discount and premium, under the Hospital's long-term debt agreements less capital lease obligations are as follows for the year ending September 30, 2017:

	<u>Principal Payments</u>	<u>Interest Payments</u>
2018	\$ 1,367,774	\$ 5,236,375
2019	3,794,526	5,149,334
2020	3,949,652	5,014,981
2021	4,085,636	4,873,644
2022	4,277,552	4,725,763
2023 – 2027	25,058,292	20,862,286
2028 – 2032	26,000,000	15,049,065
2033 – 2037	28,220,000	11,734,431
2038 – 2042	39,505,000	2,433,531
2043	<u>7,025,000</u>	<u>-</u>
	<u>\$ 143,283,432</u>	<u>\$ 75,079,410</u>

8. Employee Pension Plans

Plan description

The Pension Plan (the "Plan") is a single-employer defined benefit pension plan, which provides for retirement, death, and disability benefits to Plan participants and beneficiaries. The Hospital reserves the right to amend the Plan at any time. Generally, the Pension Benefit Guaranty Corporation reserves the right to terminate the Plan if the Hospital fails to meet the minimum funding standards, or is unable to pay benefits when due. If the Plan is terminated, the Plan assets will be distributed among the Plan participants based upon a priority allocation procedure. The Hospital shall be liable for any unfunded vested benefits to the extent required by law.

Effective September 30, 2009, the Hospital chose to freeze the Plan. Active employees as of September 30, 2009 were eligible to participate in the Plan, and any employees hired subsequent to September 30, 2009 were not eligible to participate in the Plan.

Pension benefits

Pension benefits are provided to participants under several types of retirement options based upon years of service and age. Retirement benefits are paid to pensioners or beneficiaries in various forms of joint and survivor payment options, including a lump-sum payment.

Death and disability benefits

In the event of a vested employee's death, his or her designated beneficiary will be entitled to receive a survivor benefit equal to 50% of the participant's accrued benefit, according to the Plan provisions. The survivor benefit commences on the earliest date that the deceased participant could have elected to receive retirement benefits. If a participant becomes disabled, he or she may elect disability retirement. The disability retirement payment commences in the month coincident with or following the disability retirement date.

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

Employees covered by benefit terms

At the September 30, 2017 and 2016 measurement dates, the following employees were covered by the benefit terms:

	<u>2017</u>	<u>2016</u>
Active employees	812	889
Inactive employees or beneficiaries currently receiving benefits	377	356
Inactive employees entitled to but not yet receiving benefits	<u>369</u>	<u>366</u>
	<u><u>1,558</u></u>	<u><u>1,611</u></u>

Contributions

Contributions to provide benefits under the Plan are made solely by the Hospital. The entire cost of the Plan is borne by the Hospital. Plan members are not required to contribute to the Plan. The Hospital contributes at an actuarially determined rate. The Hospital contributed approximately \$3,700,000 and \$3,000,000 to the Plan for the Hospital's fiscal years ended September 30, 2017 and 2016, respectively.

Net pension liability

The most recent annual actuarial valuation reports are as of October 1, 2016. The net pension liability of each defined benefit pension plan was therefore determined based on the October 1, 2016 actuarial valuations, using membership data as of October 1, 2016, and financial information of the pension funds as of October 1, 2016, using generally accepted actuarial procedures. Information included in the following schedules is based on the certification provided by the Hospital's consulting actuary.

For the years ended September 30, 2017 and 2016, the Hospital recognized pension expense of approximately \$834,000 and \$1,674,000.

The following represents the changes in the net pension liability as of September 30:

	<u>Total Pension Liability (a)</u>	<u>Plan Fiduciary Net Position (b)</u>	<u>Net Pension Liability (a)-(b)</u>
Balances at September 30, 2016	\$ 89,123,262	\$ 66,838,314	\$ 22,284,948
Changes for the year:			
Interest	5,196,798	-	5,196,798
Differences between expected and actual experiences	690,820	-	690,820
Contributions - employer	-	3,700,000	(3,700,000)
Net investment income	-	8,492,324	(8,492,324)
Benefits paid	(5,019,936)	(5,019,936)	-
Administrative expenses	-	(229,819)	229,819
Net changes	<u>867,682</u>	<u>6,942,569</u>	<u>(6,074,887)</u>
Balances at September 30, 2017	<u>\$ 89,990,944</u>	<u>\$ 73,780,883</u>	<u>\$ 16,210,061</u>

**Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements**

Sensitivity analysis

The following represents the sensitivity of the total pension liability and the net pension liability to changes in the interest rate based on values as of September 30, 2017:

	<u>1% Decrease 5.00%</u>	<u>Current Rate 6.00%</u>	<u>1% Increase 7.00%</u>
Net pension liability	\$ 26,203,617	\$16,210,061	\$ 7,859,190

Actuarial assumptions and methods

Actuarial valuations involve estimates of the reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and future salary increases. Amounts determined during the valuation process are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The total pension liability in the October 1, 2016 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Discount rate	6.0%
Future Salary Increase	4.0%
Expected return on plan assets	6.0%
Mortality	RP-2000 Combined Healthy (Blue Collar) Male and Female Tables projected seven years

The discount rate adopted by the Hospital for valuing Plan liabilities was determined by the methods prescribed under GASB 68 which requires the use of a long term rate of return on Plan assets, unless a projection of the net fiduciary position will not be sufficient to provide for projected benefit payments of the covered current and former employees.

The projected return on Plan assets and inflation assumptions are developed through review of current and historical capital markets data and historical performance of investment strategies. These projections are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

The target allocation and best estimates of arithmetic real rates of return for each major asset class as of the October 1, 2016 valuation date are summarized in the following table:

	<u>Target Asset Allocation</u>	<u>Expected Arithmetic Real Rate of Return</u>
Bonds	33.5%	3.1%
Equities	65.0%	8.2%
Cash	<u>1.5%</u>	1.1%
	<u>100.0%</u>	

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

Deferred inflows and outflows of resources related to pensions

At September 30, 2017, the Hospital reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference between expected and actual experience	\$ 532,846	\$ (524,536)
Changes of assumptions	-	(2,647,639)
Difference between expected and actual return on plan assets	<u>1,898,768</u>	<u>(4,047,806)</u>
	<u>\$ 2,431,614</u>	<u>\$ (7,219,981)</u>

The amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense for the year ended September 30, 2017 as follows:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
2018	\$ 1,107,358	\$ (1,728,870)
2019	1,107,358	(1,556,079)
2020	157,974	(1,556,079)
2021	58,924	(1,397,190)
2022	-	(489,903)
Thereafter	<u>-</u>	<u>(491,860)</u>
	<u>\$ 2,431,614</u>	<u>\$ (7,219,981)</u>

Defined contribution plan

The Hospital has a 403b defined contribution plan (the “contribution plan”) covering substantially all its employees. The contribution plan is employee and employer contributory. The Hospital contributed a match based on 100% of the first 3% of the employee’s elected deferral percentage calculated on the employee’s base compensation. The Hospital can also contribute a discretionary amount determined annually by the Board of Trustees. Defined contribution expense amounted to approximately \$4,033,000 and \$3,532,000 for 2017 and 2016, respectively.

9. Other Postemployment Benefit (“OPEB”)

Plan description

The Hospital offers certain postretirement benefits to employees and their spouses including health and dental insurance until age 65, life insurance coverage until age 65, and a percentage of the employee’s basic salary until age 62 for all employees who are at least age 55 and have 30 years of service with the Hospital. The Hospital has elected to partially pay the future overall cost of coverage for these benefits. The Hospital chose to freeze the salary continuation portion of the Plan effective September 30, 2010.

As of September 30, 2016, the date of the latest actuarial valuation, there were 1,292 total members of the OPEB that consisted of 1,246 active members, 46 retirees and spouses of retirees.

**Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements**

Funding policy

The Hospital has chosen to fund the healthcare benefits on a pay as you go basis.

The annual required contribution (“ARC”) rate for September 30, 2017 and 2016 for healthcare benefits is 1.0% and 1.2%, respectively, of annual covered payroll. For the year ended September 30, 2017, the Hospital contributed approximately \$730,000 for other postretirement benefits payments that represents 1.0% of covered payroll. For the year ended September 30, 2016, the Hospital contributed approximately \$926,000 for other postretirement benefits payments that represents 1.3% of covered payroll. There were no contributions made by employees.

Annual OPEB cost and net OPEB obligation

The Hospital’s annual OPEB cost (expense) is calculated based on the ARC of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

The Hospital’s annual OPEB cost for the year, the amount actually contributed to the OPEB, and changes in the Hospital’s net OPEB obligation for the healthcare benefits and retiree salaries were as follows:

	<u>2017</u>	<u>2016</u>
Annual required contribution for healthcare benefits	\$ 778,804	\$ 889,268
Interest on net OPEB obligation	204,899	196,208
Adjustment to ARC	<u>(253,884)</u>	<u>(159,730)</u>
Annual OPEB costs	729,819	925,746
Contributions made	<u>(729,819)</u>	<u>(925,746)</u>
Change in net OPEB obligation	-	-
OPEB obligation, beginning of year	<u>2,912,194</u>	<u>2,912,194</u>
OPEB obligation, end of year	<u>\$ 2,912,194</u>	<u>\$ 2,912,194</u>

The Hospital’s annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the OPEB obligation were as follows:

<u>Fiscal Year Ending</u>	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net OPEB Obligation</u>
September 30, 2017	\$ 729,819	100.00%	\$ 2,912,194
September 30, 2016	\$ 925,746	100.00%	\$ 2,912,194
September 30, 2015	\$ 1,264,261	113.18%	\$ 2,912,194

Funded status and funding progress

As of September 30, 2016, the most recent actuarial valuation date, the OPEB was not funded. The actuarially accrued liability for benefits and, thus, the unfunded actuarially accrued liability (“UAAL”) was \$7,028,000. The covered payroll (annual payroll of active employees covered by the plan) was approximately \$74,917,000, and the ratio of the UAAL to the covered payroll was 9 percent. Actuarial valuations of an ongoing plan involve estimates of the value of the reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and healthcare trends. Amounts determined regarding the funded status of the OPEB and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Self Regional Healthcare and Affiliates Notes to Combined Financial Statements

Actuarial methods and assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members at that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarially accrued liabilities and the actuarial value assets, consistent with the long-term perspective of the calculations.

In the September 30, 2016 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions for 2016 included (a) 5.0% discount rate, (b) an annual medical cost trend of 9.0%, and (c) an annual dental cost trend of 5.0%.

10. Commitments and Contingencies

Operating leases

The Hospital leases various equipment and facilities under operating leases expiring at various dates through 2020. Total rental expense in 2017 and 2016 for all operating leases was approximately \$1,053,000 and \$1,091,000, respectively.

Minimum annual lease payments for years subsequent to September 30, 2017 are as follows:

2018	\$	399,284
2019		340,538
2020		<u>151,794</u>
	\$	<u>891,616</u>

Professional malpractice liability insurance

The Hospital participates in a multiprovider captive insurance company for professional and general liability insurance coverage on a claims made basis. Liabilities are joint and several among participating providers. The aggregate limit under insurance coverage is \$12,000,000. The Hospital's premiums are accrued based on the experience to date of the participating health care providers.

In addition, the Hospital has an unsecured letter of credit related to malpractice claims with a financial institution for approximately \$1,000,000. The letter of credit expires on December 1, 2018.

Malpractice claims have been asserted against the Hospital by various claimants, and additional claims could be asserted for incidents occurring through September 30, 2017. At September 30, 2017, management is aware of no incidents that might lead to significant claims that are not adequately covered by insurance through the captive insurance company that would have a material adverse effect on the combined financial position of the Hospital. Accordingly, no provision has been made in the accompanying combined financial statements for any such claims.

Litigation

The Hospital is involved in litigation and regulatory investigations arising in the normal course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Hospital's future combined financial position or combined results from operations.

Industry

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government

Self Regional Healthcare and Affiliates
Notes to Combined Financial Statements

health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulation by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services billed.

11. Net Position Restricted by Donor

Net position restricted by donor at September 30 consists of the following:

	<u>2017</u>	<u>2016</u>
Access Health Lakelands	\$ 140,951	\$ 126,005
Benjamin Parker Pediatric Fund	96,128	97,824
Blackwell Scholarship Fund	68,798	59,687
Cancer Fund	299,835	257,959
Capital Campaign Fund	794,424	809,604
Chaplain/Pastoral Fund	17,668	18,863
Diabetes Fund	98,202	82,703
Donated Artwork	11,525	11,525
Duke – Childhood Obesity (WWKF)	5,141	5,141
Duke – Tobacco Cessation Program	363	364
Elizabeth May Fund	100,531	90,022
GCMA Scholarship Fund	13,893	14,891
Grace Fund	81,340	93,590
Heydel Respiratory Therapy Scholarship Fund	67,648	62,222
J. Smith Cardiac Rehab	93,042	87,735
Lakelands Rural Health Net	510	510
May-Magruder Lab Scholarship Fund	153,969	137,644
ME Ruff Scholarship Fund	110,058	102,825
Medical Library Fund	30,236	26,930
Medical Museum Fund	40,043	35,665
NM Thurmond Memorial Fund	134,379	97,242
Nursing Education Fund	56,903	55,111
OR Equipment Fund	37,783	33,652
Other	384,509	370,480
Pulmonary Rehab Fund	8,325	7,416
Radiology	2,695	2,400
SAFE Kids Fund	76,569	68,294
Spoone Scholarship Fund	3,718	3,764
Vascular Excellence Fund	177,296	157,913
William Barnette	188,351	167,758
Women’s Health	173,547	106,211
	<u>\$ 3,468,380</u>	<u>\$ 3,191,950</u>
Donor restricted net position	<u>\$ 3,468,380</u>	<u>\$ 3,191,950</u>

12. Subsequent Events

Series 2017 Bond Issuance

Hospital Facilities Refunding Revenue Bonds - Series 2017, were issued by Greenwood County, South Carolina, in October 2017 to be used to pay for refunding the outstanding principal amount of the Series 2009 Bonds and certain costs of issuance of the Series 2017 Bonds. The Series 2017 Bonds include term bonds with principal requirements ranging from \$475,000 to \$9,640,000 due October 1, 2019 through October 1, 2040. The Series 2017 bonds bear interest at varying rates from 2% to 5%. Interest is paid semi-annually. The Series 2017 bonds are limited obligations of Greenwood County payable solely from and secured by revenues of the Hospital, as defined in the Trust Agreement, and certain funds and accounts held under the Trust Agreement. Payment of the obligations is also secured by a mortgage on the land on which the Hospital's main and related support facilities stand.

Subsequent events have been evaluated through December 18, 2017, which is the date the combined financial statements were issued.

Required Supplementary Information

Self Regional Healthcare and Affiliates
Schedules of Required Supplementary Information
Schedules of Changes in Net Pension Liability and Related Ratios

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Total pension liability				
Interest	\$ 5,196,798	\$ 5,208,700	\$ 5,192,103	\$ 5,497,280
Differences between expected and actual experience	690,820	(382,692)	-	(489,428)
Assumption changes	-	-	-	(4,411,559)
Benefits paid	<u>(5,019,936)</u>	<u>(5,028,831)</u>	<u>(4,802,142)</u>	<u>(5,190,506)</u>
Net change in total pension liability	867,682	(202,823)	389,961	(4,594,213)
Total pension liability - beginning	89,123,262	89,326,085	88,936,124	93,530,337
Total pension liability - ending (a)	\$ 89,990,944	\$ 89,123,262	\$ 89,326,085	\$ 88,936,124
Plan fiduciary net position				
Contributions - employer	\$ 3,700,000	\$ 3,000,000	\$ 3,000,000	\$ 3,000,000
Net investment income (loss)	8,492,324	4,255,360	(755,628)	4,742,173
Benefits paid	(5,019,936)	(5,028,831)	(4,802,142)	(5,190,506)
Administrative expenses	<u>(229,819)</u>	<u>(166,506)</u>	<u>(86,549)</u>	<u>(175,029)</u>
Net change in plan fiduciary net position	6,942,569	2,060,023	(2,644,319)	2,376,638
Total plan fiduciary net position - beginning	66,838,314	64,778,291	67,422,610	65,045,972
Total plan fiduciary net position - ending (b)	\$ 73,780,883	\$ 66,838,314	\$ 64,778,291	\$ 67,422,610
Net pension liability - ending (a) - (b)	\$ 16,210,061	\$ 22,284,948	\$ 24,547,794	\$ 21,513,514
Plan fiduciary net position as a percentage of the total pension liability	81.99%	75.00%	72.52%	75.81%
Covered-employee payroll	\$ 51,284,158	\$ 54,340,899	\$ 62,349,985	\$ 62,349,985
Net pension liability as a percentage of covered-employee payroll	31.61%	41.01%	39.37%	34.50%

See independent auditors' report.

Self Regional Healthcare and Affiliates
Schedules of Required Supplementary Information
Schedules of Contributions

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Actuarially determined contribution	\$ 1,648,102	\$ 1,566,597	\$ 1,665,989	\$ 2,133,949
Contributions in relation to the actuarially determined contribution	<u>3,700,000</u>	<u>3,000,000</u>	<u>3,000,000</u>	<u>3,000,000</u>
Contribution excess	<u>\$ (2,051,898)</u>	<u>\$ (1,433,403)</u>	<u>\$ (1,334,011)</u>	<u>\$ (866,051)</u>
Covered-employee payroll	51,284,158	54,340,899	62,349,985	62,349,985
Contributions as a percentage of covered-employee payroll	7.21%	5.52%	4.81%	4.81%

Notes to Schedule

Measurement date	September 30, 2017
Valuation date	October 1, 2016
Salary increases	N/A, plan frozen in 2009
Discount rate	6.00%
Expected rate of return on plan assets	6.00%
Inflation Rate	2.5%
Mortality	RP-2000 Combined Healthy (Blue Collar) Male and Female Tables projected seven years

See independent auditors' report.